



# State Licensing Handbook

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2020

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National Association *of*  
Insurance Commissioners

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**2020**



National Association of  
Insurance Commissioners

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All of the references to the Producer Licensing Working Group and Task Force will show that both have changed parent committees since the creation of the State Licensing Handbook. The change in parent committees has not changed the role for the Working Group and the Task Force.

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## Introduction

The National Association of Insurance Commissioners NAIC is the U.S. standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states and five U.S. territories. Through the NAIC, state insurance regulators establish standards and best practices, conduct peer review, and coordinate their regulatory oversight. NAIC staff support these efforts and represent the collective views of state insurance regulators domestically and internationally. NAIC members, together with the central resources of the NAIC, form the national system of state-based insurance regulation in the U.S.

The NAIC has organized its work into various task forces and committees. The Executive (EX) Committee has working groups and task forces that focus on specific issues. In 2009, the NAIC formed the Producer Licensing (EX) Task Force to coordinate and oversee all NAIC groups addressing producer issues. One of the working groups that formerly reported to the Market Regulation and Consumer Affairs (D) Committee and now reports to the Producer Licensing (EX) Task Force is the Producer Licensing (EX) Working Group.

As its name suggests, the Producer Licensing (EX) Working Group focuses its efforts on the licensing process for individuals who sell insurance products. The Working Group has worked toward the goal of streamlining and achieving uniformity in the insurance producer licensing process. The purpose of the *State Licensing Handbook* (Handbook) is to document current guidelines and recommended best practices.

The Working Group strongly encourages all states, districts and territories to adopt, without deviation, all provisions of the NAIC's *Producer Licensing Model Act* (#218), because true uniformity cannot be achieved until that happens.

Part I of this Handbook contains background information on these efforts and current information on the implementation of Model #218, reciprocity efforts, the Uniform Licensing Standards (ULS), and related topics.

Part II of this Handbook includes information on other types of licenses that some states issue and a state licensing director may encounter.

Part III contains Appendices to this Handbook.

The NAIC and the Working Group worked to achieve reciprocity, as required by the initial provisions of the federal Gramm-Leach-Bliley Act (GLBA) and 15 U.S.C. § 6751 et seq., adopted in 1999, and create and implement the ULS and procedures in all states. In 2015, the provisions of the GLBA that prohibited the creation of the National Association of Registered Agents and Brokers (NARAB) were repealed, and NARAB was established. This Handbook contains the current recommendations and guidelines from the NAIC's Executive (EX) Committee, the Producer Licensing (EX) Task Force, and the Producer Licensing (EX) Working Group.



**Part I              Insurance Producer Licensing**

**Section A        Governing Principles**

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## Chapter 1

### Modern Producer Licensing

The process for licensing insurance producers has had numerous phases. The first NAIC model on this subject was the NAIC *Agent and Broker Model*. The next phase was the NAIC *Single License Procedure Model*. Although development of the newest model began in the late 1990s, it was the U.S. Congress' (Congress') passage of the Gramm-Leach-Bliley Act (GLBA) in 1999 that caused the NAIC to speed up the development of the *Producer Licensing Model Act* (#218).

#### Uniformity Provisions of the GLBA Adopted in 1999

In order to achieve the licensing uniformity standards of the GLBA, a majority of the states had to satisfy all five of the following requirements:

1. Adoption of uniform criteria regarding a producer's integrity, personal qualifications, education, training and experience, which must include qualification and training on the suitability of products for a prospective customer.
2. Adoption of uniform continuing education (CE) requirements.
3. Adoption of uniform ethics course requirements in conjunction with other CE requirements.
4. Adoption of uniform suitability requirements based on financial information submitted by the customer.
5. Elimination of nonresident requirements posing any limitation or condition because of the place of the producer's residence or business, except for countersignature requirements.

One of the major provisions of the GLBA was a provision to create the National Association of Registered Agents and Brokers (NARAB). While much progress was made to improve uniformity and streamline nonresident producer licensing, the NAIC endorsed the provisions of the Terrorism Risk Insurance Program Reauthorization Act of 2015 (Public Law 107-297), which modified NARAB. These provisions, commonly referred to as NARAB II, were signed by President Barack Obama on Jan. 12, 2015.

NARAB II is intended to streamline the nonresident producer licensing process while preserving the states' ability to protect consumers and regulate producer conduct. NARAB II does not create a federal insurance regulator but establishes a nonprofit corporation, known as NARAB, controlled by its board of directors. The stated purpose of the legislation is to provide "a mechanism through which licensing, CE, and other nonresident insurance producer qualification requirements and conditions may be adopted and applied on a multistate basis without affecting the laws, rules and regulations, and preserving the rights of a state, pertaining to certain specific producer-related conduct."

NARAB is to be governed by a 13-member governing board comprising eight state insurance commissioners and five insurance industry representatives subject to presidential appointment and U.S. Senate (Senate) confirmation. NARAB, acting through its board of directors, will establish membership criteria through which producers can obtain nonresident authority to sell, solicit or negotiate insurance. Satisfaction of membership criteria means a producer can sell, solicit or negotiate insurance (and perform incidental activities) in any state for which a producer pays that state's licensing fee for any line(s) of insurance for which the producer is licensed in the home state. NARAB membership is not mandatory for producers.

The law preserves the rights of a state pertaining to resident licensing and CE, the supervision and enforcement of conduct, and disciplinary actions for nonresident producers; and it leaves a state's full range of authorities for resident producers intact. Model #218 also includes important disclosures to the states, addresses business entity licensing, and protects state revenues.

Through the efforts of the Producer Licensing (EX) Task Force and the Producer Licensing (EX) Working Group, the NAIC monitors state compliance with reciprocity guidelines. The NAIC also set a goal to create uniform licensing practices. The Working Group has adopted a number of Uniform Licensing Standards and guidelines, and it continues to strive toward a more efficient licensing system among the states.

## National Insurance Producer Registry

The NAIC has long advocated for increased use of technology to streamline licensing processes. In 1996, the NAIC collaborated with industry to create the Insurance Regulatory Information Network (IRIN) as a nonprofit affiliate of the NAIC. In 1999, the organization changed its name to the National Insurance Producer Registry (NIPR). The purpose of the NIPR is to work with the states and the NAIC to re-engineer, streamline, and make more uniform the producer licensing process for the benefit of state insurance regulators, the insurance industry, and consumers. NIPR worked with the NAIC to develop and implement: 1) the Producer Database (PDB), which includes licensing information from 50 states, Washington, DC and Puerto Rico, utilized by the industry for licensing and appointment information; and 2) the State Producer Licensing Database (SPLD) for use by state insurance regulators.

The states use NIPR to link state insurance departments with the entities they regulate. Applicants and licensees can transmit licensing applications, insurers can transmit appointments and terminations, and both can transmit other information to state insurance regulators in multiple states, thereby creating electronic solutions that are easy and efficient to use by the states and industry.

Additionally, using the subsequent launch of the Attachment Warehouse, an applicant who answers “yes” to any background question on the NAIC Uniform application can submit the required supporting documentation at the time he or she is applying for or renewing a license. The submission of a document to the Attachment Warehouse will trigger an email alert to the appropriate state(s) notifying the state(s) that supporting documentation has been submitted to fulfill document requirements pertaining to the “yes” answer on the background. The advantage to the producer and the state(s) is that the documentation can be sent to the Attachment Warehouse once, and all appropriate states will be notified and have the ability to view, download or print the document. The Attachment Warehouse also allows a producer to meet the requirement from the states to report and submit documentation related to any regulatory action taken against him/her. This enables the producer to meet this regulatory obligation quickly in order to comply with the typical state requirement for producers to report an action within 30 days. Through the use of the Attachment Warehouse, all states in which the producer is licensed are notified with an email alert and have access to the document.

A complete list of jurisdictions using NIPR products and services is available at [www.nipr.com](http://www.nipr.com). The website has an updated list of the states that are making active use of NIPR electronic processing. (Product List by State)

## Chapter 2

### ***Producer Licensing Model Act***

#### **Uniformity Provisions of the *Producer Licensing Model Act***

Through the *Producer Licensing Model Act* (#218), the NAIC created a system of reciprocity for producer licensing and established uniform standards in key areas of producer licensing. Model #218 was initially adopted in January 2000. It was subsequently amended in October 2000 and in January 2005.

In December 2002, the Producer Licensing (EX) Working Group adopted a set of Uniform Resident Licensing Standards (URLS). In December 2008, the standards were revised and updated to incorporate standardization and uniformity for both resident and nonresident licensing. Therefore, the standards were renamed the Uniform Licensing Standards (ULS). Model #218 and the ULS are designed to complement each other and assist the states in creating a uniform system of producer licensing. In 2008, the Working Group was charged with reviewing the ULS. Subsequent revisions were made to the ULS in August 2010 (limited lines definitions) and in August 2011 (definitions for certain noncore limited lines). The revised standards are included in the Appendix, and updates can be found on the Working Group's web page on the NAIC website.

The key uniformity provisions of Model #218 are:

1. Definitions for “negotiate,” “sell” and “solicit,” and uniform exceptions to licensing requirements.
2. An application process for both resident and nonresident producer license applications that uses the NAIC Uniform Application for resident and nonresident producers.
3. Definitions for the six major lines of insurance: Life, Accident and Health, Property, Casualty, Personal Lines, and Variable Life or Annuity Products.
4. Exemptions from completing prelicensing education and examinations for licensed producers who apply for nonresident licenses.
5. Standards for license denials, non-renewals and revocations.
6. Standards regarding which individual producers and business entities may receive a commission related to the sale of an insurance policy.
7. Standards for producer appointments for states that have an appointment system.
8. Procedures for state insurance regulators, companies, and producers to report and administratively resolve “not for cause” and “for cause” appointment terminations.
9. A definition for limited lines insurance. The Working Group has adopted a recommended list of limited lines licenses, as set forth in the ULS, and it has encouraged the states to eliminate licensing categories for other lines of insurance.

#### **Other Key Provisions of Model #218**

Model #218 also contains a number of provisions that promote simplified licensing procedures.

##### *Home State*

The intent of Model #218 is for a producer to have one state of residence. Section 2(B) of Model #218 defines this concept as the home state:

“Home state” means the District of Columbia and any state or territory of the United States in which an insurance producer maintains his or her principal place of residence or principal place of business and is licensed to act as an insurance producer.”

A producer is permitted to designate either the actual state of residence or the principal place of business as the home state. Model #218 does not specifically prohibit the existence of two home state licenses. The producer may select either the resident state or the principal place of business. This option was intended to accommodate a producer who lives in one state but maintains his/her business in another state. However, it was the intent of the drafters for one state

to be designated as the home state to prevent forum shopping. The Working Group has discouraged any state from adopting a stance that a producer can maintain two home states.

#### *Change of Home State*

Under Model #218, there is now a simplified process for producers who move from state to state and were in good standing prior to the change of residence.

Section 9 of Model #218 provides a mechanism for licensed producers to maintain an active license when changing the state of residence. Section 9(A) creates an exemption from prelicensing education or examination for a producer who moves into a state who was previously licensed for the same lines of authority (LOAs) in another state. In this scenario, the producer receives a new resident license for the same LOAs, so long as the producer applies for a resident license within 90 days of the cancellation of the producer's previous license and the producer was in good standing in the prior state.

Section 9(B) creates an exemption from prelicensing education or examination for an LOA held by a former nonresident producer who moves into a state and becomes a resident of that state. In practice, when a nonresident becomes a resident, that producer is to be granted the same LOAs previously held, so long as the producer applies for a resident license within 90 days of establishing legal residence. States are not to impose prelicensing education or an examination on a nonresident producer who subsequently moves into another state and declares it to be the home state, unless "the commissioner has determined otherwise by regulation."

Under Model #218, letters of certification were eliminated as a prerequisite to granting a nonresident license. The State Producer Licensing Database (SPLD) provides verification of good standing in the producer's home state.

One unresolved issue is the long-established practice of requiring a letter of clearance for producers changing their resident state. Despite the fact that Model #218 does not contain any reference to a letter of clearance, some states still require the producer to provide a letter of clearance from the former state before the new state will grant the producer an active resident status. Other states grant the new nonresident license but continue to monitor the producer's record to make sure that the prior resident license changes in status from resident to nonresident. This is done to prevent the producer from holding two active resident licenses.

The Working Group and National Insurance Producer Registry (NIPR) have identified this as an issue that could best be resolved by the establishment of an electronic method for the producer to communicate the desired changes to all affected states in one transaction. NIPR's launch of the Contact Change Request (CCR) service allows producers for many states to change their physical addresses, email addresses, phone numbers and fax numbers. The Working Group will turn its attention to solving the issues surrounding a change of resident state once all states have fully implemented the CCR service.

#### **Commissioner Discretion**

Model #218 contains language that allows a state to adopt regulations to cover a state-specific situation. The states should carefully consider the impact that deviation from Model #218 might have on NAIC uniformity and reciprocity initiatives.

#### **Section-by-Section Summary of Model #218**

The full text of Model #218 is in the Appendices.

##### **Section 1: Purpose and Scope**

- To promote efficiency and uniformity in producer licensing.

##### **Section 2: Definitions**

- Defines the terms “home state,” “limited lines insurance,” “sell,” “solicit,” “negotiate,” and other pertinent terms.

#### Section 3: License Required

#### Section 4: Exceptions to Licensing

- Lists the persons and entities that do not need licenses, even though they participate in the insurance industry.

#### Section 5: Application for Examination

- Requires that producers must pass an examination in the LOAs for which applications are made.
- Allows the use of outside testing services to administer examinations.

#### Section 6: Application for License

- Sets forth the qualifications for licensure as an individual or business entity.
- Provides that limited line credit insurers must provide instruction to individuals who will sell credit insurance.

#### Section 7: License

- Sets forth the six major LOAs, the limited line of credit insurance, and any other line of insurance permitted under state laws or regulations.
- Provides guidelines for license continuation and reinstatement.
- Provides for hardship exemptions for failure to comply with renewal procedures.
- Lists the information the license should contain.
- Requires licensees to notify the insurance commissioner of a legal change of name or address within 30 days of the change.

#### Section 8: Nonresident Licensing

- Requires states to grant nonresident licenses to persons from reciprocal states for all LOAs held, including limited lines and surplus lines insurance, if those persons are currently licensed and in good standing in their home states.
- Requires a nonresident licensee who moves from one state to another to file a change of address and certification from the new resident state within 30 days with no fee or application.

#### Section 9: Exemption from Examination

- Exempts licensed individuals who change their home state from prelicensing and examination.
- Requires a licensed nonresident who becomes a resident to register in the new home state within 90 days of establishing legal residence, unless “the commissioner determines otherwise by regulation.”

#### Section 10: Assumed Names

- Requires a producer to notify the insurance commissioner prior to using an assumed name.

## Section 11: Temporary Licensing

- Allows temporary licensure for up to 180 days without requiring an exam when the insurance commissioner deems that the temporary license is necessary for the servicing of an insurance business in specific cases.

## Section 12: License Denial, Non-Renewal or Revocation

- Lists 14 grounds for denial, non-renewal or revocation of a producer license.
- Provides that a business entity license may be revoked if an individual licensee's violation was known or should have been known by one or more of the partners, officers or managers acting on behalf of the partnership or corporation, and the violation was not reported to the insurance commissioner nor was corrective action taken.

## Section 13: Commissions

- Prohibits payment of commissions or other compensation to or acceptance by an unlicensed person for "selling, soliciting or negotiating" insurance.
- Allows payment of renewal commissions to an unlicensed person if the person was licensed at the time of the sale, solicitation or negotiation.
- Permits payment or assignment of commissions or other compensation to an insurance agency or to persons who do not sell, solicit or negotiate, unless the payment would violate rebate provisions.

## Section 14: Appointments (optional)

- Prohibits a producer from acting as a producer for an insurer unless appointed. The insurer appoints the producer either within 15 days from the date the agency contract is executed or within 15 days from the date that the first insurance application is submitted.
- Sets forth processes for initial and renewal appointments.

## Section 15: Notification to the Insurance Commissioner of Termination

- Requires the insurer to notify the insurance commissioner within 30 days following the effective date of termination of a producer's appointment if the termination is for cause. The insurer also has a duty to promptly notify the insurance commissioner of any new facts learned after the termination. When requested by the insurance commissioner, the insurer shall provide additional information, documents, records, or other data pertaining to the termination or activity of the producer.
- If termination of a producer is not for cause, the insurer must notify the insurance commissioner within 30 days following the effective date of termination.
- Sets forth a detailed process for notifying the producer and for a producer to submit comments to the state.
- Provides that in the absence of actual malice, insurers have immunity from any actions that result from providing information required by or provided pursuant to this section.
- Contains penalties for insurers who fail to report or who report with actual malice.
- Requires that documents furnished to the insurance commissioner pursuant to this section shall be confidential and privileged.

## Section 16: Reciprocity

- A state cannot impose additional requirements on nonresident license applicants who are licensed in good standing in their home state other than the requirements imposed by Section 8 of Model #218 if the applicant's home state grants nonresident producer licenses on the same basis.
- A nonresident's satisfaction of continuing education (CE) in the producer's home state shall constitute satisfaction of all CE requirements in the nonresident state if the home state practices CE reciprocity.

## Section 17: Reporting of Actions (By Producers)

- A producer must report any administrative actions taken in another jurisdiction or by another government agency in the home jurisdiction within 30 days of the final disposition of the matter.
- A producer shall report any criminal prosecution taken in any jurisdiction within 30 days of the initial pretrial hearing date. The report must include the legal order, relevant court documents, and the original complaint.

## Section 18: Compensation Disclosure

- In any instance, when a producer will receive compensation from a customer for placing an insurance policy and will also receive compensation from an insurer for that placement, prior to placing that policy, the producer is required to disclose to the customer the amount and sources of compensation the producer will receive if the customer makes an insurance purchase.

## Section 19: Regulations

- The insurance commissioner may promulgate reasonable regulations to carry out the purposes of Model #218.

## Section 20: Severability

## Section 21: Effective Date

## Frequently Asked Questions

The Working Group has created several documents that answer frequently asked questions (FAQ) about reciprocity, uniformity, and how to administer Model #218. The current version of the FAQ, as of the publication date, appears below. The latest version of these documents can be found on the Working Group's web page on the NAIC website.

### ***Model #218 Implementation - FAQ***

*This document has been prepared by the Working Group for informational purposes only. The following questions and answers are based upon the language of Model #218. This document is not intended as legislative history or to replace a state insurance department's independent review and analysis of these questions. The contents of this document should not be interpreted as representing the views or opinions of the NAIC or of any individual NAIC member or state insurance department.*

**Question 1:** Is Section 14 of Model #218 regarding appointments, which is labeled "optional," intended to be optional for adoption by a state that requires insurer appointments of producers?

**Answer 1:** No. If a state requires appointments, it should adopt Section 14. It was labeled "optional" only to accommodate those states that do not require appointments (e.g., Colorado).

**Question 2:** Model #218 Section 14B starts a clock of 15 days for insurer compliance by providing, “the appointing insurer shall file ... within 15 days from the date the agency contract is executed or the first insurance application is *submitted*” (emphasis added). When is an application deemed “submitted?”

**Answer 2:** An application is *submitted* when it is dated received by the insurer. The use of any other event will undermine the ability of the states and insurers to achieve uniform national practice for regulatory notifications. This is because any other temporal event is unknown to the insurer, which has the compliance responsibility. That is, “submitted” should not mean when a producer mails an application, since different producers might use different means of communicating applications; different producers will mail applications at different times; mail pick-up and delivery varies among localities; etc. The one certain time of submission is when the application is dated received by the insurer.

**Question 3:** If a state adopts Model #218 Section 14, is there an option for the state to require an insurer to execute an agency contract with a producer prior to accepting the first insurance application from a producer that has not yet been appointed?

**Answer 3:** No. Model #218 Section 14B provides, “the appointing insurer shall file, in a format approved by the insurance commissioner, a notice of appointment within 15 days from the date the agency contract is executed **or** the first insurance application is *submitted*” (emphasis added). The use of the word “or” in the model clearly allows an insurer to notice appointment upon the earliest of the two events. Pennsylvania has adopted modified language and is not in complete agreement with this answer.

