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[GARAMENDI: BROKER COMPENSATION DISCLOSURE REGULATIONS--PIA STORY AND ANALYSIS](#)

**Garamendi: broker compensation disclosure regulations--PIA story and analysis**

**Garamendi unloads—California gets new disclosure regulations**

California Insurance Commissioner John Garamendi is going to implement new broker disclosure compensation rules. He made the announcement in a news release late Wednesday afternoon.

The entire text of the new disclosure rules can be viewed at this link.  
[http://www.insurancejournal.com/pdf/Broker\\_Fiduciary\\_Regulations\\_Text.pdf](http://www.insurancejournal.com/pdf/Broker_Fiduciary_Regulations_Text.pdf).

The Department of Insurance issued a 15-day notice and invited public comment on the changes to the proposed broker fiduciary duty regulations. Any written comments on the revisions must be received no later than 5 p.m. on May 2, 2005.

The proposed regulations will:

- Require the agent or broker to advise a client, prior to signing an agreement or receiving a fee, whether the producer will seek a quote from one insurer or more than one insurer.
- Require the agent or broker to reveal if he or she is acting on behalf of the insurer or the client in connection with the placement of insurance. A producer who accepts a fee from a client is conclusively deemed to be acting on behalf of the client.
- Require the agent or broker to reveal the amount of compensation he or she will receive if the client purchases insurance with any insurer recommended by the agent or broker. If the amount of compensation cannot reasonably be known at the time this disclosure is made, the producer may disclose the method by which any such compensation will or may be calculated.
- A broker or agent acting on behalf of the client, or who accepts a fee from the client, may not accept any compensation from a third party for the transaction done on behalf of the client without first obtaining the consent of the client.
- A broker or agent who has told a client that he or she will search for the best quote on a policy must reveal the number of quotes obtained, the name of the insurer, the premium amount, and other required information.

Leonard Freeman has an agency in Orange, California and is on the board of directors of the PIA group. It represents California for PIA. He's also on the newly formed PIA Western Alliance board of directors.

Freeman analyzed the new regulations and said he had problems with bullet point three above where agents and brokers have to disclose to customers the amount commission they make before writing a policy.

"Every time you go to Wal-Mart or any store to buy something, are they required to tell you their profit? Do they volunteer to tell you their profit? I don't think so. Some businesses like attorneys, CPAs or auto mechanics will tell you their hourly rate but that's not giving you the total details of what they make. Insurance agents and brokers should not have to do this either. This is not a reasonable thing for us to have to divulge to a client. If they don't like the price they hear, they will shop around."

And Freeman says what Garamendi and others pushing for this type of reform don't realize is that the consumer understands commissions are involved and they don't care.

"Commissions have been the method of compensation for agents in the 41 years I've been in business. Our clients know that. I can't remember one time in 41 years where a client has asked me how much I make. No one asks."

He also wonders about the wisdom of putting in a requirement that agents give consumers the number of quotes obtained, the name of the insurer, the premium amount, and other required information. Freeman thinks it's unnecessary.

"Most agents and brokers are already doing that. I won't say they all are but most do. We give our clients quotes from three or four or five companies. It's competitive out there now. You have to show your clients quotes in order to be competitive. If you don't they'll go somewhere else and find the price they're looking for."

Freeman was quite critical of Garamendi and others attempting to reform the industry. He—like many other agents and brokers—does not like being lumped in with those who have broken the law.

"I'm working hard on behalf of my clients. It's how I stay in business. What Garamendi and the others don't realize is that the system they're trying to reform actually gives consumers a good deal. The companies share their success and profits with agents and with consumers in the form of lower rates."

### **PIA Analysis**

The beginning of the news release is ominous: "The Commissioner's investigation of the industry has revealed bid-rigging and widespread "steering" of clients to insurers by the very brokers and agents who are supposed to act in the best interest of the client."

The Commissioner's investigation of broker practices started in early 2004. Then last November he filed suit against Universal Life Resources of San Diego and four major insurers: MetLife, Cigna Corporation, Prudential Financial and UnumProvident Corporation.

His complaint charged the defendants with violating state law by withholding information from clients about the "secret" deals struck between the insurers and Universal Life Resources. Garamendi's news release gave some details but few specifics, "ULR would steer clients to the four insurers in order to satisfy secret financial arrangements, regardless of whether the insurance products were the best available, or the best priced. ULR settled the case with the Department and agreed to end the practices."

**Industry News** sent a copy of Garamendi's press release to PIA National Senior Vice President Pat Borowski. She's one of the nation's leading experts on this issue. Borowski was stunned.

