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Providing Information and Value Customers Deserve • Transforming the Life Insurance Marketplace

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NAIC President Iowa Insurance Commissioner Susan E. Voss
Iowa Insurance Division
330 Maple Street
Des Moines, IA 50319-0065

Dear NAIC President Voss:

Last August, I invited your predecessor, Commissioner Jane Cline, to join my campaign to fix before year-end the life insurance industry's deplorably inadequate disclosure and problematic sales practices that are terribly costly to consumers. For background, please read my August letter and Commissioner Cline's response before reading any more of this letter. Although a few friends have with tongue in cheek good-naturedly encouraged me to declare my campaign a Complete and Total Success, I know *there is still some work remaining*, and so I am now asking you to complete it. Specifically, I am asking you to fulfill your regulatory responsibilities to enact regulations mandating appropriate life insurance disclosureⁱ, to create a new and actually useful life insurance buyer's guide, and to implement additional changes as further outlined below to enforce heretofore ignored prudent regulatory practices.

To facilitate your efforts I have recently asked the Society of Actuaries to review my policy disclosure approach and either endorse it or, if deemed necessary, sponsor a competition to see whether any available better approach exists. As you will note from the enclosed copy of my letter to the Society, I am highly confident that they will endorse my approach. While appropriate policy disclosure is an essential step in fixing the life insurance marketplace, compiling and disseminating a list of the common misrepresentations pervasively used by life insurance agents are additional imperative steps. While good disclosure will enable consumers to more readily discern the falsity in misrepresentations – a task, unfortunately, largely unsuccessfully performed by most – accessible authoritative examples of financial misrepresentations will prove to be an invaluable safeguard checklist for consumers.

The NAIC's record, I am sorry to have to say, is that state insurance commissioners have been willfully blind, deaf, and mute about the outrageous, pervasive, and terribly harmful material misrepresentations in the life insurance marketplace. That is not just my opinion, it is fact. Professor Joseph Belth whose newsletter, *The Insurance Forum*, for more than 36 years has extensively documented these misrepresentation has repeatedly stated, "The life insurance market is characterized not only by an absence of reliable price information, but also by the presence of deceptive price information....the deceptive sales practices found in the life insurance industry constitute a national scandal."ⁱⁱ

Belth is hardly alone in his criticism. Citations of other published criticisms could fill a phone book. The second sentence in the chapter on life insurance in *The Wall Street Journal's* book, *Lifetime Guide to Money*, reads, "There are lots of problems in the way it is sold." In their 2008 book, distinguished financial authors Kotlikoff and Burns state, "Life insurance agents have a well-deserved reputation for being hucksters." A must-read April, 2008 *Financial Advisor*ⁱⁱⁱ article extensively quotes fee-only advisors who have largely built their businesses around providing truthful information because policy disclosures are so inadequate and agent misrepresentations so pervasive. "This lack of disclosure is a 'sin of omission' by agents and brokers, but is really a 'sin of commission' on the part of the carriers and, indeed, the state regulators," states Advisor David Barkhausen, a former agent, attorney, and state legislator. These facts should not surprise anyone given agents' financial incentives^{iv}, the absence of readily available reliable information, and consumers' widespread insurance gullibility, ignorance, and/or misplaced trust.

Following the sales practices scandals of the 1990s, the industry created the Insurance Marketplace Standards Association (IMSA) to provide consumers and life insurers a good housekeeping seal of approval. IMSA's first principle states: "To conduct business according to the high standards of honesty and fairness and to render that service to its customers which, in the same circumstances, it would apply to or demand for itself." Given the importance of knowing the cost of any product bought, and that as the NAIC's Life Insurance Buyer's Guide states, a cash-value policy's premium is not its annual cost, how do you think agents who sell whole life explain its cost?