**Question 4:** Since Model #218 works toward uniform national procedures by eliminating the traditional distinctions between agents and brokers for the purposes of licensure, is it appropriate to require appointments of producers acting as brokers?

**Answer 4:** No. Model #218 Section 14A makes clear that an insurer need only appoint producers “*acting as agents on behalf of the insurer*.” Inasmuch as brokers are not appointed, notification of appointments of brokers is not required.

**Question 5:** Must a business entity reside in a state to obtain a producer license?

**Answer 5:** No. Section 8 outlines the requirements that a person must fulfill in order to obtain a nonresident license, and the definition of “person” (see Model #218 §2L) makes it clear that this section applies to the licensing of both individuals and business entities. Section 8 is devoid of any residency requirement, and a nonresident business entity should be able to obtain a nonresident producer license, if business entities are required to be licensed by the insurance department at all. In addition, the states that impose residency requirements on business entities are likely not compliant with the National Archives and Records Administration (NARA) provisions of the Gramm-Leach-Bliley Act (GLBA).

**Question 6:** Should the record of producer qualifications obtainable from the NIPR SPLD satisfy all certification requirements for state licensing?

**Answer 6:** Yes. Model #218 Section 7G, Section 8B and Section 9 make it clear that the states should adopt and use the SPLD record for all regulatory purposes.

**Question 7:** Should a state require that a resident be licensed as a producer if he or she is entitled to renewal or other deferred commissions produced in another state?

**Answer 7:** No. Model #218 Section 3 and Section 13C indicate that a producer license is required to sell, solicit or negotiate the sale of insurance but do not suggest that a license is needed after such activity has ceased. The person’s receipt of renewal or other deferred commissions does not result in any licensing requirement.

**Question 8:** Are insurers alone responsible for educating those persons who sell limited lines credit insurance products?

**Answer 8:** Yes. Model #218 Section 6D requires such insurers to furnish the program of instruction to those who sell limited lines insurance. The program is filed with the insurance commissioner in most states.

**Question 9:** Does reciprocity pursuant to Section 8 of Model #218 require recognition of a nonresident LOA when the state in which the nonresident license is sought does not recognize an LOA for resident producers?

**Answer 9:** Yes. For example, the reciprocity mandates of Section 8E should be respected for a limited LOA, as is the case with any other LOA. Consequently, the states should be prepared to recognize the authority on a nonresident basis.

**Question 10:** What process is to be followed by a producer in identifying a new “home state” without the loss of his or her license to do business in the prior home state?

**Answer 10:** The producer should notify the prior home state of his or her change of address and intent to apply for a resident license in the new home state. The producer must apply for resident license in his or her new home state. Pursuant to Section 9 of Model #218, the producer or applicant is not required to complete any prelicensing education or examination in order to secure the new resident license.

**Question 11:** What process is to be followed by the new home state insurance regulator with regard to a producer changing his or her state of residency?

**Answer 11:** The new home state should process the producer’s application; issue a resident license if warranted; and, if issued, notify the SPLD of the producer’s new status as a resident licensee.

**Question 12:** What is the process to be followed by the prior home state insurance regulator?

**Answer 12:** At the time the producer notifies the prior home state insurance regulator of a change of address, the prior home state insurance regulator should send a report of “active with notice of transfer of residency to [the new home state]” to the SPLD identifying the new state of residency. Upon Producer Database (PDB) notification of the new resident state licensure, the prior home state resident license is replaced with a nonresident license for the duration of its term. It is noted that time frames for notice to the states of a change in address are stated in Model #218.

**Question 13:** If a commission is paid to enroll a customer in a group credit insurance policy, must the enroller be licensed?

**Answer 13:** Yes. An individual who enrolls customers under a group insurance policy must obtain a limited lines license if a commission is paid. Model #218 Section 4B(2) provides an exception from licensing if no commission is paid to the enroller and the enroller does not engage in selling, soliciting or negotiating.

**Question 14:** May an individual sell, solicit or negotiate group credit insurance coverage without a license?

**Answer 14:** No. An individual must have a limited lines license before he or she can sell, solicit or negotiate the purchase of group insurance. While Model #218 Section 4B(2) provides an exception for securing and furnishing information in connection with group insurance coverage, there is no such exception from licensing for selling, soliciting or negotiating group insurance coverage.

**Question 15:** Can a person enrolling someone in a group insurance policy secure and furnish information about the policy to a customer and still be exempt from licensure?

**Answer 15:** Yes. As set forth in Section 4B(2) of Model #218, there is an exception that allows a group enroller to secure and furnish information about the group insurance policy to a customer, provided no commission is paid or there is no selling, solicitation or negotiation. However, Section 4B(2) generally recognizes an exception for the purposes of enrolling individuals under plans, issuing certificates under plans, assisting with the administration of plans, and performing administrative services related to the mass marketing of property/casualty (P/C) insurance.

Note: It is important to note that individual state laws and factual circumstances will control in determining whether an activity involves selling, solicitation or negotiation. Likewise, the states will have discretion in interpreting what activities constitute the “securing or furnishing” of information.

**Question 16:** With regard to products sold by life insurers, does the qualification in Model #218 that a person shall not sell, solicit or negotiate insurance “in this state” without a license mean that the producer must be licensed in the state(s) where the: 1) sale, solicitation or negotiation occurs; or 2) policyholder principally resides?

**Answer 16:** In those states that have adopted Model #218, licensure should be based upon where a producer “sells, solicits or negotiates” insurance, as specifically stated in Model #218. In traditional insurance sales transactions, licensure should be determined solely by this Model #218 standard without reference to the state of residence of the insured. Application of the “sells, solicits or negotiates” standard where an insurance transaction takes place purely by electronic or telephonic means is more complex. In such transactions, application of the Model #218 licensure standard should turn on the state of residence of the customer.

**Question 17:** Section 14B of Model #218 states: “To appoint a producer as its agent, the appointing insurer shall file, in a format approved by the insurance commissioner, a notice of appointment within 15 days from the date the agency contract is executed or the first insurance application is submitted.” In a situation in which a producer is not currently appointed by an insurer, but was previously appointed by and submitted an application to that insurer, must that producer now obtain a new appointment before submitting a new application to that insurer because it would not be the first application the producer ever submitted to that insurer?

**Answer 17:** No. Section 14B of Model #218 requires appointment within 15 days of the date an insurer receives the first application submitted by a producer who is not currently appointed, even if that producer was previously appointed by that insurer and submitted business in the past. Reference to the agency contract or the first application is based on the current time period. If a producer’s prior appointment with the insurer was terminated, each jurisdiction would consider the time period to start again with the new contract execution or the time period when the agent submits his first insurance application following the prior termination.

## Chapter 3

### Uniform Licensing Standards

In 2002, the Producer Licensing (EX) Working Group adopted the Uniform Resident Licensing Standards (URLS). The standards were revised and updated to incorporate standardization and uniformity for both resident and nonresident licensing. The standards were renamed to the Uniform Licensing Standards (ULS) in 2008. These standards will be referenced throughout this Handbook. The full text of the ULS is in the Appendices. The latest information can be found on the Working Group's web page on the NAIC website.

These standards establish an important baseline to assure state insurance regulators that all states are applying the same standards to resident applicants. The Working Group monitors compliance with the uniform standards. Since the adoption of the ULS, the Working Group has adopted interpretative guidelines and clarifications to further explain the proper implementation of the ULS.

The ULS contain guidelines in the following categories:

1. Licensing qualifications.
2. Prelicensing education training.
3. Producer licensing test.
4. Integrity/personal qualifications/background checks.
5. Application for licensure/license structure.
6. Appointment process.
7. Continuing Education (CE) Requirements.
8. Limited lines uniformity.
9. Surplus lines standards.
10. Commercial line multistate exemption standard.
11. Commission sharing.

### Initial and Renewal Producer License Applications

The Working Group has adopted initial and renewal NAIC Uniform Applications for resident and nonresident individuals and business entities. Under the ULS, the states are directed to use the Uniform Applications rather than state-specific applications. The Working Group has established a schedule for review and update of the applications. The states are encouraged to use the most current form of the Uniform Applications. The forms are available on the NAIC website. All NIPR online applications use the most recent approved uniform initial and renewal application forms.

#### Recommended Best Practices for State Insurance Regulators

- Conduct a regular review of state business rules, as well as any state-specific requirements for paper and electronic applications that are posted on NIPR's website, with NIPR or another vendor to maintain compliance with reciprocity and the ULS.
- Consider whether existing business rules are statutorily required. To the extent they are not statutorily required, they should be removed. To the extent they are statutorily required, the state licensing director should consider whether they are necessary. To the extent they are not necessary for consumer protection, the insurance commissioner should take steps to attempt to have such statutory requirements repealed (e.g., sponsor legislation).
- Carefully consider whether licensing staff should be given authority to change internal business rules or give direction to a vendor without the licensing director's approval. A change in procedure that may seem to be appropriate could cause problems with reciprocity or the ULS.
- If a state uses an outside vendor to receive and process license applications, monitor the vendor to ensure that applicants are provided only the most current NAIC uniform application, whether the applicant applies or renews online or via paper application.

- Adapt the department website to direct applicants to a single electronic location to obtain the most current version of the NAIC uniform forms, or specifically to the link for the electronic process.
- Departments should encourage the use of electronic processes, when available, rather than paper processes to expedite the licensing process.
- Eliminate all state-specific application forms and use only the most recent version of the NAIC uniform forms.
- Develop a procedure manual and cross-train staff so that several personnel can perform all licensing tasks.
- Provide adequate notice of changes to licensing and appointment fee structures, as well as changes to applications and other forms required to be submitted by applicants. With regard to the transition from an old application form to a new form, the states should continue to accept original, signed applications up to a reasonable transition period beyond the inception date for the new form. Prior to the effective revision date, the state should provide adequate notice by way of email, website updates, and any other appropriate communication device to interested parties.

## Chapter 4

### Nonresident Licensing

The previous reciprocity provisions of the Gramm-Leach-Bliley Act (GLBA) adopted in 1999 required that barriers to nonresident producer licensing be eliminated. The *Producer Licensing Model Act* (#218) contains specific guidance on this issue. A producer licensed in good standing in the home state must be granted a nonresident license unless good cause for denial exists under Section 12 of Model #218.

There are four key components to licensing reciprocity:

1. Administrative procedures.
2. Continuing education (CE) requirements.
3. Elimination of any limitations on nonresident.
4. Reciprocal reciprocity.

#### *Administrative Procedures*

Under the previous administrative procedures for reciprocal licensing mandated by the GLBA, a nonresident person received a nonresident producer license if:

1. The person was currently licensed as a resident and is in good standing in the person's home state.
2. The person submitted the proper request for licensure and paid the fees required by the nonresident state's law or regulation.
3. The person submitted or transmitted to the insurance commissioner the application for licensure that the person submitted to the person's home state or, in lieu of that, a completed NAIC Uniform Application.
4. The person's home state awarded nonresident producer licenses on the same basis to residents of the state in which the applicant is seeking a nonresident license.

The states were required to license nonresident applicants for at least the line of authority (LOA) held in the home state. This was true even if the LOA held in the applicant's home state may not have precisely aligned with the major or limited LOAs in the other state. The states were not allowed to charge a licensing fee to a nonresident that was so different from the fee charged to a resident, so as to be considered a barrier to nonresident licensure. The states also were not allowed to collect fingerprints from nonresident applicants.

Section 8(C) of Model #218 makes it clear that a licensed nonresident producer who changes residency is not required to surrender the license and submit a new application. All that is required is a change of address within 30 days of the change of legal residence. The model provides that a state should not charge a fee for processing this change of address.

The reciprocity provisions of Model #218 also extend to surplus lines producers. A majority of the states treat surplus lines as a distinct license type. Persons holding surplus lines producer licenses in their home states shall receive nonresident surplus lines producer licenses, unless some other reason for disqualification exists.

A producer holding a limited line of insurance is eligible for a nonresident limited lines producer license for the same scope of authority, as granted under the license issued by the producer's home state. The nonresident state may require only what is permitted under Section 8 of Model #218 for limited lines applicants. A limited line is any authority that restricts the authority of the licensee to less than the total authority prescribed in the associated major line.

#### *Continuing Education Requirements*

Pursuant to Model #218, a nonresident state must accept the producer's proof of the completion of the home state's CE requirements as satisfaction of the nonresident state's CE requirements if the nonresident producer's home state

recognizes the satisfaction of its CE requirements imposed upon producers from the nonresident state on the same basis.

#### *Limitations on Nonresidents*

The states had to eliminate licensing restrictions that required a nonresident producer to maintain a residence or office in the nonresident state so long as the nonresident's license was from one of the U.S., Washington, DC or the U.S. territories. The National Association of Registered Agents and Brokers (NARAB) Working Group stated that it was not a violation of GLBA reciprocity requirements if a state required nonresidents to provide proof of citizenship; however, under the Uniform Licensing Standards (ULS), it is the responsibility of the resident state to verify an applicant's citizenship status.

#### *Reciprocal Reciprocity*

To comply with the reciprocal reciprocity provisions of the GLBA, a majority of the states had to meet all three of the above components and grant reciprocity to all residents of the other states who have met those components.

#### *Reciprocity Examples*

Model #218 contains specific guidance on the proper reciprocal treatment that a state licensing director should grant. This chapter contains illustrative examples of these provisions. Unless otherwise specified, these examples assume that the applicant is in good standing in the home state and has not requested a change in LOA. There are some states that did not adopt all the reciprocity standards previously required by the GLBA in 1999 and currently reflected in Model #218. The answers to the following examples will vary when a nonreciprocal state is involved. Examples also can be found in the Working Group's Frequently Asked Questions (FAQ) contained in Chapter 2.

- Example A

A producer whose home state is State A has a nonresident license from State B and State C and moves to State D as the producer's new home state.

What should happen: The producer timely files a change of address in State A, State B and State C. State A changes the license from resident to nonresident. State B and State C record a change of address. The producer should apply for a license with State D within 90 days. State D should issue the license and may not require the producer to complete either an examination or prelicensing education; State D should verify that the license was in good standing in State A via the State Producer Licensing Database (SPLD).

- Example B

A producer who holds an LOA for surety in the home state, State A, applies for a nonresident license in State B, which does not have a separate surety LOA.

What should happen: State B issues a license that has multiple LOAs, including a surety LOA that the producer holds in the home state, but the producer is limited to the surety LOA held in his or her home state.

- Example C

A producer's home state, State A, does not have a prelicensing education requirement for any LOA, and the producer holds a life insurance LOA. The producer applies for a nonresident license in a state that has a prelicensing education requirement.

What should happen: State B issues a nonresident license with the life LOA and does not require any prelicensing education before issuance.

- Example D

A producer's home state, State A, does not have a prelicensing education requirement for any LOA, and the producer holds a life insurance LOA. The producer holds a nonresident license from State B that has a prelicensing education requirement. The producer moves into that state.

What should happen: State B should issue a resident license to the producer with a life LOA and does not require prelicensing education or completion of an examination before issuance, "except where the commissioner determined otherwise by regulation" (see Model #218 Section 9B).

- Example E

A producer's home state, State A, has a prelicensing education requirement and a CE requirement that is less than the ULS, and the producer holds a life insurance LOA. The producer applies for a nonresident license in State B, which has a prelicensing requirement that matches or exceeds the ULS and a CE requirement that matches the ULS.

What should happen: State B issues the nonresident license with the life LOA and does not require the completion of either additional prelicensing education or additional CE.

- Example F

A nonresident producer applies for the variable products LOA in State A. A check of the SPLD reveals that the applicant is not licensed for variable products in the home state, State B. Upon investigation, it is learned that State B either issues life or variable as a combined LOA or has a requirement for variable products licensing, but it is not specifically tracked by the department of insurance (DOI).

What should happen: This is a challenge, as State B has failed to adopt the variable products LOA, as defined in Model #218. A second challenge is that the records on the SPLD and/or National Insurance Producer Registry (NIPR) may not accurately reflect the home state business rule. In this example, the nonresident state will have to pend the application and contact the home state to verify if the applicant is in compliance with the home state law on variable products. The nonresident state must then decide if the applicant should be granted a license.



**Part I              Insurance Producer Licensing**

**Section B          Licensing Processes**

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## Chapter 5

### Activities Requiring Licensure

#### License Required to Sell, Solicit and Negotiate

The *Producer Licensing Model Act* (#218) uses three key words to determine when a person is required to have an insurance producer license:

“Sell” means to exchange a contract of insurance by any means, for money or its equivalent, on behalf of an insurance company.

“Solicit” means attempting to sell insurance or asking or urging a person to apply for a particular kind of insurance, from a particular company.

“Negotiate” means the act of conferring directly with, or offering advice directly to, a purchaser or prospective purchaser of a particular contract of insurance concerning any of the substantive benefits, terms or conditions of the contract, provided that the person engaged in that act either sells insurance or obtains insurance from insurers for purchasers.

The specific requirement to hold a license is found in Section 3 of Model #218 and reads as follows:

A person shall not sell, solicit or negotiate insurance in this state for any class or classes of insurance, unless the person is licensed for that line of authority in accordance with this Act.

The Producer Licensing (EX) Working Group clarified in 2006 that in traditional life insurance sales transactions, licensure should be determined solely by Model #218’s “sells, solicits or negotiates” standard, without reference to the insured’s state of residence. The key is to determine if the producer was properly licensed in the state in which the activity requiring a license took place. See also FAQ Number 16 in Chapter 2.

During the drafting of Model #218, there was considerable discussion about who should be required to hold an insurance producer license. Prior to the adoption of Model #218, the Working Group discussed guidelines for “licensable” and “non-licensable” activities. The main thrust of that effort was to distinguish acts that constitute the sale, solicitation or negotiation of insurance from administrative or clerical acts. The guidelines document gives numerous examples of “Agent” activities that do require an insurance producer license and “Clerical” activities that do not. The document is included in the Appendices. Check the Working Group’s web page for any updates.

### Commissions

Section 13 of Model #218 provides guidance regarding the relationship between being licensed and receiving commissions. Section 13(A) prohibits the payment of commission to a person who is required to be licensed. Section 13(B) prohibits a person from receiving a commission if that person was unlicensed and was required to hold a license under the model.

Section 13(C) of Model #218 states that it is not necessary, nor should any state require a producer, to maintain an active license solely to continue to receive renewal or deferred commissions.

Section 13(D) of Model #218 provides that an insurer or a producer licensed in a state may assign commissions, services fees, brokerages or similar compensation to an insurance agency (business entity) or to persons (individuals) who are not selling, soliciting or negotiating in that state and who are not licensed in that state. For example, if a regional manager in State A is, by contract with an insurer, to receive an override commission on all sales activities from subagents located in State B and State C, but the manager does not engage in any activity that would require

licensure under Section 3 of Model #218, no license should be required by State B or State C in order for the manager to receive commission payments.

Another example: A trade association with members in all states is headquartered in State A. An insurer pays a fee to the association for each member who purchases insurance from that insurer through an affinity marketing program. The association does not have to be licensed in any state because the association does not sell, solicit or negotiate insurance.

In 2008, the Working Group provided guidance on uniform interpretation of the commission sharing provision in Model #218 and recommended that adoption of Section 13 be included in the ULS. The Commission Sharing guidance document is included in the Appendix of this Handbook.

### **Exceptions to Licensing**

Model #218 contains two key sections that clarify when a license is not required. When considering whether to require a license, the states should carefully review Section 4 and Section 13 of Model #218.

Section 4 of Model #218 contains a specific list of exceptions from the licensing requirement. The states should take special note of Section 4(B)(6), which provides an exception for producers placing commercial insurance for a multistate risk with an incidental exposure in several states. As the section provides, in this situation a license is only required in the state where the insured maintains its principal place of business and the contract of insurance insures risks located in that state.

