ICP 25:
Consumer Protection

Basic-level Module
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About the Core Curriculum

A financially sound insurance sector contributes to economic growth and well-being by supporting the management of risk, allocation of resources, and mobilization of long-term savings. The insurance core principles (ICPs), developed by the International Association of Insurance Supervisors (IAIS), are key international standards relevant for sound financial systems.

Effective implementation of the ICPs requires skilled and knowledgeable insurance supervisors. Recognizing this need, the World Bank and the IAIS partnered in 2002 to develop a “core curriculum” for insurance supervisors. The Core Curriculum Project, funded and supported by various sources, accelerates the learning process of both new and experienced supervisors. The ICPs provide the structure for the core curriculum, which consists of a set of modules that summarize the most relevant aspects of each topic, focus on the practical application of supervisory concepts, and cross-reference existing literature.

The core curriculum is designed to help those studying it to:

- Recognize the risks that arise from insurance operations
- Know the techniques and tools used by private and public sector professionals
- Identify, measure, and manage these risks
- Operate effectively within a supervisory organization
- Understand the ICPs and other IAIS principles, standards, and guidance
- Recommend techniques and tools to help a particular jurisdiction observe the ICPs and other IAIS principles, standards, and guidance
- Identify the constraints and identify and prioritize supervisory techniques and tools to best manage the existing risks in light of these constraints.
Welcome to ICP 25: Consumer Protection module! This is a basic-level module on consumer protection that does not require specific prior knowledge of this topic. The module should be useful to either a new insurance supervisor or an experienced supervisor who has not dealt extensively with the topic—or is simply seeking to refresh and update knowledge.

Start by reviewing the objectives, which will give you an idea of what a person will learn as a result of studying the module. Then answer the questions in the pretest to help gauge prior knowledge of the topic. Appendix II provides an answer key for the pretest. Then proceed to study the module either on an independent, self-study basis or in the context of a seminar or workshop. The amount of time required to study the module on a self-study basis will vary but it is recommended that it be addressed over a short time, broken into sessions on parts if desired.

To help you engage and involve yourself in the topic, we have interspersed the module with questions dealing with the situation, requirements, and practices in your jurisdiction. These are intended to help you apply the material in this module to your local circumstances. If you are working with others on this module, develop the answers through discussion and cooperative work methods. Since these responses will vary by jurisdiction, the answer key suggests where you might look for the answers.

As a result of studying the material in this module, you will be able to do the following:

1. Assess the fairness and adequacy of insurer practices regarding marketing and sales, underwriting and rating, policyholder services, claims handling and complaint handling
2. List the types of information and notifications that insurers and intermediaries should provide consumers at various stages in the purchase, ownership and use of insurance products.

3. List the types of information that might be sought from a consumer by an insurer or an intermediary to assess insurance needs before giving advice or concluding a contract.

4. Recognize indicators that might prompt you to investigate an insurer or intermediary for its treatment of consumers.

5. Describe the basic considerations involved in designing such an investigation.

6. Describe the risks posed to consumers by insolvencies and monopolies and the methods you might use to minimize these risks.

7. Describe the risks to consumers that arise when they purchase insurance across jurisdictional borders and through distance marketing, and the steps that you might take to reduce those risks.

8. Assess the adequacy of methods used by insurers to protect the privacy of consumer information.

9. Describe the ways in which you might educate consumers about insurance products and pitfalls.

10. List the methods that may be available to consumers to resolve insurance disputes without resorting to litigation.

11. Summarize the requirements of ICP 25.
Pretest

Before studying this module on consumer protection, answer the following questions. The questions are designed to help you gauge your existing knowledge of this topic. An answer key is presented in appendix II at the end of the module.

For each of the following questions, circle the responses that are correct. More than one response may be valid.

1. **Which of the following insurance consumers are usually protected by consumer protection regulations?**
   a. A beneficiary under a group life insurance policy
   b. An applicant for a homeowner’s policy
   c. The owner of a worker’s compensation policy
   d. An uninsured pedestrian who submits a claim against the insurer of the vehicle that hit her.

2. **Which of the following items should be displayed in the periodic reports that insurers provide to their permanent life insurance policyholders?**
   a. The amount of outstanding policy loans
   b. Mortality charges incurred during the reporting period
c. The policy’s current cash value
d. Premiums paid during the reporting period.

3. Which of the following statements are true? “Rates for insurance products should not...”
   a. be inadequate.”
   b. incorporate underwriting judgment.”
   c. be excessive.”
   d. be unfairly discriminatory.”

4. Examples of unfair trade practices include which of the following?
   a. Terminating an automobile policy for the nonpayment of a premium
   b. Providing a rebate to induce a sale
   c. Canceling a health policy because of a claim submission
   d. Selling a life insurance policy through an unlicensed intermediary.

5. The complaint databases that insurers maintain should include which of the following?
   a. Nature of each complaint
   b. Outcome of each complaint
   c. Number of complaints by type of insurance
   d. Length of time required to process each complaint.

6. On which of the following areas of operation might a market conduct investigation focus?
   a. Policyholder service
   b. Complaint handling
   c. Executive compensation
   d. Underwriting practices.

7. Which of the following statements apply to guarantee funds?
   a. They usually cover only consumer insurance products
   b. They are funded by assessments on insurance companies
   c. They limit the amount they will pay on an individual claim
   d. They cannot easily handle large insolvencies.
8. **The types of personal consumer information that insurers and intermediaries should safeguard include which of the following?**
   a. Medical records
   b. Street addresses
   c. Claim histories
   d. Credit reports.

9. **The risks of purchasing insurance on the internet include which of the following?**
   a. The insurer or the product might not be authorized in the consumer’s jurisdiction
   b. Licensed agents are not readily available for advice
   c. Digital contracts might not be legally binding in the consumer’s jurisdiction.
A. Introduction

Insurance is an intangible product that exists on paper as a complex legal contract. Designed to provide peace of mind or satisfy various governmental or lending requirements, insurance is a product that few people thoroughly understand or enjoy buying. The complexities of coverage, pricing, and the processes involved in applying for coverage and filing a claim, combined with the lack of satisfaction inherent in purchasing an intangible product, often create a gap between what the consumer expects and what the provider delivers. This gap results in a chasm of distrust between consumers and insurance companies.

Most insurance products are based on the principle of spreading the costs of certain misfortunes (car crash, house fire, illness, or a death) among groups of people, who share these risks. At its core, this is a communal or socialistic principle. However, most insurance companies are profit-driven entities. As with all enterprises involving a public good in which the delivery mechanism is driven by profit, effective government regulation is necessary to ensure that the delivery mechanism does not shortchange or otherwise fail to maintain its fair and proper responsibilities in the delivery of insurance products.

Due to the imbalance of technical knowledge between consumers and insurance professionals, consumers are highly dependent on insurance intermediaries for help in deciding which insurance products to buy and which coverage or savings options to elect. In situations in which consumers are illiterate, such dependence on intermediaries is all but total. In many situations, there is ample opportunity for intermediaries to
take advantage of consumers by selling them products that do not fit their needs, are overpriced, are underwritten by financially unstable insurers, or are fraudulent.

Insurance companies are subject to the temptations of shortcutting services to their policyholders, avoiding the fair payment of claims and benefits, and unfairly discriminating among consumers. Insurers’ financial abilities to fulfill their contractual obligations, particularly on life insurance policies that may extend over the lifetime of the policyholder, often are difficult to predict. Furthermore, the dissemination of private consumer information and the selling of insurance products across national borders and through distance marketing methods such as the internet raise new risks for consumers.

It is these dangers, in their various forms, that supervisory authorities seek to minimize through consumer protection methods. ICP 25 on consumer protection states:

The supervisory authority sets minimum requirements for insurers and intermediaries in dealing with consumers in its jurisdiction, including foreign insurers selling products on a cross-border basis. The requirements include provision of timely, complete and relevant information to consumers both before a contract is entered into through to the point at which all obligations under a contract have been satisfied.

