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Misrepresentation and ignorance: A dangerous blend for ethics

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Questionable marketing practices are one of the most common ways agents and advisors can run afoul of ethical business standards, leading not only to angry and litigious clients, but also to regulatory action that could result in fines, suspensions, termination or the loss of a license.

There are a number of agent or insurer marketing practices that are considered unfair, unethical or deceptive. Among the most prevalent are problems like the misrepresentation of products or services in marketing, advertising or sales efforts, and a lack of knowledge or skills to competently identify the client's needs, and recommend and properly explain products that fit those needs.

"Many financial products these days are highly complicated instruments that virtually defy explanation to the average consumer," said William K. Bridgers, whose eponymous insurance consulting company is based in Pleasant Grove, Utah. "The advisor or agent may be very honest but only has as much information as is revealed in the sales material or a wholesaler's presentation. The point is, whether misrepresentation is calculated, due to ignorance or lack of training, the effect is the same: a confused and/or angry client."

David H. Kinder, ChFC, a wealth and retirement specialist in Riverside, Calif., says he has recently taken particular notice of a few issues related to misrepresentation. One is the way agents and advisors represent living benefit riders on annuities. Also known as guaranteed lifetime withdrawal benefits (GLWB) or guaranteed lifetime income benefits (GLIB), these options typically are added to annuities as riders. They aren't always easy to explain to clients.

"It's easy to misunderstand them, and it's very easy for clients to misunderstand

agents as well," Kinder said. "Clients think they are earning 7 percent per year as a rate of return [as an example] for up to 10 years, and then they can walk away with that money. That's not the way the rider works. Yet, I know of a couple of agents that have been promoting such riders exactly like that. And that's a problem."

Kinder adds that it's bad enough that clients have selective memories, but if agents and advisors are not crystal clear, or even create their own disclosures or explanations of how an annuity rider works, it can come back to haunt them.

Explaining IUL

Another area of concern for Kinder is a lack of full disclosure on how Indexed Universal Life policies work. "I love IUL, but having been securities licensed, I also know the inherent risks within the product. I'm sorry, but even with new NAIC guidelines coming out, IUL will not guarantee a 7 percent per year return, every single year, for the life of the product. Some companies allow the agent to vary the crediting interest rate year-to-year, and I think that's good," Kinder said.

The new NAIC guidelines, set to take effect Sept. 1, are intended to solve a longstanding problem regarding a lack of uniformity in how carriers and agents illustrate the potential performance of IUL policies and how hypothetical historical index returns are calculated.

IUL can be a great product for the right client, but the many moving parts inherent in IUL policies have long been a source of confusion for many agents and consumers alike. An agent who is not sufficiently up to speed on how IUL works obviously will have trouble explaining the product to a client, which could result in the selection of an unsuitable product for that particular client's circumstances.

Kinder also notes that IUL policies require ongoing service and reviews. If an agent isn't going to stay in the business, it's a real disservice to those to whom that agent has sold service-intensive programs.

Whole life dividend rates

A third issue Kinder mentions is how agents describe whole life dividend rates. "Companies put out an ad in *The Wall Street Journal* saying '7 percent dividend,' and now agents are saying that their policies are paying 7 percent. No, that's not how a dividend works. A dividend is not a rate of

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return on the cash values of the policy. Dividends are a surplus of earnings distributed to their mutual policy shareholders," he said. "Agents should not be connecting the insurance company dividend to individual policy performance ... but it happens all the time."

Two root causes of misrepresentation

Bridgers said two problems cause most cases of misrepresentation:

"One: faulty sales materials from the carrier that position the product in a number of particular situations in which the product would be very unlikely to be suitable, leading the sales professional to make recommendations that are figuratively speaking trying to fit a square peg into a round hole," he said.

"Two: pressure to sell. Intentionally misleading the client, in my experience, is rare. However, when it happens, it is definitely due to a matter of compensation and a complete lack of integrity on the part of the sales agent or sales manager. Getting the sale is the primary motivator," Bridgers said. "This typically happens when a big case is involved, the prospects are older, there has been no comparison of products or second opinions sought from other advising professionals, and the sale is critical in meeting or exceeding branch sales goals."

Kinder said advisors might stumble into ethical trouble when they aren't able to see enough people on a favorable basis, and that is often because they haven't been well trained to help clients solve their problems.

"Zig Ziglar said, 'If you help enough people get what they want, you can have everything you want.' That's my personal philosophy toward my life and this business," Kinder says. "While sometimes there are well-meaning and well-intentioned advisors who end up swindling their clients unintentionally, ignorance is not bliss in this business."