The following is a summary of types of persons and entities that are exempted from licensing:

1. An officer, director or employee of an insurer or insurance producer, provided that the officer, director or employee does not receive any commission on policies written or sold to insure risks residing, located or to be performed in the state.
2. A person who secures and furnishes information for, or enrolls individuals in, group life insurance, group property/casualty (P/C) insurance, group annuities, or group or blanket accident and health insurance.
3. An employer or association; its officers, directors and employees; or the trustees of an employee trust plan.
4. Employees of insurers or organizations employed by insurers who are engaging in the inspection, rating or classification of risks.
5. A person whose activities in a state are limited to advertising without the intent to solicit insurance in that state.
6. A person who is not a resident of a state who sells, solicits or negotiates a contract of insurance for commercial P/C risks to an insured with risks located in more than one state insured under that contract.
7. A salaried, full-time employee who counsels or advises the employer relative to the insurance interests of the employer.

#### **Recommended Best Practice for State Insurance Regulators**

- For uniformity purposes, states that still use a “transaction-based licensure” approach should eliminate that standard and change to the Model #218 standard.

## Chapter 6

### Prelicensing Education

Prelicensing education is required in some states as a condition of licensure for resident insurance producers. Neither the *Producer Licensing Model Act* (#218) nor the Uniform Licensing Standards (ULS) suggests that a state must have a requirement for prelicensing education. States that have a prelicensing education requirement should follow the uniform standards as adopted by the Producer Licensing (EX) Working Group.

The ULS set a minimum credit hour requirement for prelicensing education. In 2010, the Working Group was charged with reviewing this standard. Updated information, if there are any changes to this standard, can be found on the Working Group's web page.

States that require prelicensing education shall require 20 credit hours of prelicensing education per major line of authority. The states must accept both classroom study and verifiable self-study, which includes both text and online courses. The ULS does not have a limit on the number of credits that can be obtained by self-study. The states shall independently determine the content requirements for prelicensing education. The ULS require that a state have a method to verify completion of prelicensing education, but they do not prescribe a method.

The ULS provide that a person who has completed a college degree in insurance shall be granted a waiver from all prelicensing education requirements. The ULS also provide that individuals holding certain professional designations approved by the insurance department should be granted a waiver from the prelicensing education requirement. In 2008, the ULS were updated to indicate that the following list of designations be provided as guidance for designations that would waive prelicensing education, but the list is not exhaustive:

Life: CEBS, ChFC, CIC, CFP, CLU, FLMI, LUTCF

Health: RHU, CEBS, REBC, HIA

Property/Casualty (P/C): AAI, ARM, CIC, CPCU

Under both reciprocity standards and the ULS, no state shall require prelicensing education for nonresident applicants or nonresident producers who change their state of residency.



## Chapter 7

### Application Review for Initial Licenses

#### Individual Application Forms

The Producer Licensing (EX) Working Group adopted a uniform application, and the Uniform Licensing Standards (ULS) require its use for all producer applicants. Section 6 of the *Producer Licensing Model Act* (#218) outlines the process a state is to follow in reviewing the application and making the determination as to whether to grant a resident producer license.

Before issuing a resident producer license to an applicant, the state must find that an applicant for a resident license:

1. Is at least 18 years of age.
2. Has not committed any act that is a ground for denial, suspension or revocation set forth in Model #218 Section 12.
3. Where required by the insurance commissioner, has completed a prelicensing course of study for the lines of authority (LOAs) for which the person has applied.
4. Has paid the appropriate fees.
5. Has successfully passed the examinations for the LOAs for which the person has applied. Note that the ULS provide that examinations are not generally required for limited lines, but it is acceptable for examinations for areas such as crop and surety.

#### Business Entity Applications

The following requirements are optional and would apply only to those states that have a business entity license requirement.

The Working Group adopted a uniform application form for business entities, and the ULS require its use. Section 6 of Model #218 requires that before approving an application for a resident business entity, the state shall find that:

1. The business entity has paid the appropriate fees.
2. The business entity has designated a licensed producer responsible for the business entity's compliance with the insurance laws, rules and regulations of the state.

Section 6 also gives the insurance commissioner authority to require any documents necessary to verify the information contained in an application. In 2010, the Producer Licensing (EX) Task Force considered methods to expedite and streamline business entity licensing. Updated proposals can be found on the Working Group's web page.

#### Background Checks

The Gramm-Leach-Bliley Act (GLBA) allows the states to perform criminal background checks on resident applicants. The ULS contain guidelines on how to perform background checks, including the following three-step process for background checks:

- A. The states will ask and review the answers to the standard background questions contained on the Uniform Applications.
- B. The states will run a check against the NAIC Regulatory Information Retrieval System (RIRS)/State Producer Licensing Database (SPLD) and 1033 State Decision Repository (SDR) – Data Entry Tool.
- C. The states will fingerprint their resident producer applicants and conduct state and federal criminal background checks on new resident producer applicants.

OR

If a state lacks the authority or resources to accept and receive data from the Federal Bureau of Investigation (FBI), it shall conduct a statewide criminal history background check through the appropriate governmental agency for new resident producer applicants until such a time as it obtains the appropriate authority.

### Fingerprints

Under the ULS, the goal is that all states will electronically fingerprint their resident producers as part of the initial resident producer licensing process. States that lack the authority to run criminal history background checks through the FBI are encouraged to at least run a statewide background check until such a time that state and national fingerprinting is implemented.

The Working Group adopted model language that will allow a state to access federal databases (see the *Authorization for Criminal History Record Check Model Act* [#222]). The states are encouraged to adopt this language.

### 1033 Consent Waivers

The Violent Crime Control and Law Enforcement Act of 1994, 18 U.S.C. §§ 1033 and 1034, commonly referred to as “1033,” establishes a ban on individuals who have been convicted of certain felony crimes involving dishonesty or breach of trust from working in the insurance business. The law provides that a banned person can apply to the state insurance commissioner for a written consent to work in the insurance business. If an individual with a felony involving dishonesty or breach of trust obtains a 1033 consent waiver from that person’s resident state, the person cannot be prosecuted for engaging in the business of insurance in violation of 18 U.S.C. §§1033 and 1034.

When one state grants a written consent waiver to an individual pursuant to 18 U.S.C. §1033, the consensus of legal opinion is that this written consent waiver is effective nationwide.

The Working Group determined that the resident state bears responsibility for consideration of applications for consent waivers. Nonresident applicants should not be subject to additional procedures, nor should producers seeking nonresident licenses have to go through the 1033 process in all states after the producer’s resident state has issued a waiver. However, producers who have received waivers are required to attach them to applications for nonresident licenses. To assist these applicants, states should include a specific reference to 18 U.S.C. §1033 within the text of the document that grants a waiver. States may exercise their discretion to deny licenses based on the types of criminal convictions disclosed in consent waivers. The NAIC Antifraud (D) Task Force adopted guidelines for the reviewing and granting of these consent waivers. Under the guidelines, states are to report all activity on these consent waivers to the 1033 SDR – Data Entry Tool. The full text of the guidelines is available through I-Site.

### NAIC Databases Relevant to Initial Application Review

The NAIC maintains three databases that should be consulted as part of application review:

1. The Complaints Database System (CDS) contains information on closed complaints as reported by the states.
2. The RIRS contains any action taken by a state insurance department where the action is against an entity and where the disposition is public information. All final adjudicated actions taken and submitted by a state insurance department are reflected in the RIRS. The information typically includes: administrative complaints, cease and desist orders, settlement agreements and consent orders, receiverships, license suspensions or revocations, corrective action plans, restitutions, closing letters, and letter agreements. The RIRS does not include exam report adoption orders without regulatory actions.
3. A record of 1033 actions is maintained in the 1033 SDR – Data Entry Tool. The 1033 SDR application allows state insurance regulators to enter and search for 1033 decisions (approved or denied) that state insurance regulators have made for individuals who requested to work in the business of insurance but who

have been prohibited to do so by section 1033 of the Violent Crime Control and Law Enforcement Act of 1994.

### Review of Applications When Criminal History is Disclosed

As part of the 2009 charges for the Working Group, the Producer Licensing (EX) Task Force asked the Working Group to develop uniform guidelines for background check reviews of producers. For all jurisdictions to have a comfort level with licensing determinations made by a resident state when the applicant has a criminal history, a uniform process of review is warranted. If all jurisdictions implement these guidelines, in most situations, nonresident states will be able to defer to the resident state's licensing decision. A copy of the Uniform Criminal History and Regulatory Actions Background Review Guidelines is included in the Appendix of this Handbook.

When an application contains a disclosure with a “yes” answer to a criminal history question, in determining whether to issue a license, states should consider the following factors:

- *Resident vs. Nonresident*

If the application is for a resident producer license, it is incumbent upon the resident state to scrutinize all “yes” answers on the application and to request and obtain documentation and a detailed explanation for all criminal charges. Nonresident applicants’ criminal histories should also be documented and explained with consideration given the fact that the resident state has already issued a license to the applicant.

- *Severity and Nature of the Offense*

Felony convictions should always be considered in determining whether to issue a license to an individual and may require the applicant to apply for a 1033 consent waiver prior to application (see the section on 1033 consent waivers).

A criminal conviction is only relevant to the licensing decision if the crime is related to the qualifications, functions or duties of an insurance producer. Examples include theft; burglary; robbery; dishonesty; fraud; breach of trust or breach of fiduciary duties; any conviction arising out of acts performed in the business of insurance; or any actions not consistent with public health, safety and welfare. Special scrutiny should be given to financial and violent crimes.

- *Frequency of Offenses*

While a producer’s past criminal history is a red flag and may be a predictor of future behavior, the frequency of offenses should be considered, with more weight given to a pattern of illegal behavior than to a one-time minor indiscretion.

- *Date of the Offense*

The application form requires the applicant to disclose all criminal charges, except minor traffic offenses. A reviewer should consider when the offenses occurred and the age of the applicant at the time of the offense.

- *Completion of Terms of Sentencing*

Applicants should provide evidence that they have completed all the terms of their sentences, including paying restitution or completing any probationary periods or community service.

- *Evidence of Rehabilitation*

The applicant should be required to provide evidence of rehabilitation. Completion of the terms of sentencing alone does not demonstrate rehabilitation. A state may request a statement from the applicant’s probation officer or other appropriate official.

## Statutory Obligations and Discretion

State insurance regulators should review state law to determine guidelines for approval or denial of the application. After consideration of the above factors, the state insurance regulator has several options:

1. Request additional information or documentation.
2. If the producer failed to report an action, contact the producer and request an explanation. Technical violations, such as bad address or failure to timely report, generally do not merit formal action. However, the failure to report an action in itself can be cause for administrative penalty or a warning letter, depending on the particular state's law.
3. Approve the application with no conditions.
4. Approve the application with conditions.
5. Deny the application.

In some cases, it may be appropriate to grant a conditional license. This option may not be available in all states and may be limited by state law or regulation. Some options include:

1. Issue a probationary license that will expire after six months or a year, or that will coincide with the applicant's criminal probationary period. At the end of the probationary period, and prior to consideration of full licensure, the state insurance regulator should confirm that the applicant successfully completed all terms of the sentence and probation. This option can also be used for a producer with a record of prior administrative action.
2. Enter into a supervisory agreement, whereby another established licensed producer agrees to be responsible for the applicant during a certain period of time of the applicant's license term. This is a good option for producers who have criminal records in another state or some other evidence of past bad conduct. The supervisory agreement should include a requirement that the supervising producer report to the state insurance regulator any inappropriate behavior that is relevant to the agreement and to the applicant's license status.
3. Issue only a limited or restricted license for a particular product, such as credit life insurance. The theory of this option is that some types of products present individuals with less opportunity to commit bad acts.
4. Issue the license along with a requirement that the producer must report all complaints received against the producer and under the condition that there will be an immediate suspension for any bad act.

## Recommended Best Practices for State Insurance Regulators

- Work with state officials to adopt a fingerprint program that allows your state criminal justice agency to receive electronic prints, as well as electronically submit the reports back to the state department of insurance (DOI).
- If no fingerprint program is in place, inquire of the state criminal investigation department to determine if an alternative system for meaningful state background checks can be arranged.
- Allow pre-exam and post-exam fingerprinting.
- Make electronic fingerprinting available at test sites.
- Allow re-fingerprinting, if necessary, on a walk-in basis with no additional cost.
- Include registration for fingerprinting with registration for the exam or link the online websites to allow for electronic registration.
- Streamline the background check process to avoid delays in the overall licensing process, such as allowing for a temporary work authority pending receipt of the background check results.
- Check with other state agencies to determine what vendor(s) are used for the submission of electronic fingerprints (agencies that oversee programs such as teachers, bus drivers, social workers, foster parents, etc.)
- Adopt Model #222 for all license classes—allow some lag time before the effective date to provide sufficient time to establish procedures. Note that ULS 14 has since been updated to fingerprint new resident producers, and fingerprints are no longer required for additional LOAs under an existing home state license.
- Model #218 allows a producer to reinstate a lapsed license within 12 months of expiration, so only resident producers who are reinstating a license lapsed over 12 months should be required to submit fingerprints.

- Work with your state district attorney official to coordinate the review and approval of the enabling statute, which must be approved by the U.S. attorney general to access the Criminal Justice Information Services (CJIS) Division of the FBI criminal history record information.
- Establish a set number of times an applicant should be re-fingerprinted—at times, fingerprints are rejected. If re-fingerprinting is required, and the fingerprints are still rejected, establish a process to perform a state and federal NAME check.
- If your state is unable to use a vendor to electronically collect the cost of the criminal history background check from applicants, work with the National Insurance Producer Registry (NIPR) to collect this fee from new resident producer applicants during the electronic resident licensing application.
- Work with state officials to establish a reimbursement services agreement (RSA) for the payment of fingerprint or background checks.
- If your jurisdiction is just implementing fingerprinting, reach out to other jurisdictions for suggestions and best practices.
- Develop a system for review of 1033 consent waiver applications, and post relevant information on the department website.
- Post all information regarding 1033 consent waiver requests, approvals and denials on the 1033 SDR – Data Entry Tool.
- Accommodate applicants to the greatest extent possible with flexible hours of operation.
- Allow payment by check, credit card or debit card.



## Chapter 8

### Testing Programs

#### Introduction

The states have a responsibility to ensure that licensing examinations are fair, sound, valid and secure. Directors must consider how an exam is developed, who is involved in the development process, how the exam is offered and how security is maintained. Nearly every state has contracted with an outside vendor to assist in examination development and administration. These testing vendors employ test development experts and psychometricians to construct and evaluate examinations.

The primary purpose of a state examination and licensing program is to protect consumers. Examinations should be consistent across the states in difficulty level, content and subject matter. They should be uniformly administered and scored. Examinations should be psychometrically sound, using methods for setting and maintaining passing standards—i.e., cut scores—that are in accordance with testing industry best practices. They should use resources such as: 1) “Standards for Educational and Psychological Testing,” developed jointly by the American Educational Research Association (AERA), American Psychological Association (APA) and National Council on Measurement in Education (NCME); and 2) the U.S. Equal Employment Opportunity Commission’s (EEOC) Uniform Guidelines on Employee Selection Procedures (29 CFR 1607). Through valid, reliable and legally defensible test development practices, candidates will have a fair and equitable opportunity to pass an exam, regardless of which state exam they take. Ideally, pass rates should be consistent throughout the states; however, statistics from national examination administration have shown that the pass rates for examinations for the same line of insurance vary significantly among the states. Other variables may contribute to pass rates, such as state education systems, demographics, the existence of a prelicensing education requirement, and the quality of such prelicensing education, but the states should work with their test vendors to be sure that they eliminate any practices that do not measure the entry-level knowledge, duties and responsibilities of an insurance producer.

Different states take different approaches to the development and administration of producer license examinations. Some of the states exercise significant control over test development and review. Other states rely almost entirely on outside experts. In most of the states, the state does not pay any fee to a testing vendor, and the cost of test development and administration is passed through to the test-takers. Most of the states reserve the right to preapprove any fees charged by testing vendors.

With the state licensing system increasingly built on reciprocity, it is in the best interest of consumers, state insurance regulators, industry, producers, and prospective producers for state licensing directors to establish guidelines that promote efficiency and consistency throughout the licensing process. Directors should also reduce or eliminate artificial barriers that impede qualified applicants from obtaining a license.

The purpose of this chapter is to recommend best practices for the states in testing administration in the following areas:

1. Test development and review.
2. Test administration.
3. Test results.
4. Expectations for test vendors.

This chapter was developed with assistance from insurance test vendors, industry representatives, education providers, and state insurance regulators.

#### ***Producer Licensing Model Act Guidelines on Examinations***

Section 5 of the *Producer Licensing Model Act* (#218) contains guidance for administering licensing examinations. Under Section 5, all residents are expected to complete a written examination, which should include the following:

1. The entry-level knowledge required for an individual concerning the lines of authority (LOAs) for which the application is made.
2. The duties and responsibilities of an insurance producer.
3. The applicable insurance laws and regulations of the state.

Section 5 grants the insurance commissioner authority to hire an outside testing service to administer examinations and impose nonrefundable examination fees.

Model #218 contains several exemptions from prelicensing education and examination requirements. An individual who is licensed as a nonresident in a state and who moves into that state, or an individual who moves from his or her home state to another state and seeks a resident license, is not required to complete an examination for the LOA(s) previously actively held in the prior resident state as long as application is made within 90 days of the change in residence and the prior resident state indicates that the producer was licensed in good standing. In this situation, a nonresident state should never impose prelicensing education or examination requirements.

The Uniform Licensing Standards (ULS) provide that examinations are not generally required for limited lines, but it is acceptable to require examinations for areas such as crop and surety.

Model #218 leaves test development and administration to the discretion of the individual states. Section 5(A) of Model #218 requires, “[a] resident individual applying for an insurance producer license shall pass a written examination,” and the examination must test the knowledge of the individual in three areas:

1. The specific LOAs for which the application is made.
2. The entry-level duties and responsibilities of an insurance producer.
3. The applicable insurance laws and regulations of the state.

Beyond these broad subject matter categories, Section 5 states that tests “shall be developed and conducted under rules and regulations prescribed by the insurance commissioner.”

In order to provide more uniformity in state licensing practices, the 2012 revised ULS for Exam Content or Subject Area and Testing Administration Standards establishes implementation of the “Exam Content and Testing Administration Recommended Best Practices found in Chapter 8 of the NAIC *State Licensing Handbook*” as the uniform standard.

### **Test Development and Review**

Test development experts believe that licensing examinations should measure the minimum competency required for a candidate to perform at an entry level. Therefore, test content and curriculum development should be focused on assessing whether a candidate demonstrates sufficient knowledge to pass an examination that is appropriately targeted to an entry-level producer.

The examination should not dictate the curriculum that an entry-level insurance producer should master. Instead, the test content should be developed using the steps outlined below. Examinations and curriculums should be updated to reflect any changes in insurance laws, regulations or industry practice. An online candidate guide should be available and provide detailed testing and licensing procedures, as well as content outlines with cross-references to the curriculum.

Input from trainers who conduct test preparation courses may assist in the development of the curriculum and the exam content outline; however, some state insurance regulators believe it is not appropriate to invite these trainers to participate in reviewing final examination questions. Education providers who do not offer prelicensing education courses (such as continuing education [CE] providers) are sometimes used during test development. There are generally two approaches to examination construction. A bank-based test generates individual examinations from a large bank of items. A form-based examination will consist of a specified set of predesigned test forms that are rotated. The states use both methods, and both are psychometrically acceptable. Although contracted outside experts play a major role in test development in most jurisdictions, the state should have a regular process and procedures for developing and reviewing licensing examinations to ensure that those examinations are properly focused on the minimum competencies required of an entry-level producer. Some items that should be included in the plan include:

1. Procedures to ensure that a job analysis survey that includes input from state insurance regulators and the industry is conducted at regular intervals to determine the requirements and work performed by an entry-level insurance producer.
2. Regular, ongoing review and assessment of producer licensing examinations in the event of legislative or regulatory changes that could affect the accuracy of exam content.
3. An annual review of the examination development process conducted with the state and the testing vendor.
4. Depending on test volume, test performance, and the need for content changes, either an annual, or at least biannual, substantive review of the examination and the psychometric properties of the test. These efforts should include the involvement of content or test development professionals, department personnel and industry representatives, including recent, entry-level producers.
5. A fair and valid state-based test should incorporate knowledge, skills and abilities that measure state-specific and national expertise. This balance will shift depending on the subject matter. For example, life insurance laws and regulations tend to be more similar among the states, while health insurance standards can vary widely.
6. If the state collects demographic data, it should be reviewed annually.