When I have pretended to be an ordinary consumer needing life insurance, several agents have explained whole life's costs to me as follows^v. "The insurance company says, here, we're going to calculate all the mortality factors up-front. Rather than charging you year by year for the odds of you dying, we're going to put that all into the front end and you're going to pay those expenses upfront." Another agent explained, "They have taken out all of the mortality - it's all front loaded, they front load all of the mortality charges." A third agent reiterating this one of his many deceptions stated, "Remember how I said that the mortality costs are taken out upfront." A fourth agent, boasting of his insurer's compliance – having just returned from its annual sales meeting, explained the policy's low early years' cash values by stating "one pays for the guarantees of whole life upfront." When I subsequently expressed skepticism about "paying for guarantees" during a follow-up meeting with this fourth agent and a partner/mentor he had invited to join us, the mentor somewhat haughtily dismissed his colleague's 'explanation' and, upon being informed of what I preferred about a competitor's policy, quickly suggested a different policy from their insurer that provides much better value and much larger cash-values because of its lower commissions. The partner/mentor's suggestion, however, revealed the fourth agent's untrustworthiness because in our prior meetings his colleague had emphasized and assured me that he would act as a fiduciary, which he, clearly and undeniably, had not done.^{vi} Please note that I could submit to you several additional pages of legally acceptable evidence documenting ten agents making scores of misrepresentations on a half dozen topics that comprise the main areas of misrepresentation.^{vii} Also please note: all but one of the insurers whose agents I met with were IMSA members; and that no one could brand as a rogue any of these many agents as they all are big-producing veteran agents. **I trust you can now see why I have asserted for years that IMSA is and always has been a fraud.**^{viii} **Clearly, these IMSA insurers have not only never fulfilled IMSA's first principle, but they have also failed to even alter or curtail the pervasive, egregiously harmful, and age-old agent misrepresentations.**

As you well know, life insurance regulations prohibit misrepresentation. Specifically, all information provided to consumers about a life insurance policy or annuity contract "shall be

sufficiently complete and clear so that it is neither misleading nor deceptive, nor has the capacity or tendency to mislead or deceive.” But as I think you also readily know, Alan Press, former president of NAIFA’s predecessor, has written, “They [this quoted regulation and others] have simply never been enforced.” In fact, when I recently discussed with NY state regulators whether they think that agents make accurate disclosure regarding whole life insurance policies’ costs and early years’ low cash-values, the responding regulator replied, “I doubt it,” and none of the seven other regulators in the meeting objected. I was more than just a little incredulous^{ix}; after a long silence the discussion returned to our agenda’s topic. No testimony during our industry’s 1906 Armstrong hearings or the 1933 Pecora hearings that forever changed the securities industry exhibited any more shocking regulatory indifference regarding marketplace dishonesty and negligent enforcement. While it is understandable that evidence of pervasive market misconduct can be discomfiting to regulators, regulators still have an obligation to perform their duties. Please let me be explicit: these and many other similar facts, I contend, show unequivocally that insurance commissioners have not done essential basic tasks of their jobs, they have failed to provide appropriate policy disclosure, a fundamental regulatory responsibility, and they have never effectively enforced industry regulations^x.

Just as there is no joy for most who try working as agents^{xi} in the dysfunctional insurance marketplace built without the necessary regulations and enforcement, there is no joy for me in telling you these truths. With respect to these enforcement failures, failures certain to one day be legendary, Kenneth Mann’s seminal book^{xii} on white collar crime offers the following insightful explanation: “When inculpatory information is embedded in normal social life, that is, when it is not easily identifiable as potential evidence, there is a high probability that the government will not identify it.” Indeed, many misrepresentations regarding life insurance are supported by myths and financial misconceptions that abound in our culture, largely verbally these days as insurers have purged their sales and marketing literature following the 1990s sales misconduct scandals. Perhaps one of the all-time best examples of such, and one still very widely relied upon by agents selling whole life, can be found in the NAIC’s original Life insurance Buyer’s Guide that states there are two types of life insurance term and whole life – a misleading dichotomy terribly inadequately explained, as I’ve written about in several articles, including one in 2002 in the NAIC’s own *Journal of Insurance Regulation*.^{xiii} A recent example of the abounding misconceptions – and shocking because it actually appears in print, hence observable by all - is a *National Underwriter* article written by a life insurer’s Senior Marketing Communications Specialist who states, “In fact, whole life insurance actually can get less expensive the longer the policyholder holds the policy because the increase in guaranteed cash values and nonguaranteed dividends often exceeds the premium after a few years.”^{xiv} Another likely explanation of enforcement failures, as the Madoff whistleblower Harry Markopolos repeatedly demonstrated regarding the SEC – long, but apparently quite erroneously, considered the bastion of regulatory excellence - is that the ranks of financial regulators are almost entirely filled with individuals who have neither the real financial expertise nor the actual meaningful marketplace experience and knowledge to conduct effective enforcement.

Insurance commissioners, of course, are not the only party to have failed. Consumerists have woefully failed^{xv} in the ineffectiveness of their advocacy; after all, as Belth has stated “the solution to the problem of deceptive practices in the life insurance industry lies in disclosure.” Neither consumerists nor financial journalists, though, have ever properly pursued Belth’s recommendation^{xvi}. Insurance professors treat the subjects of life insurance disclosure and misrepresentation as the third rail to any consulting assignment, have never engaged, aided, or when necessary corrected Belth, and when broaching these subjects have functioned as industry lackeys^{xvii}.