"Where does the California Department of Insurance keep coming up with the term 'secret' compensation deals? We certainly can't speak to the specific insurers and their specific arrangements with Universal Life Resources but ALL insurers are required to do two things. One they either file specific rates and/or have their rate filing information available for ALL DOIs and two, each year they file an annual statement with ALL states in which they conduct business."

Those filings are standardized. "In both NAIC filing standards and the centralized annual statement filing system used by ALL insurers and ALL DOIs insurers are required to specifically list their marketing/production/producer costs. ALL monies paid to insurance producers whether just commissions or additional contingency monies are listed there. Further, rate filings require similar and even more detailed breakout of these costs. It is ALL there and has always been there. So what do they mean by 'secret?'"

Borowski says it can only be "secret" if one or more of four things is happening:

- First, no one in the department of insurance took the time to learn what all the data reporting lines and numbers actually mean in the carriers' filings and how they operate in the marketplace.

"If this is the case, shame on the California DOI," Borowski said.

- Second, if ULR and these carriers did some truly special side deal that was not accounted for as per filing requirements OR misreported to "hide" it from appearing as producer compensation or whatever, then THEY

violated the law.

“Punish them but don’t make them a symbol for everyone else.”

- Third, misreporting might have been happening on any 5500 filing.

Borowski said, “Again, punish them and don’t make them a symbol of all of us.”

- Fourth, if ULR acted in a manner that clearly brought into question their own legal compliance with what the California law expects them to do to keep their responsibilities to the insured-customers, insurer and themselves in proper order of obligations.

If they acted in that manner, they broke the law, and as Borowski stated with the other points, punish ULR, not independent insurance agents.

**Industry News** has covered the agent/broker compensation issue for months. We dispute Garamendi’s use of the term “widespread” in reference to the issue that led to the implementation of these regulations. The problem is at a level much higher than independent insurance agents and brokers. Garamendi’s statements imply that the entire industry is into illegal activities that line pockets with bundles of loot while ignoring the needs of the client.

Nothing could be farther from the truth.

Garamendi and the California Department of Insurance know this. Organizations representing independent agents—including PIA National and the PIA Western Alliance—have told them that current California law caught this problem and dealt with the offenders. The law works and new regulations aren’t necessary. Agents operating small businesses are not the culprits.

Garamendi and his staff didn’t listen. Neither did the National Association of Insurance Commissioners who—when they passed their own draconian amendments to the Producer Licensing Model Act last December became the inspiration for new California regs.

The news release went on to say, “Continuing his fight against harmful secret commissions paid to brokers and agents by the insurers whose products they sell, Insurance Commissioner John Garamendi announced new regulations Wednesday to provide strong, clear guidelines that ensure consumers know whether they’re getting the best deal for the best price.”

He also said these regulations are all about making it clear that brokers and agents working as brokers must put the interest of the client first and not their own financial gain.

Most agents and brokers already do that. It’s how they built their businesses and get repeat business. This is a deliberate slam of independent agents and brokers in the state of California who are honest business people and already obey the law.

In a direct quote, the Commissioner said, “Despite the industry’s opposition to comply with the most basic of disclosure proposals, I will continue my work to ensure that consumers aren’t duped into buying something that isn’t the best product for their needs or the best value for their dollar.”

Continuing that work means a bill now in the California legislature’s Senate Banking, Finance and Insurance committee. It was introduced on Garamendi’s behalf by Democratic Senator Joseph Dunn. Senate bill 938 is designed to give the DOI the power to “clarify existing rules on the obligations that brokers and agents have regarding clients. It would impose specified requirements on an agent or broker acting on behalf of a client with respect to how they make inquiries of insurers, obtain coverage, disclose information to the client, and charge fees to the client.”

Again, these are unnecessary regulations that will cause hardship on independent insurance agents. PIA

National's Borowski said, "With these regulations the need for the bill becomes even more moot."

What Garamendi, Eliot Spitzer and others doing battle with mega-corporations on behalf of consumers miss is that they are "fixing" problems that current laws already address. Their efforts to solve illegal activities at these companies are going to drive many small businesses out of business.

None of the corporations Garamendi cited in his news release as conducting illegal activities will suffer serious financial repercussions by the implementation of these regulations. And as PIA Circle of Professionals financial expert Larry Morrison states in another story in this issue, the companies settling with Spitzer and the state of New York and insurance departments in various states have enough resources to work their way through what most see as an inconvenience.

This is not the case with small businesses like independent insurance agencies. The overly broad, ill-conceived, knee jerk reaction of politicians—and yes, he is a politician—like Garamendi are doing irreparable harm to this industry and to the small businesses who have made large corporations like Universal Life Resources wealthy.

By the way, a hearing will be held on Garamendi's legislation in Sacramento on April 20th.