### **Developing the Questions**

Developing a valid and sound bank of test questions, often called “items,” is perhaps the most critical piece of any testing program. The items need to be at the appropriate level of difficulty. Items should be relevant to the profession and effective in evaluating whether the person taking the exam possesses the knowledge, skills and abilities critical to competently performing the job and safely practicing in the profession. To create this balance, most of the states use a combination of local subject matter experts (SMEs) and content or test development professionals. The local panel should include new and experienced producers to help establish such a balance.

Using multiple item writers to develop test content is a common practice, but it can lead to variation in test item style, format and difficulty. Developing a style guide with templates, development standards and rules can go a long way in improving item consistency, format and variety. Content development training can ensure that writers have the tools they need to develop credible, legally defensible items and templates that can be leveraged to create multiple variations of the same question.

### **Passing Score vs. Pass Rate**

A passing score, sometimes called a “cut score,” is the minimum score one needs to achieve in order to pass the exam. The “pass rate” is the percentage of candidates who actually pass the exam. The test development process will consider data from actual tests and data from reviewers rating the items and exams in evaluating the cut score.

In some of the states, the cut scores are arbitrarily established by rule or regulation. This is not a valid testing practice. Cut scores should be based on data collected through the test-development process. Regulatory licensing exams typically target a level referred to as “minimum” competency, rather than “average” competency. Licensing examinations try to determine who has the minimum competency to safely practice in a profession without compromising the health and safety of the public. An arbitrary cut score, which is the practice in some of the states, tends to focus on the average, rather than minimum, competency. Thus, qualified candidates could be cut because they fall below the average, not because their competency is unacceptable.

### **Exam Scoring**

Some of the states administer a one-part or one-score exam, while others administer two-part exams. In the one-part exam, general product knowledge and state-specific content are scored together. In the states with a two-part exam, the candidate must separately pass both the general product knowledge exam and the state-specific exam in order to be eligible to apply for a license for the LOA requested. A third variation is to require the first-time test-taker to pass an exam on state-specific insurance laws and regulations once. All additional LOAs are tested on general product knowledge only.

Preliminary review of pass rates indicates a tendency for more candidates to fail in the states that require two-part exams. There is no evidence that two-part exams increase consumer protections or that the states that administer one-

part exams license producers who do not know applicable state law. The states are encouraged to move to one-part exams to allow for more success among candidates without jeopardizing consumer protections.

## Exam Content

As of May 2013, the states have no standard exam curriculum. The NAIC is encouraging more uniform approaches by considering the best practices for testing programs listed at the end of this chapter to be standards for all jurisdictions to work toward. The Producer Licensing (EX) Task Force formed a subgroup of five states to develop a draft national content outline using the life and annuity LOA as a pilot. The national content outline provides guidance for entry-level subject matter that the states should test for, as well as information that will assist candidates in identifying relevant knowledge to study in preparation for the exam.

Some experts have recommended that examinations should be constructed with the following considerations in mind:

1. The states should not target examinations to an artificially set passing score. A state should determine whether its test is focused on assessing the knowledge needed by potential new producers, and only applicants who lack that level of knowledge should fail. The states should use legally defensible, recognized methodology when establishing a cut score.
2. Prior to releasing items into an exam form, the editing and review process employed is critical. This editing process should include the psychometric evaluation of the cognitive level of the items and the reading level of the items, as well as such editorial issues as grammar, sensitivity and style. Psychometric editing is best performed by test development professionals, not state SMEs or item writers. Individuals trained in the complexity of psychometric editing evaluate items in a different, critical light than SMEs or item writers. It is critical, however, to have all final items reviewed and approved by state and national SMEs in the given field for accuracy and relevancy.
3. Each examination should consist of pre-test questions that are being evaluated for performance and questions that previously have been evaluated (pre-tested) and determined to be statistically effective. Each candidate's score should be based only on the previously pre-tested and approved questions. Any time used to respond to pre-test items should not be counted against the test-takers, and responses to pre-test items should not be calculated in the test-taker's score. Pre-test items should not be used as scored items until they have been statistically proven to be effective. The test questions for any new examination should be chosen from the pool of test questions to properly represent the subject-matter outline of the examination.
4. Reports regarding exam pass rates, candidate demographics when collected, and number of exams administered should be made available to the public. Reports should include first-time pass success by subject area. Whenever possible, this information should be tracked by, and be made available to, each education provider so they may evaluate their programs and instructors and be provided with data needed for course development. The states may ask for, but generally cannot require, information on candidate population, gender, ethnicity, education level and income level. When candidate demographics are collected, reports should include the percentage and number of examinees who passed the examination by race, ethnicity, gender, education level and native language. This information is necessary for the selection of future test questions, and it will aid in making testing transparent and assessing whether differences in test scores are correlated with relevant demographic factors.
5. A state advisory committee consisting of state insurance regulators and the industry, including, where possible, recently licensed producers, should annually or, if changes are not needed every year, at least biannually work with the testing vendor to review the questions on each examination form or bank of items for substantive and psychometric requirements. Adjustments should be made to the examination to eliminate any questions that might be inaccurate or unclear, that might test subject matter that is beyond what a new producer should know, or that exhibit unsatisfactory psychometric properties.
6. Licensing examinations should be reviewed at least annually. However, if during any rolling 12-month period, a licensing examination exhibits uncharacteristically high or low pass rates, such as less than 60% or

more than 80%; unexplained fluctuations in testing volume; or other significant deviations, that examination should be reviewed immediately.

A state testing program should include statistical analysis of test items in the field and gather feedback on the candidate performance on the individual items. The most obvious and critical use of this information is to ensure that exams are equivalent and to evaluate the accuracy with which items differentiate between candidates who are minimally qualified and candidates who are not. The psychometric review can result in the continued use of items, the modification of items, or the deletion of items from the bank.

A professional test vendor should use a comprehensive strategy for developing test items and ensuring measurement of the knowledge, skills and abilities necessary for initial insurance licensees to perform their jobs effectively. The steps may include:

1. Conducting a committee-based job analysis.
2. Developing content specifications and weightings.
3. Developing items.
4. Editing and reviewing items with SMEs to ensure that items meet the required criteria.
5. Obtaining item difficulty (e.g., Angoff method) estimates to establish a passing score.
6. Developing item sampling groups to structure each examination.
7. Creating equivalent forms.

## Test Development Deliverables

A state licensing director should expect to receive the following items to ensure that the testing vendor has provided all items necessary to administer a successful testing program:

1. Finalized task and knowledge statements reflecting the requirements of each licensed insurance position.
2. Content specifications for each licensing examination.
3. A set of approved, relevant and important items for use on each licensing examination.
4. A list of references used to develop the test items.
5. Candidate Information Bulletins (CIBs).
6. A technical report describing the procedures used and results obtained from the test development process for each licensing examination.

## Candidate Information Bulletin

A CIB should describe the examinations, examination policies and procedures, and the consequences of violating security procedures. A testing vendor should be capable of making changes to the information contained within the CIB during any contract year at the state's request.

The CIB should be available at no charge to candidates, trainers and insurers in hard copy or in electronic format via the internet. The state licensing director should consider including the following topics in the CIB:

1. How to contact the testing vendor.
2. Requirements for taking an examination.
3. How to apply for an examination, including receiving authorization of eligibility from the state, prelicensing education, and background checks.
4. Links to current application forms.
5. How to obtain current forms in hard copy, if available in hard copy.
6. Examination fees.
7. Scheduling procedures.
8. The content outline and format of the examination.
9. Supplies provided at the test center.
10. The time limit for the examination.
11. The scoring system.
12. Security procedures.

13. Examination process and procedures.
14. Appropriate examination-taking strategies (e.g., “There is no penalty for incorrect answers, so be sure to answer every question.”).
15. Appropriate use of scratch paper, calculators, and/or other support material.
16. Sample questions.
17. Specific information about taking the test on the computer.
18. List of approved reference materials.
19. List of test centers, alternative test centers, and driving directions to each.
20. Procedures for requesting special accommodation.
21. Examination registration forms.
22. Licensing requirements and procedures.
23. Refund policies.
24. Holiday or weather-related test center closures.
25. Instructions about how to contact the state insurance department.

A state should approve each CIB before it is published. The licensing director should work with the vendor to set a timeline that will allow for final publication of an updated CIB in advance of the expiration of the prior edition of the CIB. The new edition should be provided to test preparation trainers at least six weeks in advance of implementation so that training materials can be updated.

### **Technology Issues**

A licensing director should consult with the state’s information technology (IT) staff to ensure that the testing vendor can deliver data to the state insurance department. This is critical when a state changes testing vendors. This is also critical if the state directs a vendor to send data to a different location than the state insurance department. Any transition should include a testing phase for hardware, software, and state insurance department staff.

The state and the testing vendor should jointly agree on a timeline for introducing new or updated examinations. State IT staff also should be consulted.

### **Legal Defensibility**

Items developed must also be legally defensible to protect the state in the event of a legal challenge. To protect the state from liability, each exam should be critically reviewed from a content and psychometric perspective to ensure that the exam was developed according to recognized standards. Validation procedures for licensing examinations should be designed to comply with content validation requirements of the EEOC’s Uniform Guidelines on Employee Selection Procedures (29 CFR 1607).

States should require testing vendors to follow and document standardized methods. This should include appropriate test development personnel in the process. Using the appropriate, credentialed professionals is critical, as there are multiple steps involved in the test development process and various methodologies that can be used for each step. State licensing directors should discuss all options with qualified professionals.

### **Vendor Responsibilities**

Test vendors should be able to meet minimum guidelines for sufficient availability, facilities, personnel and openness in terms of providing information related to their operations.

The states, and not the test vendors, must be responsible for all examination content and content outlines. The vendor should provide accessible information regarding the registration system through the internet, toll-free telephone numbers, interactive voice response, fax, and other available technologies. The available information should include permitting candidates to view exam test dates and access forms and content guidelines without requiring prior payment and scheduling of an exam.

The vendor should promptly provide the state with all pertinent information, including prompt notification of any candidate complaints, changes to test administration, conflicts at examination test sites, or other information requested or required by the state.

The vendor should provide quality, accessible facilities, with an established system of examination site supervision that ensures that competent site administrators consistently provide accurate information to applicants.

Where a vendor operates test sites in multiple states, the vendor should permit any applicant to take a state's examination in another state, under the same conditions that would apply if the exam were taken at an in-state location.

Vendors should be required, on an ongoing basis, to collect the data on customer satisfaction and, if directed by the state, to make those data available to state insurance regulators, the industry, and the public.

### **Test Administration**

The testing process should be fair and accessible for all candidates. A state should consider including the following elements below in its licensing process to ensure that applicants have equal access to examinations.

#### *Secure Administration*

The security of the test center network is important in maintaining the integrity of a test. A vendor should be equipped with adequate security features and qualified test center administrators. Each proctor should be trained and tested on his or her ability to supervise exams. A vendor should have systems in place to ensure the fair, consistent and even administration of the exam in every location. A vendor should also have a method to detect attempts to record questions. For example, a vendor should track multiple examination attempts by individuals to assess if the candidate is intentionally failing the exam so it can be repeated. A vendor should be required to notify the state immediately if the vendor suspects that the integrity of an examination has been compromised.

#### *Test Locations and Registration*

Test locations should be set up to provide flexibility and convenience. Realizing that the states have different geographic challenges and diverse population density, a state should consider, where possible, requiring the following elements:

1. Testing should be made available at locations convenient to residents of all areas of the state.
2. Test locations should provide enough testing capacity so a candidate can test at the desired location within two to five business days of registration.
3. Exam site hours should include evening and weekend hours.
4. Test vendors should provide regular reports, as required by the state, detailing site usage and availability data.
5. Test registration should be available online or by telephone and allow for next day testing when space is available. A state should consider tracking telephone hold and wait times to monitor how long callers wait.
6. State guidelines should provide for flexible means for payment of fees for testing, fingerprinting and other licensing. States should consider methods that facilitate payment by companies.

#### *Disabilities*

A state should require a vendor to develop a system that accommodates the physically impaired that is not related to a testing candidate's knowledge of insurance. Visually-impaired and hearing-impaired persons should be accommodated through all steps of the licensing process, pursuant to national standards set by the federal Americans with Disabilities Act (ADA).

#### *Examinations in Languages Other Than English*

Some industry experts suggest caution about using translated or interpreted exams. The material may not directly translate into equivalent terms or meaning. Cultural biases might cause incorrect interpretation of a meaning. Some experts recommend that tests should be developed and administered in English, especially if other materials necessary to perform job duties for the profession, such as contracts, are in English. State licensing directors should review state law and consult with legal counsel about the appropriateness of offering examinations in a foreign language.

## Reporting Examination Results

State licensing procedures should include guidelines that facilitate the prompt issuance of licenses once an applicant passes a test. Elements might include:

1. Pass/fail notices should be issued at exam sites upon completion of the exam. If an applicant has not achieved a passing score, the applicant should receive immediate notification of failure. States vary as to whether successful completion is reported with a precise score or merely an indication that the candidate passed the exam. When a candidate does not pass the exam, the state should provide the precise score and the percentage of questions in each subject area that the applicant answered incorrectly.
2. If a state issues a paper license, and if it has been predetermined that an applicant has met all requirements necessary for licensure, including any required fingerprint report, a license should be issued at the exam site, or within 48 hours of completing all necessary requirements.
3. The state should send an email or other timely communication to a candidate to whom a license has been issued outside the test site or provide information to applicants as to how to check online.
4. Within 24 hours of license issuance, the new licensee's information should be added to the state's database, and the updated status should be sent to the National Insurance Producer Registry (NIPR).
5. The states should work with their vendors to report aggregate results in a way that is more uniform with other states.
6. First-time pass rates should be maintained and made available to the public. First-time pass rates are defined as the percentage of candidates who pass the whole test the first time.
7. In performing background checks, the use of an electronic process should be required whenever possible.
8. In those states requiring fingerprints, where possible, exam sites should have the capability to collect electronic fingerprints.

## Retesting or Notice of Failure

A state licensing plan should include a method to facilitate prompt retesting of applicants who have failed a test. The “non-passing” notice should break scores out by each subject area. If the candidate requests to make another attempt, an examination should be made available within a reasonable time period.

### Producer Exam Content and Testing Administration Recommended Best Practices for State Insurance Regulators

- States should use accepted psychometric methods, including job analysis, to determine if the examination content falls within the content domain that a minimally competent candidate of that specific line of authority tested would be expected to know.
- States should set passing scores—cut scores—and difficulty level using psychometric methods and appropriate SMEs based on what an entry-level producer needs to know.
- States are encouraged to move to one-part exams to allow for more success among candidates without jeopardizing consumer protections.
- States should require the test vendor, or other entity responsible for test development, to document the process for ensuring quality control and validity of the examination, including psychometric review and editing and analysis of item bias or cultural and gender sensitivity.
- To allow for meaningful comparison, all jurisdictions should define first-time pass rate as the percentage of candidates who pass the whole test the first time.
- At least annually, reports regarding exam pass rates, candidate demographics when collected, and number of exams administered should be made available to the public. Reports should include first-time pass success and average scoring by subject area. Whenever possible, the reports should be available by education provider and provided to them.

- A state advisory committee consisting of state insurance regulators and the industry—including, where possible, recently licensed producers—should annually work with the testing vendor to review the questions on each examination form for substantive and psychometric requirements. If, during any other time, any examination results exhibit significant unexplained deviations, the examination should be reviewed.
- States should work with testing vendors and approve CIBs that describe the examinations and examination policies and procedures, and provide sufficient examination content outline and study references for the candidate to prepare for the examination. Updated editions of the CIB/content outline should be provided to prelicensing education providers at least six weeks in advance of implementation so that training materials can be updated.
- Testing should be made available at locations reasonably convenient to residents of all areas of the state, with registration available online or by telephone and the ability for a candidate to schedule testing within two to five business days of registration.
- Pass/fail notices should be issued at exam sites upon completion of the exam. The fail notice should break out scores by subject area. The state should provide a method to facilitate prompt retesting, while allowing a reasonable time for candidates to review and prepare for retest.
- States should deliver exams in a secure test center network that employs qualified test proctors.
- States should set clear performance standards for test vendors and require accountability.



## Chapter 9

### Lines of Insurance

#### The Major Lines

A line of authority (LOA) is a general subject area of insurance that a producer can be licensed to sell. The *Producer Licensing Model Act* (#218) identifies and defines seven LOAs; however, the Uniform Licensing Standards (ULS) set forth six lines that are considered major lines of authority, as well as certain core limited lines. Additionally, the ULS set forth standards for non-core limited lines. States should review all other lines of insurance and consider eliminating them in an effort to become compliant with the ULS.<sup>1</sup> Uniform adoption of the major lines is essential to fully implement NAIC licensing reforms.

The six major LOAs are defined in Model #218 as follows:

1. Life – Insurance coverage on human lives, including benefits of endowment and annuities, and may include benefits in the event of death or dismemberment by accident and benefits for disability income.
2. Accident and health or sickness – Insurance coverage for sickness, bodily injury or accidental death, and may include benefits for disability income.
3. Property – Insurance coverage for the direct or consequential loss or damage to property of every kind.
4. Casualty – Insurance coverage against legal liability, including that for death, injury or disability, or damage to real or personal property.
5. Variable life and variable annuity – Insurance coverage provided under variable life insurance contracts and variable annuities.
6. Personal lines – Property/casualty (P/C) insurance coverage sold to individuals and families for primarily noncommercial purposes.

Because the ULS also require that each major line be available individually, the states should provide individual examinations for each of the major lines except variable life and variable annuity. It is acceptable for a state to also offer combined exams. The ULS contemplate that each state will require an examination for residents to qualify for all major lines. States should give examinations only to residents, not nonresidents.

While the ULS do not specifically prohibit an examination for variable life and variable annuity products, most states do not require an examination. This LOA is usually granted if the applicant holds a life LOA and has successfully completed the Financial Industry Regulatory Authority (FINRA), formerly known as the National Association of Securities Dealers (NASD), examinations necessary to obtain a state securities license in that state. In most cases, this means successful completion of the FINRA Series 6 and/or Series 7, according to the specific state's requirements, and/or Series 63 exams.

The Producer Licensing (EX) Working Group has not specifically stated that states should not require an active state securities license of residents or nonresidents as a condition of granting the variable life and variable annuity products LOA. The ULS do contemplate that no such requirement shall be imposed. For nonresident applicants, it is not appropriate to pend a request for the variable life/annuity products LOA to verify existence of the underlying life LOA in the home state. If a proper request for licensure is received and the applicant is in good standing in the home state with the variable life and variable annuity LOA, the nonresident license should be granted. If a state cannot verify through the State Producer Licensing Database (SPLD) that the applicant holds a variable authority, it is permissible to pend the application and contact the applicant's home state to verify the variable authority.

Information regarding an applicant's status as to securities registration and securities examinations passed currently are easily accessible on FINRA's public website under "Check Out Brokers & Advisors" at [www.finra.org/InvestorInformation/index.htm](http://www.finra.org/InvestorInformation/index.htm). Information available includes: employment history, states where the individual is securities licensed, securities examinations passed, and formal and final disciplinary history. To obtain

<sup>1</sup> Model #218 does not address title insurance, which is considered a major line by some of the states and a limited line by others.

Central Registration Depository (CRD) information regarding pending complaints and unresolved cases, a state insurance department must contact its state's securities regulator.

#### **Recommended Best Practices for State Insurance Regulators**

- Adopt the major lines and the definitions exactly as stated in Model #218, and provide separate testing for each line, except variable.
- Allow combined examinations, as appropriate.

