**Part III - Section I – Appendix A**

**Frequently Asked Questions**

**Compensation Disclosure Amendment to the PLMA**

*This document has been prepared by the NAIC’s Executive Task Force on Broker Activities for informational purposes only. The following questions and answers are based on the language and development of the Compensation Disclosure Amendment to the NAIC’s Producer Licensing Model Act. This document is not intended as legislative history or to replace a state insurance department’s independent review and analysis of issues regarding the Compensation Disclosure Amendment. The contents of this document should not be interpreted as a formal opinion or policy statement of the NAIC or of any individual NAIC member or state insurance department*

**Question 1:** How has the NAIC responded to the issue of inadequate disclosure of compensation by insurance producers?

**Answer 1:** The NAIC established the Executive Task Force on Broker Activities, composed of 14 states, to develop a coordinated approach to evaluate and address the issues raised in various regulatory and law enforcement investigations of producer compensation. The Task Force immediately formulated a three-pronged action plan: (1) to amend the existing Producer Licensing Model Act (PLMA) to require greater disclosure of producer compensation information; (2) to facilitate regulatory coordination through the development of uniform “templates” for the states to use in collecting information from insurers and/or producers; and (3) to establish an online fraud reporting mechanism to allow for the anonymous reporting of “tips” of unscrupulous business practices for investigation by state insurance departments.

**Question 2:** How did the Compensation Disclosure Amendment to the PLMA evolve?

**Answer 2:** In developing the Amendment, the Task Force sought input from state insurance regulators across the country regarding possible ways to achieve greater transparency of producer compensation. An initial draft of model legislation was developed and exposed for public comment in mid-November 2004. The Task Force held numerous meetings, including two public hearings at the NAIC’s 2004 Winter National Meeting in early December. Subsequent to the public hearings, a revised draft was released for public comment. More than 100 oral and/or written comments from state insurance regulators and interested parties were considered in arriving at the final draft.

**Question 3:** Will there be further changes to the Amendment?

**Answer 3:** Yes. When the Amendment was adopted Dec. 29, 2004, the Task Force committed to giving further consideration of possible additional requirements, including but not limited to recognition of a fiduciary responsibility for producers, disclosure of all quotes received by a producer for a particular placement, and disclosures relating to producer-owned reinsurance arrangements.

**Question 4:** To whom does the Amendment apply?

**Answer 4:** The Amendment applies to all producers and their affiliates that receive any compensation from the customer for the placement of insurance or, irrespective of compensation from the customer, represent the customer with respect to that placement. In the PLMA, a producer is defined as “a person required to be licensed under the laws of this state to sell, solicit or negotiate insurance.” The PLMA goes on to define “person” to include either an individual or a business entity. For information about the definition of “affiliate,” see No. 21 below.

**Question 5:** Are any producers expressly exempt from the Amendment?

**Answer 5:** Yes. Subsection C of the Amendment expressly exempts producers, such as managing general agents, sales managers or wholesale brokers, who act only as intermediaries between an insurer and other producers. This exemption was developed because these types of producers do not have direct contact with the person involved in the purchase of insurance. In addition, Subsection C expressly exempts reinsurance intermediaries.

**Question 6:** Does the Amendment apply to producers who represent one insurer exclusively?

**Answer 6:** Yes. Such producers, commonly known as “captive agents,” are not exempt from the Amendment. However, this type of producer will typically have to comply with the disclosure requirements of only Subsection A(2), because the producer does not normally receive compensation from the customer and is appointed by the insurer the producer represents.

**Question 7:** Does the Amendment apply to independent producers?

**Answer 7:** Yes. Such producers, commonly known as “independent agents,” are not exempt from the Amendment. The disclosure this type of producer must make depends on whether the producer is appointed by the insurer the producer represents for a particular placement or whether the producer receives compensation from the customer for the placement.

**Question 8:** Does the Amendment apply to registered or licensed NASD broker/dealers?

**Answer 8:** The application of the disclosure to registered or licensed NASD broker/dealers depends on the activities of the individual broker/dealer. The disclosure requirements would apply to a broker/dealer who is licensed as a producer and engaged in the placement of insurance, such as a variable life insurance product.

**Question 9:** Does the Amendment apply to producers selling annuities?

**Answer 9:** Yes. The disclosure requirements apply when a producer receives compensation from the customer for the placement of products considered to be insurance or represents the customer with respect to that placement.

**Question 10:** Does the Amendment apply to placements of insurance in the residual market?

**Answer 10:** Yes. It is recognized that residual markets encompass placements of various types of insurance through programs established to ensure that insurance is available to individuals and businesses having difficulty obtaining coverage in the voluntary market. The Amendment does not draw any distinctions between the residual market and voluntary market based on the type or line of insurance being placed. Given the statutory nature of residual market programs, the disclosure required by the Amendment is relatively straightforward.