The full text of ICP 25 and its various essential and advanced criteria appear in appendix I. This module discusses some of the risks faced by consumers and expands upon the ways in which a supervisory authority can respond to them, as highlighted in the criteria.
B. Insurance consumers who need protection

This module defines an insurance consumer as an individual who obtains, tries to obtain, or submits a claim under, an insurance product or service intended for personal, family, or household use.\(^1\) Under this definition, we include not only purchasers of such insurance products and services but also claimants and beneficiaries.

The most common types of insurance products intended for personal, family, or household use are:

- Automobile insurance
- Health insurance
- Property insurance (homeowner's insurance, renter's insurance)
- Life insurance.

Consumers buy automobile insurance and property insurance on their own initiative. While consumers can and do buy life insurance and health insurance on their own, they also purchase or obtain such coverage through their employer or through organizations to which they belong. In the latter case, the employer or organization usually makes the purchase negotiation and decision.

Exercise

1. Are there types of consumer insurance products in your jurisdiction other than those listed above?

The definition of consumers includes individuals who file insurance claims, regardless of who owns the policy. A consumer who files a claim under a policy that he or she has purchased (or is listed as an insured or beneficiary) is referred to as a “first-party” claimant. A consumer who files a claim against someone else’s policy is called a “third-party” claimant.

Two of the essential criteria of ICP 25 directly address the need for insurers and intermediaries to deal appropriately with consumers:

The supervisory authority requires insurers and intermediaries to act with due skill, care and diligence in their dealing with consumers. (Essential criterion a)

The supervisory authority requires insurers and intermediaries to have policies on how to treat consumers fairly and to have systems and provide training to en-

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\(^1\) Strictly speaking, any entity that purchases insurance is a "consumer." However, consumer protection efforts focus primarily on individuals rather than on businesses since it is often argued that commercial enterprises (as well as trustees of group insurance programs) are quite capable of looking after their own (or their membership's) interests. On the other hand, it can be argued that very small businesses are in need of some measure of consumer protection since they face the same challenges of limited insurance knowledge and resources that individual consumers do.
sure compliance with those policies by their employees and other sales collaborators. (Essential criterion b)

While insurance companies are required to treat all claimants fairly (as will be discussed later), the companies frequently give, or are allowed to give, preferred treatment to first-party claimants. This preferential treatment is in recognition of the fact that no contractual relationship exists between third-party claimants and the insurance company.

**Exercise**

2. **Does your jurisdiction allow automobile insurers to treat third-party claimants differently from first-party claimants?**
C. Consumer education and policyholder information

Both intermediaries and insurance companies have roles to play in educating and informing consumers, as well as in obtaining information from them.

Role of Intermediaries

Due to the complexity of insurance products and the abundance of providers, most consumers rely on the intercession and advice of intermediaries when buying insurance. Intermediaries can be divided into two groups: those who are appointed by and represent a specific insurer or insurers (usually called “tied intermediaries” or “agents”) and those who represent the consumer (usually called “brokers”). While most intermediaries serve the needs of consumers well, the allegiance of tied intermediaries to the insurers they represent can create conflicts of interest.

In view of the importance of their role, insurance intermediaries are required by most jurisdictions to be licensed or registered as a consumer protection measure. To obtain a license or registration, intermediaries usually are required to demonstrate their knowledge of the types of insurance products that they will sell, to pass a background character check, and to obtain adequate insurance or bonding against liability that may result from their professional negligence. ICP 24 and the related module provide more information on the various roles of intermediaries.

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2 This module refers to intermediaries as those who assist in the purchase and sale of insurance products. It should be noted that intermediaries also exist who specialize in handling claims. These intermediaries, often referred to as “adjusters” or claims managers, are hired by, and represent the exclusive interests of, the insurer. We therefore treat them as an extension of the insurer, regardless of whether they are employed or outsourced by the insurer.

Policyholder information

One of the keys to protecting consumers is to ensure that they are provided with full disclosures of pertinent policy-related and insurer-related information in a timely manner. Occasions in which insurance consumers are most in need of such information include:

- At the point of sale
- Before policy renewals, nonrenewals, and cancellations
- During the submission of claims
- Periodically during long-term life insurance policies and annuity contracts.

**Point of sale: information needed from the consumer**

Consumers’ initial need to supply and receive accurate and pertinent information arises when they are preparing to buy an insurance policy. As stated in ICP 25, essential criterion c:

The supervisory authority requires insurers and intermediaries to seek the information from their consumers that is appropriate to assess their insurance needs, before giving advice or concluding a contract.

The intermediary must ascertain the consumer’s current risk situation (including any existing insurance policies), insurability, and needs; and then find the most appro-

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**Figure 1. Information Needed from the Consumer**

<table>
<thead>
<tr>
<th>Product</th>
<th>Information needed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Life insurance</td>
<td>Age, sex, smoker vs. nonsmoker, general health</td>
</tr>
<tr>
<td>Health insurance</td>
<td>Age, sex, smoker vs. nonsmoker, pre-existing medical conditions</td>
</tr>
<tr>
<td>Automobile insurance</td>
<td>Age, sex, driving record, type of vehicle, use of vehicle, credit history, claims history</td>
</tr>
<tr>
<td>Homeowner’s insurance</td>
<td>Value of home, type of construction, level of neighborhood fire protection, prior claims</td>
</tr>
</tbody>
</table>
appropriate coverage at the best price. To accomplish these goals, the intermediary needs to obtain a fair amount of information from the consumer. A partial list of such information might include the items shown in figure 1.

The intermediary also needs to ascertain the amounts of coverage that the consumer desires and can afford as well as any optional deductibles and subcoverages. In addition, life insurance products require the intermediary to ascertain the consumer's financial security goals such as:

- After-death support for dependents
- Retirement income
- College tuition fund for insured's children.

Much of the information that consumers provide will become part of the written and signed policy application. While consumers may be tempted to omit or distort information to lower their premiums, it is important that they be aware that relevant misrepresentations on their part may, if discovered, lead to the denial of claims or even criminal prosecution. For this reason, supervisory authorities often require that applications contain prominent warnings to consumers of the risks of omitting information or providing false information.

**Point of sale: Information to be provided to the consumer**

Conversely, the consumer also needs information from the insurer and intermediary. ICP 25, essential criterion d requires that:

The supervisory authority sets requirements for insurers and intermediaries with regard to the content and timing of provision of information:

- On the product, including the associated risks, benefits, obligations, and charges
- On other matters related to the sale, including possible conflict of interest to existing or potential policyholders.

Prior to the sale, the intermediary should provide the consumer with detailed information on the policy, including effective and expiration dates; the persons or properties that will be covered; coverage provisions and exclusions, such as policy limits, deductibles, face values, co-payments, and dividends or bonuses (if applicable); and beneficiary provisions.

The intermediary should provide the consumer with information about the total premium, including any taxes or special fees that will be charged to the consumer. If any portions of the premium are not known at the point of sale, this should be made clear
to the consumer, and examples of potential costs should be provided where feasible. Finally, the consumer should be provided with premium payment information, including payment plans where available.

In addition to detailed information on the product to be purchased and premiums to be charged, it is important that, prior to the sale, the intermediary provide information to the consumer on the insurer and the intermediary and on complaint contacts. Such information should include:

- Insurer’s name, address, phone and license
- Intermediary’s name, address, telephone, and license
- Intermediary’s relationship to the insurer (that is, is he or she tied to, or have an ownership interest in, the insurer?)
- Contact information for the supervisory authority and, if applicable, for ombudspersons and for alternative dispute resolution (ADR) mechanisms (discussed in section F) for the submission of complaints and disputes.

Note that some or all of this information may be provided on the policy cover page, sometimes referred to as a schedule or declaration page. In the case of internet sales and other forms of distance marketing for which an intermediary is not present, this information should be provided to the consumer prior to sale.

For group insurance policies, in which the consumer is an insured party but is not the policyholder, information pertinent to the consumer usually is provided by the policyholder to the consumer through a certificate of insurance and/or a brochure.

Insurers should provide privacy notices at the point of sale. These notices (see section I), alert policyholders to the kinds of nonpublic personal information that the insurer collects and how it safeguards that information.
Life insurance illustrations. Life insurance presents an interesting example of a complex product in which the consumer is heavily dependent on technical information provided by the insurer or its intermediary to make a wise purchasing choice. There are a wide variety of life insurance products that blend the goals of providing death benefits and providing cash reserves that insureds can use in a variety of ways.