#### **Limited Lines**

A limited line of insurance is a line of insurance that covers only a specific subject matter. Limited line licenses generally have simpler licensing requirements than those required by the major lines. Some states require an examination for credit insurance. For the other limited lines, some states require an examination, while some require only a simplified application process. In some states, a business entity is permitted to maintain a limited lines license on behalf of individuals who make the limited line of insurance available to its customers. Often, a limited line is adopted by regulation and not by statute.

Model #218 contains a specific definition for credit insurance and allows states to define other limited lines. The Working Group adopted definitions for specific "core" limited lines of insurance for producers, which have become part of the ULS. States are encouraged to adopt the definitions of those limited lines and review and eliminate as many non-uniform limited lines as possible. Model #218 requires the states to grant to a nonresident a nonresident limited line producer license with the same limited LOA as the license issued by the home state. Many states have adopted a special licensing category to accommodate this type of situation.

The core limited lines are:

1. Car rental insurance.
2. Credit insurance.
3. Crop insurance.
4. Travel insurance.

The ULS provide that examinations are not generally required for limited lines, but it is acceptable for examinations for areas such as crop and surety. States should give examinations only to residents, not nonresidents. The ULS specifically state that continuing education (CE) is required for only the major lines of insurance (see specifics for crop insurance).

In 2009, the Working Group was charged with reviewing limited line licensing issues, with particular focus on: 1) the establishment of a limited line that encompasses several insurance products where the business of insurance is ancillary to the business of the person offering the product; 2) the licensing requirements of individuals selling limited line products; and 3) the fingerprinting of individuals selling limited line insurance products. Throughout the year, the Working Group had discussions; however, no consensus was achieved. As a result, the Working Group reported to the Producer Licensing (EX) Task Force and requested further guidance on its charge. For 2010, the Working Group was asked to:

Finalize the review of limited-line licensing issues, with particular focus on the following: 1) individually review the licensing requirements for each core limited line; 2) review other limited lines, and determine what licensing requirements should apply to them; and 3) determine if another "catch all" limited line was needed to address licensing requirements for insurance products not already encompassed within the list of limited lines.

Updates to the limited line charge may be obtained on the Producer Licensing (EX) Working Group's web page on the NAIC website.

The NAIC has adopted a specific resolution rejecting a prior request by industry to adopt a new limited line for term life insurance. The full text of the resolution is in the Appendices.

As part of its 2010 charges, the Working Group conducted a review of the ULS and adopted several amendments. Specifically related to this chapter, revisions were made to Standard 16 (Lines of Authority), Standard 33 (Definition of Core Limited Lines), Standard 34 (Travel), and Standard 37 (Non-Core Limited Lines).

#### **Recommended Best Practices for State Insurance Regulators**

- Allow resident and nonresident limited lines license applications to be filed electronically.
- Eliminate state-specific applications.
- To further reciprocity, report all limited lines licensees to the SPLD.
- Adopt the applicable revisions to the ULS related to limited lines.

#### **A. Limited Line of Car Rental Insurance**

Under the ULS, car rental insurance is defined as:

[I]nsurance offered, sold or solicited in connection with and incidental to the rental of rental cars for a period of [per state law], whether at the rental office or by pre-selection of coverage in master, corporate, group or individual agreements that (i) is non-transferable; (ii) applies only to the rental car that is the subject of the rental agreement; and (iii) is limited to the following kinds of insurance:

- (a) Personal accident insurance for renters and other rental car occupants, for accidental death or dismemberment, and for medical expenses resulting from an accident that occurs with the rental car during the rental period.
- (b) Liability insurance that provides protection to the renters and other authorized drivers of a rental car for liability arising from the operation or use of the rental car during the rental period.
- (c) Personal effects insurance that provides coverage to renters and other vehicle occupants for loss of, or damage to, personal effects in the rental car during the rental period.
- (d) Roadside assistance and emergency sickness protection insurance.
- (e) Any other coverage designated by the insurance commissioner.

States vary in their methods of supervising the sale of car rental insurance. In the states that require a license, there are generally three methods in use. The first is a registration requirement through submission of an application. The second is the successful completion of an exam and submission of an application. States should give examinations only to residents, not nonresidents. Under the third method, a car rental company registers with the state insurance department. The company holds the license and is responsible for supervising the training and testing of its counter agents. The company reports to the department and pays all fees.

#### **B. Limited Line of Credit Insurance**

Model #218 defines limited lines credit insurance as:

Credit life, credit disability, credit property, credit unemployment, involuntary unemployment, mortgage life, mortgage guaranty, mortgage disability, guaranteed automobile protection insurance or any other form of insurance offered in connection with an extension of credit that is limited to partially or wholly extinguishing that credit obligation and that is designated by the insurance commissioner as limited line credit insurance.

Credit insurance products are designed to protect the borrower against the risk of not being able to pay a debt. Credit life, disability and involuntary unemployment insurance are typical lines of coverage. These products are generally made available by the creditor at the time the loan transaction occurs. Because the insurance is purchased at the time the borrower completes the loan, policy and certificate forms, premium structures, and underwriting conditions are generally simpler than other limited lines of insurance.

Credit insurance is issued under individual and group policies. This allows market flexibility for different distribution systems and variations in product design to insure the different types of credit risks. If an individual enrolls customers under a group insurance policy, the individual must obtain a limited lines license if a commission is paid. Section 4(B)(2) of Model #218 provides an exception from licensing if no commission is paid to the enroller and the enroller does not engage in selling, soliciting or negotiating.

Section 6(D) of Model #218 provides that each insurer that sells, solicits or negotiates any form of limited line credit insurance shall provide its producers a program of instruction that may be approved by the insurance commissioner.

#### **Recommended Best Practices for State Insurance Regulators**

- A state should establish a method to verify that each credit insurer has established a program of instruction.

#### **C. Limited Line of Crop Insurance**

Under the ULS, crop insurance is defined as:

Insurance providing protection against damage to crops from unfavorable weather conditions, fire or lightning, flood, hail, insect infestation, disease, or other yield-reducing conditions or perils provided by the private insurance market, or that is subsidized by the Federal Crop Insurance Corporation (FCIC), including multi-peril crop insurance.

There are two types of crop insurance: multiple peril crop insurance (MPCI) and crop/hail insurance.

The federal government is involved with crop insurance because a single event, such as drought, often results in multiple losses. Automobile accidents or health problems are generally independent, random events that do not trigger multiple insurance losses. For crop insurance, multiple losses are the norm, rather than the exception. For many years, capital requirements to maintain adequate reserves to cover widespread losses were so high that commercial development of MPCI policies by companies was unrealistic. As a result, the federal government created a federally subsidized risk management program.

#### **Multiple Peril Crop Insurance**

An MPCI policy provides protection against crop losses from nearly all natural disasters, including: adverse weather conditions; fire; insects, but not damage due to insufficient or improper application of pest control measures; plant disease, but not damage due to insufficient or improper application of disease control measures; wildlife; earthquake; volcanic eruption; or failure of the irrigation water supply if due to an unavoidable cause of loss occurring within the insurance period.

MPCI is subsidized by the federal government and delivered by private insurance companies. The insurer's functions include hiring and training producers, paying for marketing and advertising, hiring and training loss adjusters, carrying out loss adjustment activity, billing and collecting premiums, processing and verifying applications, conducting actual production history reviews, processing and verifying acreage reports, paying claims, auditing and verifying claims data, paying uncollected premiums, and maintaining the necessary automated data processing infrastructure to communicate data with the Risk Management Agency (RMA) on a routine basis for all MPCI policies.

The MPCI policy is a contract between the producer and the insurance company, not with the federal government. However, a farmer cannot receive the federal subsidy attached to the program unless the insurance policy followed

the federal standards and rates. Like many insurance companies, crop insurance companies have reinsurance agreements to transfer risk to other private companies known as reinsurers. Unlike most other insurance lines, the private insurance companies also transfer some of the risk associated with the crop insurance program directly to the federal government.

There are many MPCI plan options available: yield-based, revenue-based, or a combination of both. The basic policy provisions for all these plans, as well as the rates, are set by the FCIC. A combination of commodity markets results and the U.S. Department of Agriculture (USDA) establish the maximum price for each crop each year for insurance purposes; i.e., the value of each bushel in the event of loss.

While the RMA controls pricing and policy forms, producer licensing and enforcement of proper sales practices are left to the states.

### **Crop/Hail Insurance**

Crop/hail insurance is offered through companies licensed by state insurance departments. A private market has existed for crop/hail insurance for more than a century. Companies have developed stand-alone full coverage and deductible crop/hail policies, as well as companion policies that function very well in conjunction with the different MPCI plans that are offered at varying coverage levels. The premium rates for these crop/hail policies are determined by historical loss experience and are set by the companies.

### **Continuing Education**

Subsequent to the adoption of the ULS, the Working Group considered and agreed that a CE requirement for crop insurance shall not be a violation of the uniform standards. Under federal law, insurance producers selling MPCI are required to attend CE classes each year.

### **D. Limited Line of Surety**

As part of the discussion of limited lines, the Working Group made the determination to remove surety as a limited line. Although this determination was made, it is understood that surety is considered a major line by some of the states and a limited line by others.

### **E. Limited Line of Travel Insurance**

Under the ULS, as revised Aug. 6, 2010, travel insurance is defined as:

Insurance coverage for personal risks incidental to planned travel, including, but not limited to:

1. Interruption or cancellation of trip or event.
2. Loss of baggage or personal effects.
3. Damages to accommodations or rental vehicles.
4. Sickness, accident, disability or death occurring during travel.

Travel insurance does not include major medical plans, which provide comprehensive medical protection for travelers with trips lasting six months or longer, including, for example, those working overseas as ex-patriot or military personnel being deployed.

Standard 34 recognizes and sets the guidelines for the creation of an additional business entity licensing model under the travel limited line licensing structure. This structure creates the concept of a “travel retailer” in which the entity and a certain number of its employees may disseminate travel insurance under the direction of a responsible licensed producer. Said producer maintains responsibility for the training and conduct of any and all associated travel retailer(s).

**Recommended Best Practices for State Insurance Regulators**

- A state adding the travel limited line should do so in accordance with applicable ULS.

**F. Non-Core Limited Lines**

After much discussion about the concept of “auxiliary” or “miscellaneous” lines, the Working Group formally adopted Standard 37 as a basis for any future addition of other non-core limited line. The standard states, in part, that:

A state is not required to implement any non-core limited line of authority for which a state does not already require a license or which is already encompassed within a major line of authority; however, the states should consider products where the nature of the insurance offered is incidental to the product being sold to be limited line insurance products. If a state offers non-core limited lines (such as pet insurance or legal expense insurance), it shall do so in accordance with the following licensing requirements. Individuals who sell, solicit or negotiate insurance, or who receive commission or compensation that is dependent on the placement of the insurance product, must obtain a limited line insurance producer license. The individual applicant must: 1) obtain the limited lines insurance producer license by submitting the appropriate application form and paying all applicable fees as set forth in applicable state law; and 2) receive a program of instruction or training subject to review by the insurance department.

No prelicensing or testing shall be required for the identified non-core limited lines insurance.

## Chapter 10

### Surplus Lines Producer Licenses

In order to operate in a state, property/casualty (P/C) insurance companies are generally categorized in one of two ways. An admitted company obtains a certificate of authority to operate in a given state, and it is fully subject to and regulated by the laws of the state. Its policyholders are protected, at least to some extent, by the state's guaranty fund.

A nonadmitted company, otherwise known as a surplus lines company, has limited authority to operate in a state. These companies may be required to be eligible in a state, but they are subject to significantly less regulation. States allow surplus lines companies to operate because they recognize that certain types of insurance, or insurance at certain amounts, are not available from admitted companies. Generally, surplus lines companies are not subject to rate and policy form regulation, and their policyholders are not covered by state guaranty funds.

Under the Uniform Licensing Standards (ULS), a producer who wishes to engage in the sale of surplus lines insurance (SLI) must first obtain a surplus lines producer license. Under the ULS, this is considered a license type and not a line of authority (LOA); however, in some states, it is treated as an LOA. The ULS require that a resident producer hold both property and casualty LOAs before an SLI producer license can be issued. Under the previous reciprocity provisions of the Gramm-Leach-Bliley Act (GLBA), surplus lines producers were entitled to reciprocal licensing if they were licensed for surplus lines and in good standing in the producer's home state. The NAIC uniform application is to be used for application as a surplus lines producer.

Some states also require a resident producer placing SLI to complete an examination or post a bond. However, to comply with the reciprocity provisions of Section 8 of the *Producer Licensing Model Act* (#218), these requirements cannot be imposed on nonresidents. States cannot impose an additional continuing education (CE) requirement on nonresident SLI producers.

### The Nonadmitted and Reinsurance Reform Act

The federal Nonadmitted and Reinsurance Reform Act (NRRA) was signed into law by President Barack Obama on July 21, 2010, as part of the federal Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), 12 U.S.C. § 5301. The NRRA set federal standards for the collection of surplus lines premium taxes, insurer eligibility, producer licensing, and commercial purchaser exemptions. Most of the provisions of the NRRA went into effect on July 21, 2011.

For licensing of surplus lines brokers, the most significant change was to limit the licensing requirements to only the home state of the insured. Specifically, to place a surplus lines multistate risk policy, the broker only needs to be licensed as a surplus line broker in the insured's home state, not in all of the states where the policy risk is located. The NRRA defines the home state of the insured as "(i) the state in which an insured maintains its principal place of business or, in the case of an individual, the individual's principal residence; or (ii) if 100% of the premium of the insured risk is located out of the state referred to in clause (i), the state to which the greatest percentage of the insured's taxable premium for that insurance contract is located." The definition goes on to clarify that, with respect to affiliated groups, "[i]f more than one insured from an affiliated group are named insureds on a single non-admitted insurance contract, the term 'home state' means the home state, as determined pursuant to [clauses (i) and (ii) above], of the member of the affiliated group that has the largest percentage of premium attributed to it under such insurance contract."

The NRRA also prohibits a state from collecting fees relating to the licensing of a surplus lines broker unless the state participates in the NAIC's national insurance producer database for surplus lines broker licensure by July 21, 2012. Currently, all states accept applications and renewals for surplus lines broker licenses for individuals through the National Insurance Producer Registry (NIPR), and all but one state accept applications and renewals for surplus lines broker licenses for business entities.

## **Surplus Lines Distribution Systems**

SLI is generally produced through one of two distribution systems. One, generally referred to as a retail distribution system, involves a single broker accessing the surplus lines company directly to place insurance. The second, generally referred to as a wholesale distribution system, involves a surplus lines broker that operates as an intermediary between a “retail agent” and a surplus lines company. In the retail distribution system, there is only one producer in a transaction, so that producer would need to conduct the diligent search of the admitted markets prior to accessing the surplus lines markets, unless there is some exception, such as a large commercial purchaser or an export list. In the wholesale distribution system, the diligent search is often conducted by the retail broker, who determines that there is no admitted market prior to contacting the surplus lines wholesale broker; however, some states have different requirements.

The vast majority of the states take the position that a broker conducting a diligent search would need a P/C agent’s license because it is necessary to solicit insurance, take an application, and make a submission to an admitted company. Many states do not require a retail producer to obtain a surplus lines broker’s license unless the broker is going to access the surplus lines companies directly. There are a couple of states that require a retailer to have a surplus lines license before using the services of a surplus lines wholesale broker.

## **Diligent Search Requirements**

The vast majority of states require a “diligent search” of the admitted market to determine if there is an admitted carrier willing to write the risk, prior to accessing the surplus lines markets. A couple of states have abolished the diligent search requirement. Many states require that brokers search those admitted companies that are actually writing the coverages sought. If there is no admitted carrier willing to write the risk, the risk can be placed in the surplus lines markets. Many states require an affidavit to be completed documenting that the diligent effort was completed. Recently, a number of states have replaced the affidavit, which was sworn under penalty of perjury, with a report from the surplus lines licensee that the diligent search was conducted. Some states have also replaced the requirement that the affidavit, or report, be filed with the insurance department or Surplus Line Association (SLA) with a requirement that the report of the diligent search be maintained in the office of the broker and available for audit by the insurance department.

Many states specify that the diligent search can be conducted by the retail broker, commonly called producing broker, when a surplus lines wholesaler accesses the surplus lines markets. The retail broker has access to admitted markets. The retailer uses the services of a surplus lines wholesale broker only after the retail broker has determined that the admitted markets are not willing to underwrite the risk.

The most common diligent search standard requires declinations from three admitted carriers, but as many as five are required. Other states simply require the producing broker to make an effort, a reasonable effort or a good faith effort, to place the coverage in the admitted markets. A couple states require that the insurance not be procurable after a diligent effort has been made to place the coverage among a majority of insurers, but this standard has been called into question as unclear and impractical. A number of exceptions to the diligent search requirement exist in state law, and the NRRA implemented a national exception to the diligent search rules for insureds that qualify as exempt commercial purchasers (ECPs). Twenty-two states have laws authorizing an “export list” of coverages that the insurance commissioner has determined are not generally available in the admitted markets. Coverages on the export list can be placed in the surplus lines market without a diligent search. In some states, the state insurance department is required to conduct an annual public hearing regarding the export list. The purpose of the hearing is to take testimony on the export list to determine whether any items should be added or removed.

The former NARAB (EX) Working Group updated the NAIC’s standard for determining compliance with the GLBA’s previous reciprocity provisions. In a report that was adopted by the NAIC in September 2009, the Working Group refined its approach to reciprocity relating to any underlying P/C licensing requirements for nonresident surplus lines producers. The Working Group determined that if a state requires the surplus lines producer to perform the diligent search of the admitted market, then the state may require the nonresident surplus lines producer to obtain an underlying nonresident P/C license in addition to a nonresident surplus lines license. However, the Working Group determined that a state may not require a nonresident surplus lines producer to also obtain a nonresident P/C license if they do not perform the diligent search. Many surplus lines producers do not

perform diligent searches because the retailer has already conducted the diligent search, and the law does not require a second diligent search. In such instances, the surplus lines producer is not accessing the admitted market. Consequently, the Working Group determined that it was inconsistent with the previous GLBA reciprocity requirements to require an underlying P/C license for a surplus lines wholesale broker unless they are required by law to conduct a diligent search or conduct diligent searches in their agency.

The NRRA established a single ECP exemption from state diligent search requirements that is applicable in every state. As of July 21, 2011, a diligent search in the admitted market is not required to place a policy for an ECP if: 1) the broker has disclosed to the ECP that coverage may be available from the admitted market, which may provide greater protection with more regulatory oversight; and 2) the ECP has requested in writing that the broker procure/place such coverage with a surplus lines insurer.

An ECP is defined in the NRRA as a purchaser of commercial insurance that:

1) employs or retains a qualified risk manager to negotiate insurance coverage; 2) has paid aggregate nationwide commercial P/C insurance premiums in excess of \$100,000 in the immediately preceding 12 months; and 3) meets at least one of the following criteria: (i) possesses a net worth in excess of \$20 million (as adjusted for inflation); (ii) generates annual revenues in excess of \$50 million (as adjusted for inflation); (iii) employs more than 500 full-time employees per individual insured or is a member of an affiliated group employing more than 1,000 employees in the aggregate; (iv) is a not-for-profit organization or public entity generating annual budgeted expenditures of at least \$30 million (as adjusted for inflation); or (v) is a municipality with a population of more than 50,000.

A number of states elected to maintain their statutory exemptions from diligent search requirements, which were sometimes known as industrial insured exemptions. If the state's industrial insured exemption was more liberal than the NRRA ECP exemption, then the state's requirements were not in conflict with the NRRA, and the exemption in the NRRA would not apply.

SLI producers are routinely subject to additional state administrative requirements that are considered to be outside the scope of licensing reciprocity considerations or the ULS. The regulations regarding the administration of surplus lines are different from other types of insurance (TOIs) because states typically require the licensed surplus lines producers to perform certain compliance activities that would usually be the responsibility of the licensed insurance company in a transaction in the admitted market. In a surplus lines transaction, the compliance obligations are imposed upon the producer because the producer is the licensed party. The surplus lines insurer is unlicensed and often referred to as a "nonadmitted insurer" in some states or "unauthorized insurers" in other states.