**Question 11:** What does the drafting note about the licensing of business entities mean?

**Answer 11:** Most states permit business entities to be licensed as producers. The drafting note is intended to encourage these states to evaluate the applicability of the Amendment to licensed business entities. States that do not require producer business entities to be licensed should adjust the language of the amendment in a manner consistent with their statutory framework, if necessary, to ensure that individual licenses make the required disclosures when compensation is made to the licensee’s unlicensed corporate employer.

**Question 12:** At what point in the placement of insurance must disclosure be made?

**Answer 12:** Pursuant to Subsection A, disclosure under Paragraph (1) or (2) must be made prior to the purchase of insurance. For disclosure to be useful to the consumer, disclosure should be made before the customer has committed to purchasing the insurance. Logistical concerns about obtaining the customer’s documented acknowledgement are addressed in Subsection D(4). See Nos. 15 and 16.

**Question 13:** Must a producer provide disclosure when servicing an existing policy, such as adding a driver to existing coverage under an auto policy or changing policy limits?

**Answer 13:** No. These types of policy changes are viewed as modifications to existing placements, which do not typically involve the customer evaluating various options for the purchase of insurance.

**Question 14:** Must a producer provide disclosure when processing a policy renewal?

**Answer 14:** Yes. A renewal is considered to be the placement of insurance. As such, if the producer is involved in the renewal process, the disclosure should be given. However, if the insurer independently generates and processes a renewal without the producer’s participation or involvement, the renewal would not trigger disclosure by the producer.

**Question 15:** How should a producer document the customer’s acknowledgement of the required disclosures?

**Answer 15:** The producer should be able to establish that: (1) the required information was conveyed to the customer on a specific date; and (2) the customer indicated his or her consent regarding the described compensation to be received by the producer or affiliate. The definition of documented acknowledgement in Subsection D(4) is intended to address the technological possibilities for obtaining the customer’s written consent.

**Question 16:** What if: (1) a producer cannot figure out his or her compensation on a particular placement; or (2) the producer believes it is too difficult to explain how the producer’s compensation is calculated?

**Answer 16:** The disclosure of compensation required by Subsection A should make the customer aware of factors and methodology used that affect the producer’s compensation. While it is not necessary to provide mathematical formulas, the appropriate disclosure is nonetheless required. If a producer is unable to provide the amount of compensation on a particular placement, the producer may accomplish this by providing specific information about compensation from the past year and any anticipated changes or a range of possible outcomes while being sufficiently specific to provide valuable information to the customer.

**Question 17:** For group insurance where a producer receives compensation from the customer or represents the customer, to whom must a producer make the required disclosures prior to the receipt of compensation from the insurer or other third party for that placement of insurance?

**Answer 17:** The producer must make the disclosures to the entity named on the policy as the group policyholder. The disclosure should be made to the person actually applying for insurance or that person’s authorized representative. A producer does not need to provide the disclosures to each individual certificate holder under a group insurance policy.

**Question 18:** Will a producer who is also an investor with an insurer and who receives stock be considered to have received “compensation from the insurer” and thus be subject to the disclosure requirements? Will an agency that has a separate, structured financial loan with a carrier for an agency acquisition or a new computer system also trigger compliance?

**Answer 18:** The intention of the disclosure is to ensure that the insurance consumer is aware of the various aspects of compensation involved in any particular insurance placement so that the consumer can make an informed decision as to whether he/she wishes to proceed with the transaction under the disclosed terms. Because of this, the disclosure should focus on “compensation from the insurer” that is related to the placement of an insurance policy. If the receipt of the stock or the structuring of the loan is connected in any manner to the placement of insurance, this should be disclosed.

**Question 19:** Will a producer who provides services unrelated to the placement of insurance be required to provide the disclosures to a customer who pays compensation to the producer for these services?

**Answer 19:** A producer may receive compensation from the customer for services unrelated to the placement of insurance without providing the disclosure as long as the producer does not receive compensation from or represent the customer with respect to the placement of insurance. For example, the receipt of compensation for the preparation of IRS Form 5500 is not related to the placement of insurance.

**Question 20:** Subsection D(3) refers to fees or expenses permitted by statute. What does this mean?

**Answer 20:** By separate law or regulation, some states permit payment for the recovery of expenses related to a specific service, such as the receipt of the cost to obtain a Motor Vehicle Report. Some states may enact the Amendment to include a specific reference to these specific laws or regulations. If the Amendment when adopted in a state includes such a statutory reference, the producer may also receive compensation from the insurer without providing the disclosure so long as the receipt of such fee does not result in any additional compensation to the producer, or the producer does not represent the customer with respect to the placement of insurance.

**Question 21:** What is the intent of the disclosures applying to an “affiliate” of the producer?

**Answer 21:** The intent of this provision is to ensure that the disclosures apply to those situations where a producer or insurer may direct a payment of compensation to another appropriately licensed affiliated entity. States that do not require producer business entities to be licensed should adjust the language of the Amendment in a manner consistent with their statutory framework, if necessary, to ensure that individual licenses make the required disclosures when compensation is made to the licensee’s unlicensed corporate employer.