Such life insurance products may produce an expectation gap between what the consumer expected and what the insurer promised and ends up delivering. To protect both consumers and insurers, supervisory authorities require insurers and intermediaries to take great care in explaining these complex details and options to consumers both at the point of sale and throughout the life of the policy.

When the premiums, cash values, death benefits, or dividends of a life insurance policy depend on interest rates or other factors that are not guaranteed, insurers must provide detailed examples, called “illustrations,” that display how the benefits and premium outlays that are not guaranteed may change as interest rates and other variable factors change. Scenarios are displayed for key evaluation points into the life of the policy, such as after 5, 10, 20, and 30 years. Either the supervisory authority or the jurisdiction’s life insurance association normally determines the principles on which these benefit illustrations are to be based.4

Life insurance illustration
A document that insurers provide to consumers that displays scenarios of how various life insurance benefits and costs may change over time with changes in interest rates and other nonguaranteed factors.

Renewals, nonrenewals, and cancellations
Unnecessary lapses, cancellations, and nonrenewals of insurance policies are disruptive and usually costly to consumers. Thus, insurers should provide policyholders with adequate written notice of whether the former intends to renew fixed-term policies that are not guaranteed renewable so that policyholders can plan accordingly. In jurisdictions that have residual market mechanisms, nonrenewal and cancellation notices should include contact information for applying to residual markets.

Residual market plan
A mechanism through which high-risk insureds who cannot obtain insurance through normal market channels are insured.

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4. For additional information on illustrations, see the Life Insurance Illustrations Model Regulation, www.naic.org.
Renewal notices routinely include the amount of the renewal premium. If premiums increase upon renewal, insurers provide an important courtesy to their policyholders if these renewal notices include an explanation of the reasons for any premium increases.

Cancellation of policies before their expiration dates, when allowed, must be done in writing with appropriate advance notice. Some reasons for cancellation, such as non-payment of premium, require the insurer to notify the policyholder only a short time before the effective date of the cancellation. Other reasons require longer periods of notice similar to those required for nonrenewals.

Reasons for cancellation that require only a short forewarning to the insured often include:

- Nonpayment of premium (except for life insurance policies with a cash value)
- Concealment or misrepresentation of significant facts during the application process
- Submission of a fraudulent claim.

Exercise

4. What residual market mechanisms, if any, exist in your jurisdiction?

Exercise

5. For what reasons are insurers in your jurisdiction allowed to cancel policies before their expiration dates?

Submission of claims

Typically, insurers take several distinct steps in settling a claim, such as providing the claimant with notices, forms, payment checks, and other documents. Many jurisdictions specify the maximum amount of time that insurers may take to perform each of

Exercise

5. For what reasons are insurers in your jurisdiction allowed to cancel policies before their expiration dates?
these steps for their first-party claimants. Claims-handling procedures are discussed in
detail in section F.

LIFE INSURANCE ACCOUNT UPDATES

Insurers who write life insurance policies that contain a cash value should provide their
policyholders with periodic statements of the financial status of their accounts. Figure
2 provides a simplified example of an annual statement on a permanent life insurance
policy.

Consumer outreach efforts

Supervisory authorities, industry associations, and civic organizations individually or
jointly can attempt to educate consumers about insurance coverages, costs, and pitfalls

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**Table: Sample Annual Statement for a Life Insurance Policy**

<table>
<thead>
<tr>
<th>Date</th>
<th>Premium payments</th>
<th>Mortality charges</th>
<th>Expense charges</th>
<th>Unpaid loans</th>
<th>Interest income</th>
<th>Cash value</th>
</tr>
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<td>3/3/05</td>
<td>65.42</td>
<td>9.81</td>
<td>4.24</td>
<td>4,236.41</td>
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</table>

Total: 785.04 116.86 50.88 46.49

Death Benefit as of March 3, 2006 100,000.00
Surrender Value as of March 3, 2006 85,876.41
as well as elicit feedback and complaints from consumers. Outreach methods for these purposes can include:

- Brochures
- Toll-free hotlines
- Press releases
- Newspaper and magazine articles
- Public meetings
- Radio talk shows (particularly effective for reaching illiterate consumers)
- Websites.

Insurance supervisory authorities’ websites are becoming an increasingly important method for broadcasting information. Supervisory authorities commonly use their websites to post and update various kinds of consumer information including:

- Newsworthy items, including alerts on fraudulent operations
- On-line submission of complaints
- Complaint statistics by insurer
- Lists of licensed or registered insurers
- Premium comparison guides.

Premium comparison guides can be particularly helpful to consumers. Such guides show the premiums that each company charges for automobile, homeowner’s, and other types of standard insurance products. For a given type of insurance, premiums are displayed for a select sample of hypothetical insureds of different ages, genders, claim histories, locales, insured properties, and other risk characteristics.

**Exercise**

6. **What consumer outreach methods are in place or would be most effective in your jurisdiction?**
D. Policy forms and rates

Coverage provisions

Insurance policies are legal contracts crafted by lawyers and insurance experts who may be oblivious to the difficulties that consumers face in reading and understanding these contracts. Included in most policies are a variety of provisions that restrict or eliminate coverage under various circumstances. Such exclusionary provisions can be difficult to understand, can seriously weaken the overall coverage provided by the policy, and can conflict with insurance laws and regulations. Supervisors may play a role in helping consumers in this area, as noted in ICP 25, advanced criterion h:

The supervisory authority promotes the consumers’ understanding of insurance contracts.

Some supervisory authorities review all insurance products sold by licensed insurers to consumers in their jurisdictions to ensure that all policy forms, endorsements, riders, applications, and other standard components of insurance contracts:

- Contain coverage provisions that comply with applicable laws and regulations
- Are easy to read and understand
- Do not conflict with the public good.

Required provisions and disallowed provisions vary by jurisdiction and by type of product. For example, the list of required provisions in life insurance policies often includes the following:

- A “free look” period, granting the policyholder the right to cancel or withdraw from the policy for a full refund during the first several days that the policy is in effect
- A grace period for the late payment of premiums without allowing the policy to lapse
- An “incontestability” provision barring insurers from voiding the contract for misrepresentations made by consumers in the policy application, if those misrepresentations are not discovered by the insurer within a set time
- For policies that contain a cash value, a nonforfeiture provision that disallows policies to lapse for nonpayment of premium. Policy continuation options contained in a nonforfeiture provision may include: (a) refunding the cash value to the policyholder, then terminating the policy; (b) using the cash value to make premium payments until the cash value is exhausted; (c) reducing the amount
of coverage to what the cash value can afford to fund for the remainder of the insured’s lifetime.

**Permanent life insurance**
Any form of life insurance except term. Generally, insurance, such as whole life or endowment, that accrues cash value. Universal life and variable life are examples of permanent life insurance.

**Cash value**
The amount of savings to which a policyholder has contributed or earned under a permanent life insurance policy.

**Nonforfeiture option**
Privilege available to the policyholder based upon his or her interest in the contract, or once cash value has been created.

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**Readability**

Supervisory authorities may require that consumer insurance policies be written and printed in such a way that the average person can understand them. To accomplish this, policies should be written in everyday, conversational language consistent with their legal standing as a contract.

Ways to make policies more readable include simplifying policy language, organizing the content in a clear and logical manner, and using good graphic layout.

Policy language may be simplified by:

- Using commonly understood words
- Avoiding the use of technical legal terms wherever possible
- Using simple sentence structure and short sentences

Policies are easier to read if:

- They include a table of contents of important provisions
- Each section is as self-contained and independent as possible.

Good graphic layout techniques include the following:

- Avoid using small fonts
- Use captions, headings and spacings liberally.

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Rates

The derivation of premiums charged for insurance products is a mystery to most consumers, who simply rely on market competition to keep premiums as low as possible. Equally confusing to consumers are the differences in premiums charged for various options in coverage limits, benefits, deductibles, and co-payment provisions.