There are additional administrative requirements in some states for licensed surplus lines producers that apply once the coverage is placed. These may include:

1. Filing reports with state insurance departments or state stamping offices of placements made.
2. Collecting and paying surplus lines premium taxes.
3. Maintaining a record of all surplus lines placements made.
4. Providing the insured with a disclosure stating that the policy he or she has purchased is being issued by an insurer that is not licensed in the state, is not subject to the financial solvency regulation and enforcement that apply to the state's licensed insurers, and does not participate in any of the insurance guarantee funds created by the state's law.
5. Using a designated stamping office.
6. Including declaration or binder pages with the surplus lines tax filings.
7. Filing a report stating that no policies were written that are known as "zero reports," as discussed later in this section.

In order for a producer to place business in the surplus lines market, the producer must first determine that the company is an eligible surplus lines company in a given state. Most states require that a surplus lines company be deemed "eligible" by meeting certain financial criteria or by having been designated as "eligible" on a state-maintained list. Prior to the enactment of the NRRA, state eligibility standards varied widely from state to state.

As of July 21, 2011, a surplus lines transaction is subject only to the eligibility requirements of the NRRA. The NRRA eligibility requirements are based on two provisions from the *Nonadmitted Insurance Model Act* (#870).

Specifically, the NRRA requires surplus lines carriers to comply with Section 5A(2) and Section 5C(2)(a) from Model #870, which require an insurer to be authorized in its domiciliary state to write the TOI that it writes as surplus lines coverage in the state where it is eligible and to have capital and surplus, or its equivalent, under the laws of its domiciliary jurisdiction equaling the greater of: 1) the minimum capital and surplus requirements under the law of the home state of the insured; or 2) \$15 million. The insurance commissioner in the insured's home state may reduce or waive the capital and surplus requirements down to a minimum of \$4.5 million after the insurance commissioner makes a finding of eligibility based on several factors set out in Model #870, such as the quality of management, the surplus of a parent company, and the reputation within the industry.

In addition to eligibility requirements for U.S. domiciled insurers, the NRRA requires states to permit the placement of surplus lines coverage with surplus lines companies organized in a foreign country, alien insurers, that are listed on the NAIC *Quarterly Listing of Alien Insurers*. The states cannot prohibit a broker from making a placement with an NAIC-listed alien insurer. A state also may allow placement of coverage with alien insurers not on the NAIC *Quarterly Listing of Alien Insurers*. A number of states have authority to individually approve an alien carrier that is not listed on the NAIC *Quarterly Listing of Alien Insurers*.

The NAIC *Quarterly Listing of Alien Insurers* is available for reference and download on the NAIC Products – AVS, Data & Publications website at [http://www.naic.org/prod\\_serv\\_alpha\\_listing.htm](http://www.naic.org/prod_serv_alpha_listing.htm).

### Premium Taxes

Surplus lines premium tax generally is the obligation of either the policyholder or the surplus lines producer, depending on the applicable state law. In all states, the producer or the insured, rather than the insurance company, remits the surplus lines tax. If the policy covers risks that are located entirely in one state, the tax is assessed at that state's tax rate.

Under the NRRA, the home state of the insured has sole regulatory authority over the collection of surplus lines premium taxes. The NRRA prohibits any state other than the home state of the insured from requiring any premium tax payment for SLI.

The NRRA permitted, but did not require, allocation of the surplus lines taxes among the states where the exposure was located. The states initially pursued three different approaches to allocation of taxes following the adoption of the NRRA: 1) the Nonadmitted Insurance Multi-State Agreement (NIMA); 2) the Surplus Lines Insurance Multi-State Compliance Compact (SLIMPACT); and 3) taxing and keeping 100% of surplus lines premium tax on policies in the home state of insureds. NIMA is no longer operational, and SLIMPACT never became operational. The prevailing rule is that states are taxing and keeping 100% of the premium. The NRRA requires surplus lines brokers to adhere to the law of the home state of the insured to determine the amount of premium tax owed on a surplus lines transaction and for any other regulatory requirements the state may require in connection with the payment of the premium tax, such as the timing of tax payments and whether the state requires the submission of risk allocation information for multistate transactions. The NRRA requires surplus lines brokers to submit the premium tax payment on a surplus lines transaction only to the insured's home state. In the case of a state that has joined NIMA, the payment will be made to the clearinghouse in accordance with the home state's law. Should SLIMPACT become operational, it could also elect to require multistate payments to be made to the clearinghouse.

Many states require brokers to submit documentation regarding allocation by state of the risks covered by a surplus lines transaction. If the home state of the insured is a state that has joined NIMA, the broker will be required to use the NIMA risk-allocation formula. If the home state is a state that has joined SLIMPACT, the broker will be required to use the SLIMPACT risk-allocation formula. As of May 2013, both NIMA and SLIMPACT have adopted the same allocation formula. Other states require the broker to submit allocation data in accordance with individual state laws and regulations, but the vast majority of states do not require allocation data because there are very few states allocating

premium at this time. In some states, taxes are paid to a state agency other than the insurance department, such as the department of revenue.

### **Guaranty Fund Warning**

Nearly all states require a disclosure regarding the unavailability of guaranty fund coverage for a surplus lines policyholder, even if the state represents a small portion of the risk. Prior to the NRRA, when a multistate risk was involved, the company would be required to include several pages of guaranty fund notices, many of which had nearly the same language, with minor variations. Brokers may choose to continue to use this approach following the enactment of the NRRA, but the NRRA initiated a compliance system that requires compliance only with laws of the home state of the insured.

As an example, a typical disclosure statement is as follows:

#### **NOTICE TO POLICYHOLDER**

**This contract is issued, pursuant to Section \_\_\_\_ of the (State) Insurance Code, by a company not authorized and licensed to transact business in (State), and as such, is not covered by the (State) Insurance Guaranty Fund.**

After review of this and other issues by a special NAIC subgroup in 2006, the Producer Licensing (EX) Working Group adopted its recommendation that, on a multistate risk, the home state's disclosure should fulfill all other states' disclosure requirements.

### **Stamping Offices**

Stamping offices are entities that are not governmental agencies but whose existence is authorized by law. These offices act as the liaison between the surplus lines producer and the state insurance departments. The stamping offices have varied responsibilities, which may include evaluation of insurance companies for inclusion on a white list, review of surplus lines policies, and education. Stamping offices also provide reports of premiums and taxes to the state insurance department.

Stamping offices are nonprofit and funded by stamping fees assessed on each policy of SLI written in the state. As of April 2017, there are stamping offices in 14 states.

### **Zero Reports**

In some of the states, a producer is required to file a report, known as a "zero report," stating that the producer has not placed any SLI business during a specified time period.

In 2006, a special NAIC study group documented that five states require this report monthly, 12 quarterly, seven semi-annually, and 27 annually. States also use the reports for different recording purposes, so it was not determined if it would be possible to eliminate these reports altogether. However, the study group concluded and recommended to the Working Group that zero reports be eliminated. The study group also recommended further study to determine the feasibility of any other use of a zero report. As of January 2017, the Working Group has not taken any formal action on this issue.



## Chapter 11

### Appointments

An appointment is a registration with the state insurance department that a producer is acting on behalf of an insurer. The *Producer Licensing Model Act* (#218) contains several sections related to appointments. Section 14 of Model #218 establishes the requirement that a producer acting as an agent of an insurer must have an appointment. This is an optional provision and applies only in those states that require appointments. Section 15 of Model #218 establishes a procedure for the reporting of appointment terminations. The Gramm-Leach-Bliley Act (GLBA), as modified in 2015, prohibits any state other than a producer's home state from imposing any appointment requirements upon a member of the National Association of Registered Agents and Brokers (NARAB).

In 2002, the Producer Licensing (EX) Working Group adopted a uniform appointment process. The full text is included in the Appendices and is available on the Working Group's web page. This process is referred to in the Uniform Licensing Standards (ULS). The key elements include:

1. States should allow the electronic filing of appointments and appointment terminations. Paper filings are discouraged.
2. States should establish a billing system for payment by insurers of initial appointments.
3. States shall allow insurers to select the effective date of the initial appointment.
4. States shall require insurers to follow a prescribed timeline to file appointments.
5. States shall require only one appointment or termination form or transaction per producer per company. At this writing, appointments by company group are not available.
6. States shall require insurance companies to submit terminations to the insurance department in accordance with the requirements of Section 15 of Model #218.
7. States shall require that, if a producer is terminated for cause, the insurer must submit supporting documentation. Any information received by the insurance department must remain confidential in accordance with Section 15 of Model #218.

In states that renew appointments, the key elements include:

1. States shall provide or publish a pre-renewal notice to insurers informing them that appointment renewals are imminent.
2. At the time for renewal, a state will deliver an invoice. The invoice may not be altered, amended, or used for appointing or terminating producers.
3. Insurers shall return the invoice and the payment to the department or its designee.
4. States shall establish a dispute resolution process to accommodate errors after the fact.

### Appointment Terminations

Section 15 of Model #218 imposes a requirement on insurers to report terminations of producer appointments. Section 15 requires that the insurer report a termination within 30 days of its occurrence. If a termination is for any of the reasons listed in Section 12, License Denial, Non-Renewal or Revocation of Model #218, insurers are required to submit a detailed report to the state and a copy of the report to the producer. Section 15(E) grants immunity from civil liability for good-faith reporting to insurers and state insurance regulators. Reports filed under Section 15 are considered confidential.

#### Recommended Best Practices for State Insurance Regulators

- Automatically terminate appointments if a license goes inactive for any reason.
- Eliminate fees for appointment terminations and instead assess all charges at the time of an appointment. This will eliminate delays in cancellations.
- Do not require an appointment as a condition of licensure. Model #218 and the ULS provide that a producer can hold a license without holding an active appointment.

- Require only one appointment or termination form or transaction for each company for each producer per state.
- Sub-appointments and Business Entity appointments are discouraged.
- Immediately accept terminations for cause and refer them for investigation. States should follow the procedures as outlined in Model #218. No advance notice should be required to the producer or the state insurance department.
- Use electronic filing for appointments, terminations and renewals, to the extent possible, to eliminate delays and increase efficiency.

## Chapter 12

### Business Entities

Prior to the *Producer Licensing Model Act* (#218), most states used the term “insurance agency” to refer to the business structure used by insurance producers. Under Model #218, the term “business entity” (BE) is used. This term is intended to cover a broad range of legal business operating structures. BEs are considered to be producers under Model #218.

Section 2(A) of Model #218 defines a BE as a corporation, association, partnership, limited liability company, limited liability partnership, or other legal entity.

The Producer Licensing (EX) Working Group has adopted a uniform application form that is the standard for all states for resident and nonresident BE applications. Section 6(B) of Model #218 provides further guidance about the licensing of BEs:

A BE acting as an insurance producer is required to obtain an insurance producer license. Application shall be made using the Uniform Business Entity Application. Before approving the application, the insurance commissioner shall find that:

1. The BE has paid the fees set forth in [insert appropriate reference to state law]; and
2. The BE has designated a licensed producer responsible for the BE’s compliance with the insurance laws, rules and regulations of this state.

Since BEs are considered producers, the reciprocity issues discussed in other sections also apply to BEs. States should not require additional attachments to the application that might interfere with reciprocity.

A common issue that arises with resident and nonresident BE licensing is the role of the secretary of state (SOS) and the state corporation statutory requirements. Most states have adopted a Model Corporation Law that requires resident and nonresident businesses to register with the state corporation department. The issue for state licensing directors is whether the state insurance department should require some proof of registration with the SOS as a pre-condition to licensing. The NAIC legal department has studied this issue extensively and advised the Working Group that states should not require items such as articles of incorporation or proof of registration with the SOS as a pre-condition to licensing for nonresident BEs.

Model #218 does require that all producers, including BEs, notify the insurance commissioner prior to using an assumed name. Section 10 of Model #218 states:

An insurance producer doing business under any name other than the producer’s legal name is required to notify the insurance commissioner prior to using the assumed name.

The uniform appointment process, as adopted by the Working Group, does not specifically address BEs. Section 14 of Model #218 states that a producer acting as an agent of an insurance company must be appointed. States vary in the interpretation of these guidelines. This issue is one that the Producer Licensing (EX) Task Force considered in 2010 as part of its efforts to streamline BE licensing. In the absence of specific guidance from the Working Group, the guidelines discussed in the paragraphs below are suggested.

State insurance regulators should balance the cost of a regulatory requirement with the benefit that requirement adds to consumer protection. If detailed information is collected, such as several levels of appointments, that information should be a meaningful part of the state insurance department’s consumer protection plan. If information is only rarely used in support of investigations, it may not be cost-effective to collect that information and require staff to compile it and process it. During a recent assessment of state insurance department licensing units, it was often found that

information about affiliations and branch offices often required at the time of application was rarely used. Sub-appointments and BE appointments are discouraged.

Just as the uniform appointment process contemplates that only one appointment will be required for an individual producer no matter how many types of products that producer sells for a given company, if a state requires appointments for a BE, then the state should require only one appointment per BE per company, no matter how many types of products that BE sells for a given company.

Section 6(B)(2) of Model #218 requires a BE to designate a licensed producer as responsible for compliance. This is commonly referred to as the designated responsible producer (DRP). There is no provision in Model #218 to require multiple DRPs if the BE chooses to write multiple lines of insurance. For example, if a DRP holds a life line of authority (LOA) only, and an affiliated producer is authorized to sell property/casualty (P/C) products, it is not necessary for a DRP with a P/C LOA to be named as a second DRP.

Model #218 does not give specific guidance on appropriate action to take when a notification is received that the DRP has lost their home state license. A recommended practice is to send a notification to the BE and inform it that the BE license will go inactive unless a new DRP is named and approved within a reasonable number of days.

A BE has an ongoing responsibility to report misconduct of the BE or any of its affiliated producers. Section 12(c) of Model #218 states:

The license of a BE may be suspended, revoked or refused if the insurance commissioner finds, after hearing, that an individual licensee's violation was known or should have been known by one or more of the partners, officers or managers acting on behalf of the partnership or corporation and the violation was neither reported to the insurance commissioner nor corrective action taken.

#### **Recommended Best Practices for State Insurance Regulators**

- Use the NAIC uniform application for BEs, and eliminate all other state-specific forms.
- Review all state insurance laws and regulations, and amend any that require attachments that might violate reciprocity.
- Review the practical consumer protection value of all information collected, and collect only information that adds value.
- Require only one DRP per BE.
- If appointments are required for a BE, require only one appointment per state, and require no sub-appointments.
- Use electronic filings for more efficiency.

## Chapter 13

### Temporary Licenses

Section 11 of the *Producer Licensing Model Act* (#218) contains a provision that allows a state insurance director to issue a temporary license to the survivor of a producer if the insurance commissioner deems it necessary for servicing the deceased producer's customers.

The license is limited to 180 days and also may be limited in scope by the insurance commissioner. The intent of this section is to wind up the business affairs of the producer and not indefinitely continue the decedent's insurance business.

Model #218 gives three examples of persons eligible for a temporary license:

1. The surviving spouse or court-appointed personal representative of a licensed insurance producer who dies or becomes mentally or physically disabled to allow adequate time for the sale of the insurance business owned by the producer, the recovery or return of the producer to the business, or the training and licensing of new personnel to operate the producer's business.
2. A member or employee of a business entity (BE) licensed as an insurance producer, upon the death or disability of an individual designated in the BE application or the license.
3. The designee of a licensed insurance producer entering active service in the armed forces of the U.S.

The insurance commissioner is also given discretion to grant a temporary license in any other circumstance where the insurance commissioner deems that the public interest will best be served by the issuance of this license. The insurance commissioner may also require the temporary licensee to have a licensed producer as a sponsor.



**Part I              Insurance Producer Licensing**

**Section C          License Continuation**

- Chapter 14        Continuing Education
- Chapter 15        Reporting of Actions and Compensation Disclosure
- Chapter 16        License Renewal and Reinstatement
- Chapter 17        Post Licensing Producer Conduct Reviews



## Chapter 14

### Continuing Education

The completion of continuing education (CE) is the method used by state insurance regulators to ensure continued competence of producers. Under the previous Gramm-Leach-Bliley Act (GLBA) reciprocity requirements, a state had to recognize a producer's completion of a CE requirement in the producer's home state as satisfying the other state's CE requirement for license renewal. The only exception was if the producer's home state refused to provide reciprocity to another state.

Some states have adopted special training requirements for specific lines of insurance. When such a requirement exists, it is typically imposed on resident and nonresident producers selling a specific insurance product. A specific CE standard, which is derived from federal mandates, may be imposed on nonresidents, such as for long-term care (LTC), flood, or crop insurance, and it would not violate the Uniform Licensing Standards (ULS).

Section 16(B) of the *Producer Licensing Model Act* (#218) specifically states:

A nonresident producer's satisfaction of his or her home state's CE requirements for licensed insurance producers shall constitute satisfaction of this state's CE requirements if the nonresident producer's home state recognizes the satisfaction of its CE requirements imposed upon producers from this state on the same basis.

Under the ULS, producers are to complete 24 credits of CE for each biennial compliance period. Three of the 24 credits must be in ethics. Fifty minutes is equal to one credit hour of CE. If applicable, the CE compliance period should coincide with the license renewal. The ULS indicate that the license term should be tied to the birth date or birth month.

CE is required if the producer holds one of the six major lines of authority (LOAs) contained in Model #218, but it is not required for each LOA. For example, if a producer holds a life and property LOA, the requirement for renewal is 24 credits. If a producer holds only the life LOA, the requirement for renewal is 24 credits. States may limit the subject area requirements for CE. Some states prohibit CE credit for training on sales techniques. Generally, CE is not required for limited lines. Under the ULS, producers may repeat CE courses for credit in successive renewal terms, but they are not permitted to take a course for credit more than once in the same license continuation period. States must accept both classroom study and verifiable self-study. States should not impose a limit on the use of self-study courses.

Producers and CE providers must submit evidence of course completion in the method specified by the insurance commissioner. Some states require the producer to present a certificate of completion at the time of license renewal. Many states require the CE provider to report attendance. Under this system, a producer is required to present only the attendance certificates if there is a discrepancy. Another option is to require producers to self-certify completion and then verify compliance by random desk audits.

Model #218 and the ULS contain two exemptions from CE requirements. The exemptions are an inability to comply due to military service and/or a demonstration of an extenuating circumstance, such as medical disability. States with waivers for professional designations should consider allowing CE credits for filed and approved courses used to obtain and maintain professional designations.

Some states grant an extension instead of an exemption. This decision is left to each state to decide.

### Course Approvals

The Producer Licensing (EX) Working Group has adopted standards for course approval and reciprocity in filing of courses. States are to follow the standards set forth in the Continuing Education Reciprocity (CER) process, as adopted by the Working Group. Under a reciprocity filing, states are to accept the number of credits awarded by another state

and treat a request for reciprocity as a registration. Only the home state of the CE provider is to perform a content review of the course filing. The Appendices contain information on CER and the current filing forms. The most current information on CER can be found on the Working Group's web page.

States vary in their method for course content approval. Some states use outside vendors, and others do the course reviews internally. The Working Group has not adopted any guidelines on methods for approving classroom courses.

The Working Group has adopted guidelines for the approval of online and self-study courses. The goal of these standards is to deliver functional computer-based internet courses that offer quality insurance and/or risk management material in a password-protected online environment.

The key elements are:

1. Material that is current, relevant and accurate, and includes valid reference materials, graphics and interactivity.
2. Clearly defined objectives and course completion criteria.
3. Specific instructions to register, navigate and complete the coursework.
4. Technical support or provider representative available during business hours.
5. A process to authenticate student identity.
6. A method for measuring the student's successful completion of course material and evaluating the learning experience.
7. A process for requesting and receiving CE course-completion certificates.