It is important that rates and rating methodologies used to determine premiums are not excessive, inadequate, or unfairly discriminatory. By rates and rating methodologies we include everything used to determine the premium that a policyholder is charged, such as:

- Manuals of rates for each class of risk
- All schedules of rate adjustments to reflect variations in individual risk characteristics within a class
- All factors applied to rates, including but not limited to factors to reflect increased coverage limits and policy deductibles
- Any policy fees and charges, including but not limited to: installment fees for premium payment plans; fees to reinstate policies canceled due to nonpayment of premium; and all initial and recurring charges and commissions
- Minimum premiums, if applicable
- Rating rules and algorithms.

Supervisory authorities seldom have the actuarial and staff resources to thoroughly scrutinize consumer rate filings. In some cases, supervisory authorities require appointed actuaries or other experts to certify the appropriateness of the rates or rating methodology. In any case, supervisory authorities that chose to prioritize the level of scrutiny they will give to various filings may wish to consider:

- Availability of actuarial resources
- Levels of competition in the marketplace for various consumer insurance products
- Magnitude of rate changes contained in particular filings
- Number of policyholders affected by particular filings.
Rate filings should include adequate documentation to support the insurer’s estimates of the rates and rating factors needed to produce fair rates for policyholders and an adequate profit for the insurer. Such supporting documentation should include:

- The relevant premium, claims, and other statistical data of the insurer or its rate advisory organization
- Adjustments and interpretations of these statistics
- Methodologies used
- Judgments and competitive considerations used, if applicable.

**Exercise**

8. **What actuarial resources are available to the supervisory authority in your jurisdiction?**

Rate filings should include adequate documentation to support the insurer’s estimates of the rates and rating factors needed to produce fair rates for policyholders and an adequate profit for the insurer. Such supporting documentation should include:

- The relevant premium, claims, and other statistical data of the insurer or its rate advisory organization
- Adjustments and interpretations of these statistics
- Methodologies used
- Judgments and competitive considerations used, if applicable.

**Actuary**

A professional trained in evaluating the financial implications of contingent events. Actuaries require an understanding of the stochastic nature of insurance, the risks inherent in assets and the use of statistical models. For example, these skills often are used in establishing premiums and technical provisions for insurance products, using the combination of discounted cash flows and probabilities.

**Rate Advisory Organization**

An organization that compiles and uses statistical data to produce advisory rating components available for the use of its member insurance companies.

**Checking for excessive rates**

A universal concern of consumers is that their insurance rates not be too high. A competitive marketplace with well-informed consumers will, in theory, self-police its own rates. However, the supervisory authority may review rate filings to determine if filed rates are adequately supported and justified. If a rate increase is being filed, supporting documents should show that the current rates are inadequate to produce a reasonable profit.
CHECKING FOR INADEQUATE RATES

Inadequate rates can contribute to insurance company insolvencies, which are, of course, detrimental to consumers.⁶

CHECKING FOR UNFAIRLY DISCRIMINATORY RATES AND RATING PRACTICES

Rates and rating practices are unfairly discriminatory if they produce higher premiums for certain policyholders or demographic groups that are not correlated with increased risk for these policyholders or groups. In addition, it is widely accepted that the use of race, national origin, religion or income as rating factors should be forbidden, even if they correlate with insurance risk. Demographic factors that have demonstrated a statistical correlation to risk and often are allowed for use include:

- Age and gender for life, health, and automobile insurance
- Credit history for automobile and property insurance.

Note that some jurisdictions allow supervisory authorities to prohibit rating practices that disadvantage a particular demographic group, such as low-income ethnic minorities or those inflicted with HIV/AIDS, even if there is evidence that the particular demographic group is costly to insure. Gender also may be prohibited as a rating factor in some jurisdictions.

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⁶ ICP 19 discusses the measures that supervisory authorities may take to ensure that rates are not too low.
E. Unfair trade practices

As mentioned earlier, most consumers have a limited understanding of the complexities of insurance products and, quite properly, rely on the advice of insurance intermediaries. Unfair trade practices arise when insurance companies and intermediaries take advantage of this imbalance in insurance knowledge in their marketing, sales, underwriting, and rating practices.

Deceptive and unfair marketing and sales practices

Insurers and intermediaries take unfair advantage of consumers at or before the point of sale if the former exaggerate the coverages and services provided, fail to mention exclusions and other product shortcomings, downplay the true price, or fail to mention hidden costs or contingencies. Specific examples of deceptive or unfair marketing and sales practices can include:

- Using advertising and sales materials, intermediary training materials, and/or mass-marketing activities that are false or deceptive
- Inducing a sale through the use of kickbacks or rebates
- Selling products through inadequately trained intermediaries
- Selling consumers more coverage than they need
- Misrepresenting a product’s coverages, rates, terms, or benefits
- Exerting undue control over the marketplace through any form of boycott, coercion, or intimidation
- Failing to provide life insurance customers with full and accurate “illustrations” showing how costs and benefits may change with future changes in interest rates and other variables
- Making unfair or incomplete comparisons among life insurance policies to induce policyholders to replace their current policy, called “twisting”
- Investing life insurance funds in riskier assets than those promised in marketing materials or contractual agreements.

Rebate
A reduction in the premium that otherwise would be charged to a policyholder, to induce the consumer to purchase the policy.

Twisting
The practice of encouraging the replacement of one life insurance policy with another through the misrepresentation or incomplete disclosure of all relevant information on the existing and proposed policies.
Deceptive practices include fraudulently posing as an insurer or insurance intermediary or otherwise offering insurance-type products without a license. An example is the proliferation of fake insurance companies and unlicensed intermediaries selling fraudulent health, life, and funeral insurance plans. Such counterfeit plans often are spawned by restrictions in the availability of affordable insurance from legitimate carriers.

**Exercise**

9. What fraudulent insurance schemes, if any, are currently issues in your jurisdiction?

**Unfair underwriting practices**

The key ingredient of good underwriting is the ability to distinguish good risks from bad risks. Insurance companies are expected to develop and maintain written guidelines for help in determining which applicants to accept and which to decline. Such guidelines are based on a mixture of statistical analysis of the marketplace and seasoned underwriting judgment. Nonetheless, insurers and their underwriters will occasionally make decisions that supervisory authorities view as unfair or illegal, such as:

- Using policy forms and endorsements that have not been filed (if required) with the supervisory authority
- Using intermediaries who are not properly licensed and appointed (if required) in the jurisdiction in which the application was taken
- Rescinding policies for insignificant misrepresentations on the application
- Refusing to insure an applicant because s/he have been rejected by another insurance company
- Terminating a policy because of the submission of a claim.

**Unfair discrimination in underwriting**

Issues involving social discrimination occur when either statistics or judgment lead insurance companies to believe that certain races, genders, age brackets, income levels, or credit histories generally represent worse than average or better than average risks. Insurance companies might act on such beliefs on a broad scale when defining the targets of their marketing efforts or on an individual basis when accepting or declining applications.

When such assessments are grounded in actuarial statistics, supervisory authorities may often allow them. Examples of the latter include higher automobile insurance
rates for young male drivers and lower automobile and homeowners insurance rates for people with good credit histories.

However, social discriminations that are based primarily on judgment often are either illegal or are viewed by supervisory authorities as unfair. Examples of unfair discrimination usually include refusing to insure an applicant, or otherwise disadvantage a consumer, because of:

- Their sex, marital status, sexual orientation, race, ethnicity, religion, or income
- For property insurance, the age, or neighborhood of the property
- For automobile or property insurance, or the mental or physical impairment of the insured.

Unfair discrimination
Favoring one demographic group over another in the underwriting or rating process for reasons either unrelated to the groups’ relative insurance risk or considered unacceptable by the society.

Exercise
10. What demographic underwriting considerations or rating factors are not permitted in your jurisdiction?

Unfair rating practices

Insurance companies are expected to develop, maintain, and strictly adhere to rating manuals that detail all the steps involved in calculating the premium to be charged for any coverage offered on any given risk. The following are examples of unfair rating practices:

- Charging premiums that are not in accordance with filed rates and rating manuals
- Permitting illegal rebating, commission cutting, or other kickbacks to intermediaries or policyholders
- Applying credits and deviations in an inconsistent or discriminatory manner
- Charging higher or lower premiums to applicants or policyholders due to race, income, gender, religion, marital status, geographic location, or any reason not directly related to insurance risk.
Poor administration of policyholder accounts

As with banks and other entities entrusted with the proper handling of other people's money, insurance companies are responsible for maintaining accurate accounting of various funds held in policyholder accounts. Such accounts include:

- Provisions for premiums paid but not yet earned. This includes the accurate calculation of the amount of money to be returned to a policyholder if their policy is cancelled prior to its expiration date.
- Cash surrender values, benefit amounts, outstanding loan balances, and other account values in permanent life policies, as well as the allocation of such funds to the proper investment portfolios.
- Policyholder dividends that have been paid or are payable, as in some insurance policies that provide for participation in profits.

The poor administration of such accounts can lead to the improper calculation or denial of return premiums, life insurance benefits, and policyholder dividends as well as the improper investment of policyholder funds and errors or delays in the payment of claims.

Ways to combat unfair trade practices

There are several lines of defense against the proliferation of the unfair, deceptive, or careless practices described above, such as the following:

- The requirements for obtaining an insurance license or registration should be designed to ensure that intermediaries and insurance executives have adequate knowledge, experience, integrity, and financial resources to conduct insurance operations fairly and reliably.
- Insurers should be required to maintain internal controls to prevent unfair, deceptive, or unprofessional trade practices.
- Insurers, supervisory authorities, and ombudsmen can provide consumers with opportunities and methods to submit complaints against such practices.
- Supervisory authorities in most jurisdictions are empowered to conduct on-site investigations into the market conduct of insurers and intermediaries suspected of engaging in such practices. If wrongdoing is revealed, supervisory authorities can take disciplinary actions ranging from fines to the revocation of licenses or registrations.
F. Claim and complaint handling

The majority of consumer complaints relates to claims and benefit payments. While most insurers handle and pay claims and benefits in a timely and fair manner, some insurers succumb to the temptation to look for ways to avoid paying claims, particularly when under financial stress. ICP 25, essential criterion e addresses this explicitly, stating:

The supervisory authority requires insurers and intermediaries to deal with claims and complaints effectively and fairly through a simple, easily accessible, and equitable process.

There are a number of ways in which companies may try to avoid paying legitimate claims, cash value settlements, policyholder dividends, and other benefits. The following are some of the more common ways:

- Denying a claim without conducting a reasonable investigation
- Needlessly delaying the investigation or payment of a claim
- Requiring unnecessary or duplicate reports or documents
- Failing to explain the reason for denying a claim
- Paying or offering to pay less than a reasonable amount
- Refusing to communicate the status or outcome of a claim investigation
- Failing to adopt and follow reasonable guidelines for handling claims and other benefits
- Misrepresenting relevant facts and coverage provisions
- Compelling claimants to sue to get a proper settlement
- Neglecting the fair distribution of profits on policies that the insurer has stopped marketing.

It is critical that insurers adopt and follow detailed internal guidelines and procedures for the fair and prompt handling of claims and other policyholder benefits. Such guidelines, among other things, should require senior management review of claim and benefit decisions that exceed particular monetary or other thresholds. These guidelines also should list the steps required (and timeframes allowed) to investigate and process claims and benefits. These steps are likely to include (in chronological order):

1. Receiving notification of a claim from the claimant or intermediary
2. Providing the claimant with claim forms, instructions, and reasonable assistance
3. Receiving properly executed proofs of loss from the claimant
4. Advising the claimant as to whether the claim is accepted or denied
5. Paying the claim if the insurer has accepted liability for it.
**Consumer complaints**

It is important for the protection of consumers that their complaints against insurers and intermediaries not only be promptly and fairly investigated and processed by the insurer, but that those complaints also be knowable to the supervisory authority. Supervisory authorities can learn of complaints:

- Directly from consumers
- Through inspections of insurers’ complaint databases
- Through formal reports from insurers on claims and claim handling
- From ombudsmen.

**Ombudsperson**

An official appointed by an appropriate governmental, civic, or industry body to investigate consumer complaints.

**Exercise**

11. What methods and venues do consumers in your jurisdiction have to submit complaints?

Supervisory authorities depend on insurers’ complaint databases for the review and investigation of the full body of recorded consumer complaints. The ability of a supervisory authority to scrutinize complaint databases provides additional motivation to insurers to treat consumers and complainants properly. Such databases should include the:

- Number of complaints by line of insurance
- Nature and disposition of each complaint
- Time required to process each complaint.

**Alternative dispute resolution methods**

Despite the efforts of insurers and supervisory authorities, from the consumer’s viewpoint, a fair number of complaints do not get satisfactorily resolved. In these situations, litigation remains, or should remain, an option. However, it is often to the consumer’s benefit to resolve disputes in ways that are simpler, quicker, cheaper, and less stressful than litigation.
A variety of ADR methods have been developed in many jurisdictions. These methods often are administered by government bodies or by industry associations that include consumer representatives. Regardless of the sponsoring body, most ADR methods involve the key assistance of a neutral party knowledgeable in the type of issue that is under dispute. This neutral party, often an ombudsperson, renders a finding or decision after hearing both sides argue their cases.

When the insurance industry administers the dispute resolution mechanism, the decisions of the ombudsperson usually are binding on the insurer but not on the consumer, who retains the right to take the matter to court. When a government agency administers the dispute resolution, the decisions of the ombudsperson often are binding on both parties.

Consumer protection is optimized when insurance policies contain clauses that allow the policyholder to decide whether to use ADR or go to court. For that reason, many supervisory authorities disallow provisions in insurance policies that mandate the exclusive use of ADR.

The European Community has created an ADR mechanism for disputes involving insurance and other financial services. Called FIN-NET, this mechanism provides a well-structured network of procedures for the swift, fair, and efficient redress of cross-border consumer disputes, including a printed guide that advises consumers how to file a complaint in the FIN-NET system.7

Exercise

12. What alternative dispute resolution mechanisms are available to consumers in your jurisdiction?

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7. The guide and other information on FIN-NET can be downloaded from europa.eu.int/comm/internal_market/finservices-retail/finnet/index_en.htm.
G. Investigations of market conduct

As mentioned earlier, some insurers and intermediaries do engage in various unfair and deceptive practices toward consumers. Such practices often produce a high level of consumer complaints.

**Market conduct**

The treatment of policyholders, claimants, insureds, and beneficiaries by insurance companies in regard to claims handling, underwriting and rating, policyholder service, complaint handling, and marketing and sales.

To investigate alleged patterns of misconduct toward consumers, it is important that supervisory authorities conduct on-site investigations into the market conduct of insurers and intermediaries. Such market conduct investigations may be triggered by:

- A high level of complaints
- A large share of the market
- Routine scheduling of examinations.

**Exercise**

13. If market conduct investigations are performed in your jurisdiction, what most commonly triggers them?

The methods and standards that supervisory authorities use in such investigations should be fair and unbiased, transparent, open to public inspection, and known in advance to the industry. Such investigations may focus on particular products or coverages as well as on one or more of the following operational areas:

- Claims handling
- Underwriting and rating
- Policyholder service (such as required notices, premium billings, account management)
- Complaint handling
- Marketing and sales.

**Compliance**

Adherence to applicable laws and regulations.
Once the supervisory authority determines which product lines and operational areas to inspect, it should compile a list of specific supervisory authority standards that the insurer likely may be violating. Say, for example, that the inspection is focused on claims handling, and claimants have alleged that the insurer is slow in investigating claims, often provides unrealistically low settlement offers, and does not communicate reliably with claimants. The supervisory authority may choose to inspect the insurer’s compliance with the following standards:

- Company’s initial contacts with claimants are within required timeframes
- Company conducts timely investigations
- Claims are resolved in a timely manner
- Company responds to claim correspondence in a timely manner
- Claim files are adequately documented
- In cases of clear liability and coverage, the company does not offer claimants unreasonably low amounts.

Once the scope of the inspection has been determined, the supervisory authority should specify the methods, techniques, and criteria of the inspection. Such specifications will include the sample sizes that should be drawn to achieve the desired level of confidence in the results. Although a proper discussion of sampling techniques and confidence levels is beyond the scope of this module, figure 3 provides a rough sampling method used in some jurisdictions.