The standards call for an examination that is proctored by a disinterested third party. The standards also provide several methods to compute the number of credits that should be awarded. The standards also recommend acceptance of courses that are part of a program that is part of a nationally recognized professional designation. For designation courses, the course should receive credit hours equivalent to hours assigned to the same classroom course material.

The Continuing Education Recommended Guidelines on Online and Self-Study is included in the Appendices.

The ULS prohibit CE providers from advertising CE programs until state course approval is received.

The Appendices contain a sample list of questions and answers frequently asked by insurance producers about CE requirements.

### **Continuing Education Providers**

A state should have a process for registering and qualifying persons who wish to be recognized as CE providers. The process should include duties, responsibilities and performance standards for CE providers. An aspiring CE provider should demonstrate an ability to deliver quality instruction and comply with all reporting and course supervision requirements. These standards should also contain the conditions under which a CE provider may be removed from the state's approved provider list.

The Appendices contain a sample outline of instructions to CE providers.

**Recommended Best Practices for State Insurance Regulators**

- Require CE providers to electronically report class attendance to the state insurance department or its designated vendor.
- Set a reasonable deadline for CE providers to deliver electronic reports.
- Require CE providers to promptly issue attendance certificates, or certificates of completion for self-study courses, and require producers to retain them. The certificates should be sent only to the state insurance department in the event of a dispute.
- Provide access for producers and insurers to department records to monitor CE credits on file.
- Implement an audit program to observe and evaluate CE providers and instructors.
- Participate in the NAIC Personalized Information Capture System (PICS) to receive alerts or monitor actions against existing licensees.



## Chapter 15

### Reporting of Actions and Compensation Disclosure

#### Reporting of Actions

Section 17 of the *Producer Licensing Model Act* (#218) requires a producer to report, to all states in which the producer is licensed, any administrative action taken against the producer in another jurisdiction or by another governmental agency in this state within 30 days of the final disposition of the matter. Producers are also required to report any criminal prosecution of the producer taken in any jurisdiction within 30 days of the initial pretrial hearing date.

The challenge for producers is that it can be difficult to ensure that all relevant states received the report. The National Insurance Producer Registry (NIPR) has created an electronic solution, called Reporting of Actions (ROA), to facilitate the distribution of one report to multiple states. States should encourage the use of this electronic process to save time and create an electronic record of timely submission.

State licensing directors should have a method to receive these reports and refer them for investigation. The director should consider giving staff limited authority to review and clear reports that include violations such as traffic citations or certain misdemeanors.

#### Recommended Best Practices for State Insurance Regulators

- Use the Attachment Warehouse/ROA system to receive electronic notifications to alert a state when an individual or business entity producer has added information into the Attachment Warehouse since their initial entry regarding administrative, criminal or civil actions.

#### Compensation Disclosure

Section 18 of Model #218 requires disclosure where the producer receives any compensation from the customer for the placement of insurance or represents the customer with respect to that placement. This section contains several specific definitions and exceptions to the disclosure requirement. The Producer Licensing (EX) Working Group has not developed any formal guidance on the implementation of Section 18, but the NAIC issued a frequently asked questions (FAQ) document to give additional guidance. This FAQ is in the Appendices. State licensing directors should confer with their legal counsel about appropriate methods for implementing this section.



## Chapter 16

### License Renewal and Reinstatement

#### License Renewal

Under the *Producer Licensing Model Act* (#218), the general rule is that a producer license remains in effect unless suspended, cancelled or revoked. All states have a procedure for individual producers to verify compliance with continuing education (CE) requirements. In states that renew licenses, the CE compliance period should coincide with the license renewal.

The Producer Licensing (EX) Working Group has adopted a uniform license renewal application that is recommended for use by states that renew producer licenses. The current version of the application can be found on the Working Group's web page. States should use the data elements from the uniform renewal application, whether renewal is done via paper application or electronically.

The previous reciprocity provisions of the Gramm-Leach-Bliley Act (GLBA) also applied to the license renewal of nonresidents. The process should be similar to initial licensing:

1. The proper application and fee are submitted.
2. If the answers to any of the questions on the renewal application indicate conduct prohibited by Section 12 of Model #218, a state can require additional documentation.
3. No other attachments should be required.

A number of states use the electronic license renewal process. This process automatically checks the NAIC and National Insurance Producer Registry (NIPR) databases to verify the producer's standing in the home/resident state. The NIPR process uses the data elements from the uniform renewal application.

Model #218 contains a special process for producers who cannot comply with CE requirements due to military service or other extenuating circumstances.

#### Reinstatement

Model #218 allows a producer to reinstate a lapsed license within 12 months of expiration. No examination is required as long as the producer was otherwise eligible to renew. Model #218 also provides that a penalty fee can be assessed.



## Chapter 17

### Post Licensing Producer Conduct Reviews

Section 12 of the *Producer Licensing Model Act* (#218) contains a list of 14 reasons a producer may be disciplined. The insurance commissioner is given authority to take administrative action against a producer who commits any of these acts. Disciplinary action may include suspension, revocation or refusal to renew the producer license. Some states have added additional provisions to this list. For example, if a state does not align the continuing education (CE) compliance term with license renewal, it may be necessary to commence an administrative action to suspend the producer's license for failure to timely complete CE. In some states, insurance departments are required to suspend the license of any individual who fails to pay student loans on a timely basis.

States should use caution in adding additional disciplinary reasons and carefully review the requirements of the Uniform Licensing Standards (ULS). The full text of Model #218 can be found in the Appendices.

After a license is issued, a state insurance regulator may become aware of potential violations of Section 12 in several ways:

1. A licensed producer notifies the state insurance regulator of pending criminal charges.
2. The state insurance regulator receives a notice from the NAIC Personalized Information Capture System (PICS) indicating that a nonresident producer failed to disclose criminal charges.
3. A PICS Notice is received of previously unreported administrative action.
4. A letter is received from the producer informing of an administrative sanction by another state or the Financial Industry Regulatory Authority (FINRA).
5. The state insurance regulator receives subsequent arrest or conviction information from the state's department of justice (DOJ).

The following considerations should be taken into account:

1. If the producer is a nonresident, the state insurance regulator should consider what, if any, action was taken by the producer's resident state or FINRA.
2. Whether the criminal charge or administrative action indicates that the producer is or may be a danger to consumers.
3. Whether the charge involves theft or other financial fraud, or involves an activity that threatens the safety of consumers, such that action should be taken immediately to revoke or suspend the producer's license.
4. Whether it is appropriate to contact the producer and request a voluntarily surrender of the license.
5. If the producer failed to report an action, the state insurance regulator should consider contacting the producer and requesting an explanation from the producer. Technical violations (e.g., bad address, failure to timely report, etc.) generally do not merit formal action. However, the failure to report an action in itself can be cause for administrative penalty or a warning letter, depending on the particular state's statutes and regulations.
6. Whether the individual did not disclose previous criminal or administrative actions taken in response to the answers to the background questions on any application.

### License Reinstatement or Reissuance After Disciplinary Action

Reinstatement of a producer license means the producer's previous license is re-activated and will expire at the end of the license term. Reissuance of a license means the issuance of a new license with a full license term.

Reinstatement or reissuance of a license after disciplinary action is usually not automatic. A producer whose license has been revoked or suspended by order, or who forfeited a license in connection with a disciplinary matter, should be required to make a written request to the insurance commissioner for reinstatement or reissuance in accordance with the terms of the order of revocation or suspension or the order accepting the forfeiture.

When a producer's license has been suspended for a period of time that extends beyond the producer's license expiration date, reinstatement is not an option. The producer must request reissuance of a license and should not be allowed to merely apply for a new license by passing an examination and submitting a new application.

The producer's request for reinstatement or reissuance must include sufficient information to allow the insurance department to determine whether the basis of the revocation, suspension or forfeiture of the applicant's license no longer exists and whether it will be in the public interest to grant the request for a new or reinstated license. The burden of proof to establish such facts is on the producer. In most states, the producer will have a right to an administrative hearing if the reinstatement request is denied.

Some states allow a license to be voluntarily forfeited in lieu of compliance with an order of the insurance commissioner. In this scenario, a request for voluntary forfeiture of a license should be made in writing to the insurance commissioner. The written consent of the insurance commissioner is usually required.

Forfeiture of a license is effective upon submission of the request, unless a contested case proceeding is pending at the time the request is submitted. If a contested case proceeding is pending at the time of the request, the forfeiture becomes effective when and upon such conditions as required by order of the insurance commissioner. A forfeiture made during the pendency of a contested case proceeding is usually considered a disciplinary action subject to reporting to the Regulatory Information Retrieval System (RIRS).

### **Collaboration and Referrals Among State Insurance Regulators**

There are several NAIC tools to facilitate communication about enforcement actions among state insurance regulators.

The NAIC's Market Actions (D) Working Group identifies and reviews insurance companies that are exhibiting or may exhibit characteristics indicating a current or potential market regulatory issue that may affect multiple jurisdictions. The Working Group determines if regulatory action should be taken and supports collaborative actions in addressing problems identified.

The NAIC has adopted the *Market Regulation Handbook* to guide state insurance regulators in the conduct of investigations and enforcement activities. The *Market Regulation Handbook* also gives guidance to market conduct examiners on some licensing issues. The Producer Licensing (EX) Working Group has advised examiners that insurers should not be required to keep a hard copy of each individual producer license. Under Model #218 and the *Market Regulation Handbook*, insurers and state insurance regulators are directed to rely on the State Producer Licensing Database (SPLD) to verify license status.

### **Recommended Best Practices for State Insurance Regulators**

- Report all formal final administrative actions to the RIRS regardless of the voluntary forfeiture, fine or penalty amount.
- Use the Central Registration Depository (CRD), SPLD, RIRS, 1033 Application, PICS, and state court records to verify information submitted by applicants. State court records databases may be available online to analysts.
- Check the producer's resident or home state's website or other licensing records to verify actions reported or taken by that state. The NAIC website has a map with links to each state insurance department's website.
- Develop form letters or consent order templates pre-approved by legal staff to be used by experienced licensing staff to propose the settlement of minor violations without the need to involve legal staff.
- Adopt an administrative rule that if an order of revocation or suspension does not contain terms regarding reissuance or reinstatement, an application for reinstatement or reissuance may not be made until at least one year has elapsed from the date of the order or acceptance of the forfeiture of a license.
- Maintain a record tickler system of all special conditions imposed on any producer licenses so that the compliance with the conditions can be reviewed as the end of any special supervision term nears.

## **Part II**

### **Miscellaneous Licenses**

Chapter 18	Adjusters
Chapter 19	Bail Bond Agents
Chapter 20	Charitable Gift Annuities
Chapter 21	Fraternals and Small Mutuals
Chapter 22	Insurance Consultants
Chapter 23	Managed Care Providers
Chapter 24	Managing General Agents
Chapter 25	Multiple Employer Welfare Arrangements
Chapter 26	Reinsurance Intermediaries
Chapter 27	Risk Retention Groups and Risk Purchasing Groups
Chapter 28	Third-Party Administrators
Chapter 29	Title Insurance Agents
Chapter 30	Viatical and Life Settlement Brokers



## Chapter 18

### Adjusters

An adjuster is a person who investigates claims, determines coverage, examines relevant documents, and inspects property damage. An adjuster may also determine the amount of a claim, loss or damage payable under an insurance contract or plan. An adjuster often settles or negotiates settlement of the claim. In some states, the adjuster's authority is limited to a specialty area such as auto, homeowner, workers' compensation or crop insurance.

There are three kinds of adjusters: 1) public; 2) independent; and 3) company, sometimes called staff adjusters. Public adjusters represent the insured, while independent and staff adjusters represent the insurer. More than 30 states require licensure of one or more of these types of adjusters.

Public adjusters directly contract with the person who is seeking coverage or benefits under an insurance policy or other kind of insurance plan. The role of a public adjuster is to represent an insured or claimant in the settlement of a claim. The NAIC has adopted the *Public Adjuster Licensing Model Act* (#228).

Under the model, a public adjuster is defined as:

"Public adjuster" means any person who, for compensation or any other thing of value, acts on behalf of an insured by doing any of the following:

1. Acting for or aiding an insured in negotiating for or in effecting the settlement of a first-party claim for loss or damage to real or personal property of the insured.
2. Advertising for employment as a public adjuster of first-party claims or otherwise soliciting business or representing to the public that the person is a public adjuster of first-party claims for loss or damage to real or personal property of an insured.
3. Directly or indirectly soliciting the business of investigating or adjusting losses, or of advising an insured about first-party claims for loss or damage to real or personal property of the insured.

Staff adjusters are typically salaried employees of an insurer or an insurer's affiliates and do not adjust claims for entities other than their employer or its affiliates. Independent adjusters are self-employed or associated with or employed by an independent firm. Independent adjusters may adjust claims on behalf of many insurers. The NAIC has adopted model guidelines for *Independent Adjuster Licensing Guideline* (#1224) adjusters that states are encouraged to adopt. The Appendices contain the model guideline.

Most states recognize one or more of the following exemptions to adjuster licensing:

1. Attorneys-at-law admitted to practice in this state, when acting in their professional capacity as an attorney.
2. A catastrophe situation officially declared by the insurance commissioner or governor, according to state law. Registration may be required, but no permanent license should be required of a nonresident adjuster who is sent on behalf of an insurer for the purpose of investigating or adjusting a loss or a series of losses resulting from a catastrophe.
3. A person employed solely to obtain facts surrounding a claim or furnish technical assistance to a licensed independent adjuster.
4. An individual who is employed to investigate suspected fraudulent insurance claims but who does not adjust losses or determine claims payments.
5. A person who solely performs executive, administrative, managerial or clerical duties, or any combination thereof, and who does not investigate, negotiate or settle claims with policyholders, claimants, or their legal representative.
6. A licensed health care provider or its employee who provides managed care services as long as the services do not include the determination of compensability.
7. A managed care organization, any of its employees, or an employee of any organization providing managed care services as long as the services do not include the determination of compensability.
8. A person who settles only reinsurance or subrogation claims.

9. An officer, director, manager or employee of an authorized insurer, surplus lines insurer, risk retention group (RRG), or attorney-in-fact of a reciprocal insurer.
  10. A U.S. manager of the U.S. branch of an alien insurer.
  11. A person who investigates, negotiates or settles life, accident and health, annuity, or disability insurance claims.
  12. An individual employee, under a self-insured arrangement, who adjusts claims on behalf of his or her employer.
  13. A licensed insurance producer to whom claim authority has been granted by the insurer.
  14. A person authorized to adjust workers' compensation or disability claims under the authority of a third-party administrator (TPA) license pursuant to [applicable licensing statute].
- Drafting Note: This guideline is drafted to eliminate redundant licensure requirements with respect to the activities engaged in by a licensee. If licensed as an independent adjuster, TPA, or similar business entity (BE), licensees should not be required to obtain separate independent adjuster licenses, provided that the types of claims adjusted do not include life, health, annuity or disability insurance claims.

### **Qualifications of an Adjuster**

States that do require licensure assess the qualifications of potential adjusters in various ways. States use one or more of the following methods to determine that a person has the requisite knowledge to properly adjust claims:

1. Specialized or related education prior to licensure; i.e., prelicensing coursework.
2. A specified amount of experience that is relevant to the kind of adjusting work the applicant will be doing; i.e., property/casualty (P/C), workers' compensation or life/health.
3. A license examination.
4. Relevant professional designation such as the Chartered Property Casualty Underwriter (CPCU) or Associate in Claims (AIC).
5. Prior similar licensure in another state.

For states implementing a new regulatory scheme for adjusters, it is common practice to waive the initial exam for applicants with appropriate credentials and experience.

### **Fitness and Character Considerations**

Like insurance producers, many states also evaluate an applicant's fitness, character and trustworthiness to engage in this aspect of the insurance business. State insurance regulators typically consider:

1. Criminal history.
2. Administrative actions taken by other state insurance regulators.
3. Civil judgments that may shed light on an applicant's character or fiscal integrity.

In some states, an adjuster must apply for a license by line of insurance, or line of authority (LOA), similar to the manner in which producers are licensed. Other states require adjuster licenses by categories such as motor vehicle physical damage, workers' compensation or crop.

States are encouraged to implement a fingerprint requirement for public and independent adjusters similar to what is required of producers. Additionally, if a state permits a nonresident adjuster to designate that state as its home state, fingerprinting of that nonresident should be required. States are encouraged to adopt the *Authorization for Criminal History Record Check Model Act* (#222) when evaluating and considering whether an applicant or licensee has met the character and trustworthiness requirements to obtain, maintain or renew a license.

### **Reciprocity**

In almost every jurisdiction where licensure is required, it is the "home state" insurance regulator who assesses the qualifications of his or her resident adjusters. Based upon securing a license in one's home state, many states will grant a comparable or similar nonresident license to such an individual. This is not the case in all states, and varying

LOAs, qualification standards and license types have created barriers to nonresident licensure. In addition, an adjuster based in a state that does not license adjusters may be required to take exams in multiple states.

**The New NAIC Public Adjuster Model Act (# 228) defines home state as:**

“Home state” means Washington, DC and any state or territory of the U.S. in which the public adjuster’s principal place of residence or principal place of business is located. If neither the state in which the public adjuster maintains the principal place of residence nor the state in which the public adjuster maintains the principal place of business has a substantially similar law governing public adjusters, the public adjuster may declare another state in which it becomes licensed and acts as a public adjuster to be the “home state.”

**Guideline #1224 defines home state as:**

“Home state” means Washington, DC and any state or territory of the U.S. in which an independent adjuster maintains his, her or its principal place of residence or business and is licensed to act as a resident independent adjuster. If the resident state does not license independent adjusters for the line of authority sought, the independent adjuster shall designate as his, her or its home state any state in which the independent adjuster is licensed and in good standing.

There are a few states that will not grant nonresident licensure based upon a person having qualified and passed a license exam in the applicant’s home state. Instead, these states require the nonresident applicant to take an exam in the nonresident state even though the person has taken and passed the license exam in the home state.

Adjuster licensing processes were modeled on producer licensing processes, and in 2011, the NAIC adopted the *Independent Adjuster Reciprocity Best Practices Guidelines* paper, which provides jurisdictions with a model to meet reciprocity requirements, as well as take major steps toward reaching uniformity. The NAIC uniform licensing forms are designed to be used by applicants for adjuster licenses. Producer licensing for nonresidents is predicated on the producer satisfying the requirements for a home state license. Those producer requirements often include prelicensing education and examination. Since, at this writing, 40 states license public adjusters, 33 states license independent adjuster licenses, and only 15 states require company adjusters to be licensed, obtaining nonresident adjuster licenses becomes more complex because adjusters often do not have an underlying resident license. Until states adopt the provision that allows an individual to qualify for licensure by designating another state as the person’s home state or to designate the state in which the application is filed as the person’s home state, obtaining a nonresident adjuster license becomes more complex because adjusters often do not have an underlying resident license.

Some states do not license adjusters. In order for the use of electronic licensing systems, adjusters residing in states that do not license adjusters can select an Adjuster Designated Home State (ADHS). The ADHS is the state in which the adjuster does not maintain his, her or its principal place of residence or business, and the adjuster qualifies for the license as if the person were a resident.

A state whose laws permit a nonresident adjuster to designate that state as its home state will require the nonresident to qualify as if the person were a resident—exam requirements; fingerprinting, if required; and continuing education (CE). Once the individual has met the qualifications, the Designated Home State (DHS) will issue a nonresident license. The Producer Database (PDB) and DHS will list the record as nonresident DHS.

If the resident state of the adjuster does not require an adjuster license, adjusters cannot use the National Insurance Producer Registry (NIPR) ADHS module unless they declare another state to be the home state. NIPR has recently added a new Nonresident Adjuster Licensing (NRAL) application that allows an individual to designate a state other than the resident state as the home state. NIPR contains functionality to allow adjusters that have designated another state as the home state to renew online. Adjusters with any license can update contact information through the NIPR Contact Change Request (CCR) tool.

### **Continuing Education**

Approximately 18 states have CE requirements for their resident adjusters. Reciprocity exists among a majority of these states, but not all, in part as a result of the inconsistency among LOAs granted within each state’s adjuster

licensing scheme. It also becomes problematic when the resident adjuster's home state does not have any CE requirements.