The supervisory authority should determine the documents that will be needed to conduct the inspection. While many of these documents, such as sampled files and internal guidelines and controls, will come from the insurance company being investigated, some documents such as pertinent laws and regulations will come from the supervisory authority. Additional documents may come from other sources.

The various preliminary steps in conducting a targeted investigation of an insurance company’s market conduct are summarized below:

- Determine the types of insurance products to be examined
- Within these types of products, determine the operational area or areas to be investigated

### Figure 3. Possible Sampling Method

<table>
<thead>
<tr>
<th>If the population of files under investigation is</th>
<th>Then sample this number of files from the population</th>
</tr>
</thead>
<tbody>
<tr>
<td>more than 5,000</td>
<td>100</td>
</tr>
<tr>
<td>between 50 and 5,000</td>
<td>50</td>
</tr>
<tr>
<td>less than 50</td>
<td>all the files</td>
</tr>
</tbody>
</table>
Within each of the chosen operational areas, select the compliance standards to be examined
- List the methods, techniques, and criteria that the examiner will use, including the appropriate method of drawing samples
- List the documents needed to conduct the examination.

Figure 4 provides an example of a design for examining compliance with the standard that claims be resolved in a timely manner.8

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**Figure 4. Example of an Inspection of Compliance with Claim Handling Requirements**

*Type of insurance:* Personal automobile liability coverages

*Operational Area:* Claim handling

*Compliance Standard:* Claims are resolved in a timely manner

**Review Procedures and Criteria:**

- Review company procedures, training manuals, and claim bulletins to determine whether company standards exist and whether standards comply with applicable laws and regulations
- Determine whether claim resolutions (such as determinations of coverage, determinations of liability, and claim payments) are made in accordance with applicable laws and regulations
- Perform time studies to measure settlement time of claims
- Sample and review 100 claim files selected at random

**Documents to Be Reviewed:**

- Applicable laws and regulations
- Company claim procedure manuals
- Company claim training manuals
- Company claim audit reports
- Canceled claim checks
- Claim files

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H. Insolvencies and monopolies

Insolvencies

Financial strength and experienced management are the best indicators that an insurance company will remain in business to fulfill its commitments. Nonetheless, all insurance companies, even the biggest and strongest, run the risk of failing financially, perhaps for reasons and events beyond their control.

When insurance companies become insolvent, consumers face the risk that existing claims (or claims that may yet arise during the remainder of their policy terms) may not be paid and that any other services that they have a right to expect from their insurers may no longer be provided. For these reasons, it is in consumers' best interest to examine, either directly or with the help of their intermediaries, the strength of a particular insurance company prior to purchasing its products.

Such an examination is particularly important when buying life insurance, for which the insurance company must remain strong throughout the consumer’s lifetime. For this reason, life insurance policyholders also should be encouraged to study the annual financial communications from their insurers.

Guarantee funds

A number of jurisdictions have established funds to pay the claims of insolvent insurance companies. Such “guarantee funds” are funded by assessments levied against licensed insurers in proportion to each insurer’s pro-rated share of the market in the jurisdiction. While some guarantee funds are prefunded before insolvencies occur, others levy assessments only in response to specific insolvencies.

Most guarantee funds cover only certain types of insurance and often limit the amount of claim payments. Such provisions are employed in order to give highest priority to the disbursements of funds to consumers, to injured workers, and to small businesses.

While the social benefits of guarantee funds are clear, the following negative consequences may also arise:
• Ultimately, assessments are passed on, at least in part, to consumers in the form of higher premiums
• Assessments penalize the prudent business practices of solvent insurers by forcing them to pay for the underpriced products and other imprudent business practices of their now-insolvent competitors
• The insolvencies of large or monopolistic insurers can strain the resources of guarantee funds and leave claimants and other creditors with only a fraction of the reimbursements to which they otherwise would have been entitled
• The “safety net” provided by guarantee funds may entice insurers to underprice their products and lower their underwriting standards.

**Exercise**

14. What guarantee funds, if any, exist in your jurisdiction? How are they administered and funded?

**Monopolies**

Dangers also arise when monopolies exist. When an insurer or group of insurers monopolize or otherwise exert undue control over products in the insurance marketplace, prices for these insurance products tend to increase and the range of coverage options available to consumers tends to diminish. Since there are fewer viable insurers in the marketplace, residual market mechanisms (such as mandatory pools for insuring unattractive risks and sharing the experience among all insurers) tend to grow as consumers find it harder to obtain affordable insurance coverage in the voluntary market.

If a monopolistic carrier goes insolvent, the resulting unpaid claims may either exceed the resources of the guarantee fund or require severe assessments that disrupt the market and ultimately are borne by consumers or taxpayers. These ill effects occur regardless of whether the failing monopoly is privately owned or government run.

**Licensing insurers**

As a first line of defense against insolvencies, supervisory authorities should license or register only the insurers that can demonstrate that they have:

• An experienced and reputable management team
• A viable business plan
• Adequate capital to support their current and planned operations.  

9. Additional details on licensing insurers are provided in ICP 6.
Financial examinations of insurers

In addition to scrutiny during the license application process, supervisory authorities should conduct periodic financial examinations of all insurers domiciled in their jurisdictions. Supervisory authorities also should conduct financial examinations whenever an insurer appears have financial difficulties, regardless of the date of their last examination.\(^\text{10}\)

\(^{10}\) Additional details on the conduct of financial examinations are provided in ICPs 13 and 23.
I. Privacy of consumer information

The electronic era has led to the capture and dissemination of increasing amounts of personal information about consumers. Insurance companies use this information when reviewing policy applications, determining rates, processing billings, handling claims, and marketing their products. The danger is expanding of this information being obtained by inappropriate entities. Supervisors can contribute to the protection of private information, as specified by ICP 25, advanced criterion f:

The supervisory authority requires insurers and intermediaries to set rules on the handling of customer information paying due regard to the protection of private information of customers.

The types of personal information that can cause damage to consumers if mishandled include:

- Financial
- Bank account numbers and balances
- Credit card numbers and balances
- Credit reports
- Health
- Medical records
- Communicable diseases
- Identity
- Social security numbers
- Race or ethnicity
- Insurance
- Claim histories
- Premium payment histories
- Lifestyle
- Sexual preference
- Religious, political, or philosophical beliefs
- Trade union membership.

Potential harms that can befall consumers if their nonpublic personal information falls into inappropriate hands include:

- Identity theft
- Unwanted marketing
- Harm to their personal reputations
- Blacklisting by other insurance companies.
To safeguard the privacy of consumer information, insurers should be prohibited from obtaining information under false pretenses, and supervisory authorities should encourage or require insurers and intermediaries to:

- Maintain procedures to safeguard such information
- Inform consumers of the company’s privacy policies and practices
- Allow consumers, without penalty, to opt out of allowing their information to be disseminated to unaffiliated third parties.

**Information security programs**

Insurers should be encouraged or required to develop and implement comprehensive written information security programs that include administrative, technical, and physical safeguards to protect consumer information. These safeguards should be appropriate to the size and complexity of the insurer and to the nature and scope of the insurer’s activities.

The goals of these security programs are to:

- Ensure the security and confidentiality of consumer information
- Protect against any anticipated threats or hazards to the security or integrity of the information
- Protect against unauthorized access to, or use of, the information that could result in harm or inconvenience to consumers.

When designing an information security program, insurers should:

- Identify internal and external threats that could result in unauthorized disclosure, misuse, alteration, or destruction of consumer information
- Assess the likelihood and potential damage of these threats, taking into consideration the sensitivity of the consumer information
- Assess the sufficiency of policies, procedures, consumer information systems, and other safeguards that already are in place
- Design systems that will control the identified threats commensurate with the sensitivity of the information as well as with the complexity and scope of the insurer’s activities.

An insurer’s information security program should include procedures to:

- Train its staff to properly implement the program
- Test or monitor the program’s key controls, systems, and procedures regularly
• Require service providers to implement appropriate measures to safeguard the insurer’s customer information while it is in their possession

An insurer should adjust its information security program whenever changes occur in the relevant technology, sensitivity of the consumer information, internal or external threats to this information, and the insurer’s business arrangements (such as mergers, alliances, outsourcing, and consumer information systems).

**Privacy notices to consumers**

Insurers should provide their customers with written notices regarding the company’s use of personal information as well as any rights the consumer may have to further restrict the dissemination of such information. While the timing and frequency of such notices may vary by jurisdiction, the notices should:

- Contain a clear, conspicuous, and accurate statement of the insurer’s privacy practices
- State the kinds of information that the insurer collects on its customers
- State the types of affiliated and unaffiliated entities with which it shares this information
- Provide opt-out procedures for the types and uses of information for which the consumer may choose to opt out.

**Opt out**

The right of a consumer to block the dissemination of his or her nonpublic personal information to parties unaffiliated with the insurer.

A sample privacy notice is shown in figure 5.¹¹

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¹¹ For more information on the protection of personal consumer information, see European Union Directive 95/46/EC at europa.eu.int/comm/internal_market/privacy/law_en.html and the Privacy of Commercial Financial and Health Information Regulation, www.naic.org
Figure 5. Sample Privacy Notice

Privacy Notice

The Rock Solid Insurance Company respects your privacy and safeguards information about you. We gather nonpublic personal information about you for the purposes of conducting business with you and offering you additional products and services in which we believe you may be interested.

We collect from you and other sources information such as your name, address, and telephone number. We also collect from affiliated and unaffiliated sources histories of your insurance purchases, premium payments, claim submissions, and credit reports.

We share information about you with our affiliates and also with unaffiliated companies that perform marketing services for us. We require these companies to keep your information confidential and to limit its use to specific purposes. We also provide information about you to others for the limited purposes of processing transactions that you request, responding to queries by government agencies, and investigating fraud.

We maintain physical, electronic, and procedural safeguards to protect your nonpublic personal information and restrict access to this information to employees who need to know.

Exercise

15. Is the privacy of consumer information viewed as a problem in your jurisdiction? If so, what steps do most insurers in your jurisdiction take to protect such information from unwanted dissemination?
J. Cross-border issues and distance marketing

Many insurers sell and administer their products in multiple jurisdictions, whether through traditional methods or through “distance marketing” methods such as the internet. Problems arise when insurers sell in jurisdictions in which they or their products are not licensed. Lack of licensure greatly reduces or eliminates the powers of supervisory authorities to protect consumers. It also reduces consumers’ trust in purchasing insurance products through distance marketing.12

Furthermore, products such as automobile insurance and accident and health insurance often offer worldwide coverage. While it is generally understood that the laws and regulations of the jurisdiction in which the policy was sold should prevail, cross-border disputes still can arise when claims occur.

Purchasing insurance on the internet, while offering unique marketing opportunities and efficiencies, also presents consumers with new risks, including:

- Lack of an intermediary to explain the product and advise the consumer
- Uncertainty over whether the insurer or the product are authorized in the consumer’s (or any) jurisdiction
- Theft, sale, or other unwanted dissemination of private consumer information
- The fact that contracts entered into on the internet are not legally binding in some jurisdictions
- Difficulties in enforcing benefit payments.

Insurance products offered across borders or through distance marketing are subject to the same requirements as insurance products offered locally and through intermediaries. The insurer (and intermediary, if used) should be licensed in the consumer’s jurisdiction and be subject to the same laws and regulations regarding trade practices and consumer notifications discussed earlier. Additional steps that can be taken by supervisory authorities to help protect consumers from these risks are identified in ICP 25, essential criterion g:

The supervisory authority gives information to the public about whether and how local legislation applies to the cross-border offering of insurance, such as e-com-

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merce. The supervisor issues warning notices to consumers when necessary to avoid transactions with unsupervised entities.

**Exercise**

16. **Which forms of distance marketing are used in your jurisdiction and for which insurance products? What regulatory oversight exists over these sales?**

**Memoranda of Understanding**

In addition to educating consumers on distance marketing risks and on known fraudulent operations, supervisory authorities can reduce cross-border problems by developing working relationships with their counterparts elsewhere. A frequently used tool for this purpose is the Memorandum of Understanding (MOU).

Supervisory authorities in differing jurisdictions often enter into MOUs to facilitate cross-border cooperation and exchanges of information. MOUs serve as statements of intent and outlines of cooperative procedures. They are not legally binding and do not override local laws and regulations. MOUs among insurance supervisory authorities frequently are used to obtain information to monitor and investigate the conduct of specific insurance companies. They also provide opportunities for supervisory authorities to develop broad cross-border working relationships.

**Memorandum of Understanding**

A written statement of intended cooperation among government agencies.

An example of an MOU designed to provide a mechanism to resolve consumer disputes is the *Memorandum of Understanding on a Cross-Border Out-of-Court Complaints Network for Financial Services in the European Economic Area*, which underpins FINNET, the alternative dispute resolution (ADR) mechanism discussed earlier. 13

**Exercise**

17. **Has the supervisory authority in your jurisdiction entered into any MOU with other jurisdictions? If so, to what do these MOUs pertain?**

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13. This MOU can be viewed at europa.eu.int/comm/internal_market/finservicesretail/finnet/index_en.html.
Whether accomplished through MOUs or other means, the development of cooperative relationships among supervisory authorities in various jurisdictions can have several benefits, including:

- Facilitating out-of-court settlements of cross-border disputes
- Aiding the monitoring, investigation, and prosecution of fraudulent or non-compliant insurance activities
- Raising the level of supervisory expertise of the signatories through sharing experiences and procedures
- Improving the level of confidence that supervisory authorities have over the quality of home supervision performed over insurers domiciled elsewhere
- Contributing to the standardization of insurance coverages and practices across jurisdictions.

Finally, we should note the importance for supervisory authorities to cultivate cooperative relationships with other governmental agencies within their jurisdictions. Examples include working with agencies that prosecute fraud to aid in the identification and prosecution of fake health insurers, and working with motor vehicle departments to identify uninsured drivers.
K. Summary

In this module, we have discussed the various dangers to which insurance consumers are exposed and the ways in which supervisory authorities strive to protect consumers. The discussion focused on insurance products for personal, family, and household use, including automobile, property, life, and health insurance. The imbalance in insurance knowledge between consumers and insurance professionals, and the important advisory role of intermediaries, were noted.

There are a variety of situations in which consumers need to obtain information from, or supply information to, insurers and intermediaries; the types of information and notifications expected were highlighted in the module. Supervisory authorities, industry associations, and civic organizations use various methods to provide helpful information to consumers.

Policies should be easy to understand and must comply with applicable laws and regulations regarding mandated provisions and prohibited exclusions. Rates also need to be appropriate for the coverages provided and not be unfairly discriminatory.

A range of unfair trade practices may exist in marketing, sales, underwriting, rating, and claims handling. The ways that supervisory authorities can curb these practices were mentioned in the module. Methods for encouraging the submission and reporting of complaints were discussed, along with methods other than litigation that might be used for resolving disputes between consumers and insurance companies.

The module provided an overview of market conduct investigations of insurers, including concerns that may trigger such examinations and areas that may be targeted for inspection. It also surveyed the steps involved in designing such examinations.

Insurer insolvencies and monopolies present dangers to consumers. Licensing requirements can help to protect consumers from such dangers, while detailed financial examinations of all insurers can provide early warning and allow supervisory intervention before insolvencies occur. The value and the shortcomings of guarantee funds in protecting consumers after insolvencies occur were discussed.

Insurers and intermediaries must safeguard the privacy of the financial, health, insurance, and identity information of consumers. Consumers should also be advised of their right to limit the dissemination of personal information.

Finally, we noted the risks posed by the sale and use of insurance products across jurisdictional borders and through distance marketing methods such as the internet. Communication and active cooperation among supervisory authorities of various jurisdictions are essential in dealing with such risks. The use of Memoranda of Understanding can facilitate such cooperation.
L. References

Organizations that produce an abundance of insurance regulatory publications and resources include: the National Association of Insurance Commissioners (NAIC), which is the main association of insurance supervisory authorities in the United States; the European Union (EU), which has promulgated a number of directives addressing insurance and other financial services; and the International Association of Insurance Supervisors (IAIS), which maintains a database of insurance laws and regulations from around the world.

**NAIC Publications**

An index of model laws and regulations promulgated by the NAIC is available at www.naic.org. These model laws and regulations, as well as the NAIC “Market Conduct Examiners Handbook,” are available from the NAIC for a fee.

**EU Directives**

Various EU directives are available online for free viewing and downloading, including:

- Directive 2002/65/EC, on the distance marketing of consumer financial services
- Directive 2002/92/EC, on insurance mediation
- Directive 95/46/EC, on the protection of individuals with regard to the processing of personal data and on the free movement of such data.

**IAIS**

Publications of the IAIS are freely available, and the Insurance Laws Database is available to members, at www.iaisweb.org.
Appendix I. ICP 25

ICP 25: Consumer protection
The supervisory authority sets minimum requirements for insurers and intermediaries in dealing with consumers in its jurisdiction, including foreign insurers that sell products on a cross-border basis. The requirements include provision of timely, complete, and relevant information to consumers both before a contract is entered into through to the point at which all obligations under a contract have been satisfied.

Explanatory notes

25.1 Requirements for the conduct of insurance business help to strengthen consumer confidence in the insurance market.

25.2 The supervisory authority requires insurers and intermediaries to treat their customers fairly, paying attention to their information needs. With respect to consumers in their own jurisdiction, the supervisory authority should set requirements with which insurers and intermediaries must comply. The requirements applicable to cross-border sales also should be clear.

25.3 For a large number of consumers, insurance products are difficult to understand and evaluate. Insurers and intermediaries have a greater knowledge of insurance issues than the consumers. Arrangements should therefore exist for potential policyholders:

- to have access to information needed to make an informed decision before entering into a contract
- to be informed about their rights and obligations for the duration of the contract.

25.5 These requirements should distinguish between particular types of customers. In particular, detailed conduct of business rules may not be appropriate for reinsurance transactions or in respect of professional customers. Nonetheless, this does not relieve reinsurers of their duty to provide complete and accurate information to the insurers with whom they deal.

Essential criteria

a. The supervisory authority requires insurers and intermediaries to act with due skill, care and diligence in their dealings with consumers.
b. The supervisory authority requires insurers and intermediaries to have policies on how to treat consumers fairly and to have systems and provide training to ensure compliance with those policies by their employees and other sales collaborators.

c. The supervisory authority requires insurers and intermediaries to seek the information from their consumers that is appropriate to assess their insurance needs, before giving advice or concluding a contract.

d. The supervisory authority sets requirements for insurers and intermediaries with regard to the content and timing of provision of information:

   • on the product, including the associated risks, benefits, obligations, and charges
   • on other matters related to the sale, including possible conflict of interest to existing or potential policyholders.

e. The supervisory authority requires insurers and intermediaries to deal with claims and complaints effectively and fairly through a simple, easily accessible and equitable process.

**Advanced criteria**

f. The supervisory authority requires insurers and intermediaries to set rules on the handling of customer information paying due regard to the protection of private information of customers.

g. The supervisory authority gives information to the public about whether and how local legislation applies to the cross-border offering of insurance, such as e-commerce. The supervisor issues warning notices to consumers when necessary to avoid transactions with unsupervised entities.

h. The supervisory authority promotes the consumers’ understanding of the insurance contracts.
Appendix II. Answer key

Pretest

1. All except c. Retail insurance consumers are usually protected by regulations, but employers own workers compensation policies.
2. All.
3. All except b. When appropriate statistics are not available, rates can incorporate underwriting judgment.
4. All except a.
5. All.
6. All except c. Executive compensation does not directly affect consumers and usually is more pertinent to a financial examination than to a market conduct investigation.
7. All except a. Guarantee funds often cover workers compensation and other commercial insurance products.
8. All except b. Street addresses are already public information.
9. All.

Exercises

1. Are there types of consumer insurance products in your jurisdiction other than those listed above?

The products listed (automobile, health, property, and life insurance) are available to consumers in almost all jurisdictions. Examples of other consumer insurance products that might be available and subject to consumer protection requirements include liability insurance and motor vehicle assistance plans (although the latter is often exempted from insurance regulation). Review the website of your supervisory authority, examine legislation and regulations, or consult with colleagues to identify the types of consumer products available in your jurisdiction.

2. Does your jurisdiction allow automobile insurers to treat third-party claimants differently from first-party claimants?

Examine legislation and regulations or consult with colleagues to determine the requirements for treating claimants in your jurisdiction.
3. **What are the intermediary licensing or registration requirements in your jurisdiction?**

Examine legislation and regulations or consult with colleagues to determine the requirements for licensing or registration of intermediaries in your jurisdiction.

4. **What residual market mechanisms, if any, exist in your jurisdiction?**

Examine legislation and regulations or consult with colleagues to determine the existence of residual market mechanisms in your jurisdiction. When they do exist, the organizations that operate such mechanisms may have websites that provide information on their operations.

5. **For what reasons are insurers in your jurisdiction allowed to cancel policies before their expiration dates?**

Examine legislation and regulations or consult with colleagues to determine the allowable reasons for cancellation in your jurisdiction. In some jurisdictions, such provisions are set out in legislation that deals specifically with insurance contracts.

6. **What consumer outreach methods are in place or would be most effective in your jurisdiction?**

Examine the websites of the supervisory authority and industry associations in your jurisdiction.

7. **What actuarial resources are available to the supervisory authority in your jurisdiction?**

Consult with colleagues to determine the actuarial resources that are available to the supervisory authority. If the actuarial profession is formally established in your jurisdiction, review the website of the professional organization for information on the extent of the profession, standards of practice, and so forth.

8. **What fraudulent insurance schemes, if any, are currently issues in your jurisdiction?**

Consult with colleagues to determine whether any fraudulent insurance schemes are currently of concern in your jurisdiction.
9. What demographic underwriting considerations or rating factors are not permitted in your jurisdiction?

Examine legislation and regulations or consult with colleagues to identify any demographic underwriting considerations or rating factors that are not permitted in your jurisdiction.

10. What methods and venues do consumers in your jurisdiction have to submit complaints?

Examine the websites of the supervisory authority, industry associations, consumer protection organizations, and ombudspersons to identify the alternatives available to consumers in your jurisdiction for submitting complaints.

11. What alternative dispute resolution mechanisms are available to consumers in your jurisdiction?

Examine legislation and regulations, as well as the websites of the supervisory authority, industry associations, consumer protection organizations, and ombudspersons to identify alternative dispute resolution mechanisms available to consumers in your jurisdiction.

12. If market conduct investigations are performed in your jurisdiction, what most commonly triggers them?

Consult with colleagues to discuss the circumstances that have most commonly triggered market conduct investigations in your jurisdiction.

13. What guarantee funds, if any, exist in your jurisdiction? How are they administered and funded?

Examine the websites of the supervisory authority and industry associations in your jurisdiction to identify whether any guarantee funds exist in your jurisdiction. If they do exist, examine legislation and regulations, as well as the websites of the organizations that operate the guarantee funds, to determine how they are administered and funded.

14. Is the privacy of consumer information viewed as a problem in your jurisdiction? If so, what steps do most insurers in your jurisdiction take to protect such information from unwanted dissemination?
Consult with colleagues to identify any consumer privacy issues that might currently exist and to discuss the steps taken by most insurers in response to such issues. Examine any legislation, regulations, and guidelines that may exist in this area.

15. *Which forms of distance marketing are used in your jurisdiction and for which insurance products? What regulatory oversight exists over these sales?*

Consult with colleagues to identify forms of distance marketing that are used in your jurisdiction, the products that are marketed in this manner, and the nature of regulatory oversight. Consider whether your supervisory authority has, for example, staff that are charged with surfing the internet to identify instances in which insurers or intermediaries are marketing insurance over the internet. Examine any legislation, regulations, and guidelines that may exist in this area.

16. *Has the supervisory authority in your jurisdiction entered into any MOU with other jurisdictions? If so, to what do these MOUs pertain?*

Consult with colleagues to determine whether any MOUs exist and, if so, the main points to which they pertain.