Model #228 and Guideline #1224 contain a CE requirement that the home state shall require 24 hours of CE every two years, with three of the 24 hours covering ethics. It is recommended that a state accept an adjuster's satisfaction of its home state's CE requirements as satisfying that state's CE requirements, provided that the home state recognizes CE satisfaction on a reciprocal basis. For a state that permits a nonresident adjuster to designate that state as its home state, the home state will require and track CE compliance for that adjuster.

### **Emergency/Catastrophic Adjusters**

A state that offers temporary licensure or registration for emergency/catastrophic adjusters are encouraged to follow Guideline #1224 and develop an automated notification or registration procedure that allows for an immediate, streamlined and efficient filing process for adjusters who are seeking authority to adjust claims in the event that an emergency or catastrophe is declared.

### **Non-U.S. Adjusters for Limited Lines Portable Electronics Insurance Products**

Many states license, or are considering licensure for, limited lines portable electronics insurance producers. Because some major portable electronics insurance companies provide claims adjustment services via non-U.S. entities, the issue of licensing adjusters who do not reside in the U.S. has gained increased prominence. Guideline #1224 and Model #228 are silent on the licensing of non-U.S. citizens beyond the requirement to designate a home state. Some states, however, have tax laws or other laws that require licensees and applicants for licenses to submit and maintain a Social Security number (SSN). State license laws that allow for the licensing of non-U.S. adjusters must take this possible barrier to licensure into consideration. States should also require non-U.S. citizens to comply with all necessary qualification requirements, such as passing the resident license examination, if applicable.

### **Recommended Best Practices for State Insurance Regulators**

- Adopt Model #228.
- Adopt Guideline #1224.
- Use the NAIC uniform applications and develop a mechanism for electronic submission and electronic bulk submissions.
- Use the definition of "home state" as defined in Model #228 as the basis of reciprocity.
- Provide resident and nonresident adjuster licensing requirements on forms, websites, and the State Producer Licensing Database (SPLD).
- Allow electronic payment for residents and nonresidents for authorized submitters, as well as individual adjusters.
- Post applications and license status information on websites and the SPLD
- Eliminate perpetual licenses, eliminate the word "perpetual" from issued licenses, and adopt a biennial renewal process tied to the uniformity standards.
- Adopt the *Independent Adjuster Reciprocity Best Practices Guidelines* paper.
- Use the definition of "home state" as defined in Guideline #1224.
- Participate in the NIPR ADHS application.
- Participate in the NAIC Personalized Information Capture System (PICS) to receive alerts or monitor actions against existing licensees.
- Use the Attachments Warehouse/Reporting of Action (ROA) system to receive electronic notifications to alert a state when an adjuster has added information into the Attachments Warehouse since their initial entry regarding administrative, criminal or civil actions. For nonresidents that designate your state as the "home state," a nonresident license should be issued.
- For nonresidents that designate your state as the "home state," develop internal data fields that will allow the tracking of CE compliance.
- Include a provision in law that prohibits simultaneous licensure as both an independent adjuster and a public adjuster.

- If your state requires a license examination, require applicants for a resident license to pass your own state's examination, not simply use passing results from another's state's examination. However, recognition of an exam taken in another state may be given where a nonresident license is being requested.
- Grant an exemption from the license examination requirement to applicants for the crop LOA who have satisfactorily completed the National Crop Insurance Services (NCIS) Crop Adjuster Proficiency Program (CAPP) or the loss adjustment training curriculum and competency testing required by the Federal Crop Insurance Corporation (FCIC) Standard Reinsurance Agreement (SRA).
- If your state allows non-U.S. citizens to receive a license, ensure that other laws in your state, such as tax laws, do not require every licensee or applicant for a license to submit a SSN or Individual Taxpayer Identification Number (ITIN).



## Chapter 19

### Bail Bond Agents

A bail bond is one method used to obtain the release of a defendant awaiting trial upon criminal charges from the custody of law enforcement officials. A bail bond can be based on an insurance product or collateral. The defendant, the defendant's family and friends, or a professional bail bond agent executes a document that promises to forfeit the sum of money determined by the court to be commensurate with the gravity of the alleged offense if the defendant fails to return for the trial date. A bail bond is considered a three-part contract between the defendant, the government and the insurance company.

Some states regulate bail bonds through the insurance department, and others leave the administration to the discretion of the court system. It is usually required that a bail bond insurer file a power of attorney with the local court authority. This power of attorney is proof to the court that the bail agent is authorized to write bonds for that insurer up to a certain dollar amount.

State insurance departments vary in the manner in which bail bond activities are regulated. There is no NAIC model to guide state licensing directors for bail bond agents. A number of states use the surety line of authority (LOA) to regulate only the bonds that are insurance-based. In other states, a more comprehensive system has been developed that includes examinations, background checks, and personal integrity bonds. The majority of bail bond transactions are executed by resident bail bond agents. Some states prohibit nonresident bail bond agents. In many states, the state court system and local county sheriff may also have a process for approval of bail bond agents.

States that regulate bail bond agents should consider including the following elements in their regulatory scheme:

1. Minimum content and disclosure requirements for the bail bond contract.
2. Detailed record-keeping.
3. Requirement that bail funds be segregated in a trust account.
4. Appointments for all bail bond agents.
5. Written examination.
6. Background check, including fingerprints.
7. Prelicensing education on state laws and bond procedures.
8. Completion of continuing education (CE).
9. Laws that clearly place liability on insurers' appointed bail bond agents who fail to comply with state law on bail bonds and return of collateral.
10. Cross reference the *Producer Licensing Model Act* (#218) and the state's unfair trade practices act to apply penalties for misconduct.
11. Laws that create a fiduciary relationship between the bail bond agent and the criminal defendant.
12. Dialogue with the appropriate state court and law enforcement officials to coordinate efforts at regulating bail bond agents.
13. Adoption of a specific list of prohibited activities by bail bond agents.

### Bond Forfeiture

Forfeiture enforcement may or may not be the responsibility of the state insurance department. In some states, enforcement is left to the court system. This may result in a bail agent's bond privileges being revoked in a particular county. If enforcement is the responsibility of the state insurance department, the state will likely have authority to suspend or revoke the license of a bail agent.

### Prohibited Activities

The following list contains excerpts from several states' laws and regulations regarding bail bond agent licenses. This is a suggested starting point for states to draft a list of prohibited activities for bail bond agents and insurers:

1. Pay, rebate, give or promise anything of value to a jailer, peace officer, magistrate, or any other person who has power to arrest or hold a person in custody, or to any public official or public employee for the purpose of securing a settlement, compromise, remission or reduction of the amount of a bail bond, or to secure delay or other advantage. This section does not prohibit public reward paid for the return of a fugitive.
2. Pay, rebate, give or promise anything of value to an attorney in a bail bond matter, except in defense of an action on a bail bond, collateral or indemnification agreement.
3. Pay, rebate, give or promise anything of value to a defendant or anyone acting on the defendant's behalf in exchange for a referral of bail bond business.
4. Recommend a particular attorney to represent a defendant.
5. Solicit business where a prisoner is confined in or near a courtroom if otherwise prohibited by court order or law.
6. Sign or countersign a bail bond that the licensee did not execute.

### **Immigration Bonds**

An immigration bond guarantees the Immigration and Naturalization Service (INS) that an alien will comply with one of several obligations under U.S. immigration laws. Most often, an immigration bond guarantees the alien while released from U.S. custody during the pendency of the government's case for unlawful entry into the country. An immigration bond can be in the form of a surety product or collateral (see INS Form I-352). With respect to surety products, the underlying guarantee is an insurance product permitted to be issued solely by a licensed insurer. Consequently, an individual selling, soliciting or negotiating an immigration bond must maintain a resident or nonresident producer license in order to legally sell the bond in a state.

States should recognize that immigration bonds are a form of insurance required to be issued by a licensed insurer, and the sale, solicitation and negotiation of immigration bonds constitute activities for which an individual must maintain a license as a resident or nonresident producer under the respective states' licensing laws. New Jersey Bulletin No. 09-09 contains an example of notification regarding appropriate treatment of immigration bonds.

## Chapter 20

### Charitable Gift Annuities

A charitable gift annuity (CGA) is a transfer by a donor to a charitable organization. In return, the donor receives an annuity payable over one or two lives. If the actuarial value of the annuity is less than the value of the property transferred, then the difference in value constitutes a charitable deduction for federal tax purposes. CGAs are not investments. Annuity payments are tax-free partial returns of the donor's gift based on actuarial tables of life expectancy.

To qualify as a charitable organization under the federal law, the entity must be one described in either Section 501(c)(3) or Section 170(c) of the Internal Revenue Code (IRC).

The maximum rates of return that are typically paid on these uninsured annuities are established by the American Council on Gift Annuities (ACGA).

Gift annuity payments are fixed. They never go down or up. CGAs are not insured. A charity could become insolvent and be unable to make annuity payments. Most gift annuities are not protected by any state guaranty fund.

The NAIC has adopted two models to regulate CGAs. The *Charitable Gift Annuities Model Act* (#240) contains a detailed licensing scheme for CGAs. The *Charitable Gift Annuities Exemption Model Act* (#241) calls for a simplified registration mechanism.



## Chapter 21

### Fraternals and Small Mutuals

#### Fraternal Benefit Societies

A fraternal benefit society is a membership organization that is legally required to: 1) offer life, health and related insurance products to its members; 2) be not-for-profit; and 3) carry out charitable and other programs for the benefit of its members and the public. It must be composed of members having a common bond and be organized into lodges or chapters; i.e., local membership groups. A fraternal benefit society exists solely for the benefit of its members and their beneficiaries. Fraternal benefit societies must have a representative form of governance.

Federal law allows a fraternal to offer life and health insurance products. Section 501(c)(8) of the Internal Revenue Code (IRC) defines a fraternal beneficiary society as:

- (a) a nonprofit mutual aid organization;
- (b) operating under the lodge system or for the exclusive benefit of the members of a fraternity itself operating under the lodge system; and
- (c) providing for the payment of life, sick, accident or other benefits to the members of such society, order or association, or their dependents.

Fraternal benefit societies: 1) offer insurance products; 2) are chartered and licensed according to state insurance laws; and 3) are regulated and examined by state insurance departments. Individuals who sell, solicit or negotiate insurance products for a fraternal benefit society are required to obtain a state insurance producer license.

The NAIC has adopted the *Uniform Fraternal Code* (#675). However, this model is not widely in use. At this writing, 45 states had adopted a version of Model #675 as drafted by the National Fraternal Congress of America (NFCA). Both the NAIC model and the NFCA model contain a section about producer licensing that pre-dates the *Producer Licensing Model Act* (#218). States should check the fraternal law that has been adopted in their state and update it to reference Model #218.

#### Small Mutual Insurers

Small mutual insurers are risk-bearing entities that historically formed around common interests of farmers, householders, and ethnic and religious groups. Small mutuals, commonly known as farm mutuals, may also be called “town,” “county” or “state” mutuals.

Small mutuals provide, with only a few exceptions, property insurance for homes, farmsteads, crops, and some small businesses. They do not, except for the legal liability associated with those risks, write casualty insurance. In some states, small mutuals are allowed to offer liability coverage through an affiliation with an insurer. State laws usually limit small mutuals to either a certain premium volume, geographic area or both. Most states also impose a lighter regulatory burden than that applied to larger mutual and investor-owned insurers.

Mutual insurers are owned and operated by the policyholders. Unlike a stock company, a mutual policyholder has an indivisible interest in the enterprise that, in general, cannot be bought or sold like a share of stock. Policyholders are often referred to as “members.” In some cases, a dividend or return of premium is paid when the mutual’s board of directors judges that it has sufficient capital. Members of the board are also policyholders.

Individuals who sell products for small mutuals should be licensed as producers, as outlined in Model #218 and the Uniform Licensing Standards (ULS).



## Chapter 22

### Insurance Consultants

An insurance consultant is a person who charges a fee for giving advice about insurance products. Not all states require a separate consultant license. In those states, the individual can obtain a producer license and abide by the disclosure provisions for insurance consultants. In states that do require a special license, the applicant is usually required to pass an examination. The exam may be either one of the same subject-matter examinations that insurance producers must pass or an examination specific to consultants. In states that require an examination, a waiver may be granted if the applicant can demonstrate a specified amount of insurance experience.

States usually adopt exemptions from the consultant licensing requirement. The exemptions are available as long as the person is acting in his or her professional capacity or in the normal course of business. Common exemptions are:

1. A licensed attorney.
2. A trust officer of a bank.
3. An actuary or certified public accountant.
4. A risk manager who consults for his or her employer only.

If a state requires appointments for insurance producers, appointments should not be required for insurance consultants. The consultant represents the insured and is not an agent of the insurance company. Some states prohibit an individual from holding both an insurance producer license and an insurance consultant license. Other states allow an insurance producer to function in either capacity with full disclosure. In all cases where an individual is acting as an insurance consultant, a written contract should be used to clearly explain the terms of the consultant arrangement.

In states that have a separate insurance consultant license, it is a common practice to have a continuing education (CE) requirement that mirrors the CE requirement for insurance producers.



## Chapter 23

### Managed Care Providers

#### Health Maintenance Organizations

A health maintenance organization (HMO) is a type of managed care organization that provides a form of health care coverage that is fulfilled through hospitals, doctors and other providers with which the HMO has a contract. Unlike traditional health insurance, an HMO sets out guidelines under which doctors can operate. On average, an HMO costs less than comparable traditional health insurance, with a trade-off of limitations on the range of treatments available. Unlike many traditional insurers, HMOs do not merely provide financing for medical care. The HMO actually delivers the treatment as well. Doctors, hospitals and insurers all participate in the HMO business arrangement.

The NAIC has adopted a model law and regulation that governs the licensure of HMOs: the *Health Maintenance Organization Model Act* (#430) and the *Model Regulation to Implement Rules Regarding Contracts and Services of Health Maintenance Organization* (#432). In most cases, access to an HMO is only available to employer group plans.

#### Preferred Provider Organizations

A preferred provider organization (PPO) is a group of doctors and/or hospitals that provides medical service only to a specific group or association. The PPO may be sponsored by a particular insurance company, one or more employers, or some other type of organization. PPO physicians provide medical services to the policyholders, employees or members of the sponsor(s) at discounted rates, and they may set up utilization review programs to help control the cost of medical care.

In some states, managed care providers may be licensed by an agency outside the insurance department.



## Chapter 24

### Managing General Agents

A managing general agent (MGA) is an insurance producer authorized by an insurance company to manage all or part of the insurer's business in a specific geographic territory. Activities on behalf of the insurer may include marketing, underwriting, issuing policies, collecting premiums, appointing and supervising other agents, paying claims, and negotiating reinsurance. Many states regulate the activities and contracts of MGAs.

The NAIC has adopted the *Managing General Agents Act* (#225) to guide the states in regulating MGAs. Under the model, an MGA is defined as any person who engages in all of the following:

1. Negotiates and binds ceding reinsurance contracts on behalf of an insurer or manages all or part of the insurance business of an insurer—including the management of a separate division, department or underwriting office—and who acts as an agent for such insurer whether known as a managing general agent, manager or other similar term or title.
2. With or without authority and either separately or together with affiliates, directly or indirectly produces and underwrites an amount of gross direct written premium equal to or greater than 5% of the policyholder surplus in any one quarter or year, as reported in the last annual statement of the insurer.
3. Engages in either or both of the following:
  - (a) Adjusts or pays claims in excess of an amount determined by the insurance commissioner.
  - (b) Negotiates reinsurance on behalf of the insurer.

Under the model, an MGA does not include any of the following:

1. An employee of the insurer.
2. A manager of a U.S. branch of an alien insurer who resides in this country.
3. An underwriting manager who, pursuant to contract, manages all insurance operations of the insurer, who is under common control with the insurer, subject to [cite to state law] relating to the regulation of insurance holding company systems, and who is not compensated based upon the volume of premiums written.
4. An insurance company, in connection with the acceptance or rejection of reinsurance on a block of business.
5. The attorney-in-fact authorized by or acting for the subscribers of a reciprocal insurer or interinsurance exchange under a power of attorney.

In most states, MGAs must be licensed as producers and are not allowed to place business until a written contract exists among all parties. Under Model #225, insurers are required to monitor the financial stability of MGAs under contract.



## Chapter 25

### Multiple Employer Welfare Arrangements

Multiple employer welfare arrangements (MEWAs) are arrangements that allow a group of employers to collectively offer health insurance coverage to their employees. MEWAs are most often found among employer groups belonging to a common trade, industry or professional association.

MEWA plans are generally available to the employees, and sometimes their dependents, of the employers who are part of the arrangement. People who do not have an employment connection to the group cannot obtain coverage through the MEWA plan. MEWA plans cannot be sold to the public.

To qualify as an MEWA, the organization must be nonprofit, in existence for at least five years and created for purposes other than that of obtaining health insurance coverage. In other words, employers cannot group together solely for the purpose of offering health insurance. However, employers that have already grouped together for another common purpose (e.g., a trade association) may also offer health insurance coverage to their member employers.

States and the federal government coordinate the regulation of MEWAs pursuant to a 1982 amendment to the federal Employee Retirement Income Security Act (ERISA). This dual jurisdiction gives states the primary responsibility for overseeing the financial soundness of MEWAs and the licensing of MEWA operators. The U.S. Department of Labor (DOL) enforces the fiduciary provisions of ERISA against MEWA operators to the extent that a MEWA is an ERISA plan or is holding plan assets. State insurance laws that set standards requiring specified levels of reserves or contributions are applicable to MEWAs even if they are also covered by ERISA.

The NAIC has adopted a model regulation, *Prevention of Illegal Multiple Employer Welfare Arrangements (MEWAs) and Other Illegal Health Insurers Model Regulation (#220)*, to give guidance to the states in the supervision of MEWAs.

## Chapter 26

### Reinsurance Intermediaries

A reinsurance intermediary acts as a broker in soliciting, negotiating or procuring the writing of any reinsurance contract or binder. Reinsurance intermediaries act as insurance producers in accepting any reinsurance contract or binder on behalf of an insurer.

The NAIC has adopted the *Reinsurance Intermediary Model Act* (#790), which contains a simplified registration process for nonresident reinsurance intermediaries. Nonresident reinsurance intermediaries verify that they are licensed in their home states under similar laws as in the nonresident states—i.e., Model #790—and the nonresident reinsurance intermediaries are granted reciprocity.

## Chapter 27

### Risk Retention Groups and Risk Purchasing Groups

#### Risk Retention Groups

The U.S. Congress (Congress) enacted the federal Risk Retention Act (RRA) in 1981. This federal law enabled product sellers to form risk retention groups (RRGs) to provide group self-insurance. RRGs are insurers licensed and fully regulated in one state pursuant to that state's laws. In the mid-1980s, general liability insurance premiums skyrocketed, and certain lines were unavailable. Coverage for some classes of businesses was typically either unavailable or extremely expensive for the desired limits and coverages. Congress intervened again in 1986, this time expanding the RRA to permit RRGs to cover broader liability risks. The RRA is now referred to as the federal Liability Risk Retention Act (LRRA).

Under the *Model Risk Retention Act (#705)*, an RRG “registers” in non-domicile states and is then exempt from most insurance laws in non-domicile states. RRGs are limited to providing non-workers’ compensation commercial lines liability insurance to its members. All owners of an RRG must be insureds, and all insureds must be owners.

RRGs can be required by states to:

1. Comply with the unfair claim settlement practices law.
2. Pay applicable premium and other taxes that are levied on admitted insurers and surplus lines insurers, brokers or policyholders.
3. Participate in residual market mechanisms.
4. Register and designate the insurance commissioner as agent for service.
5. Submit to a financial examination in any state in which the group is doing business if:
  - a. The domiciliary insurance commissioner has not begun or refused to initiate an examination.
  - b. Any examination shall be coordinated to avoid unjustified duplication and repetition.
6. Comply with a lawful order issued in a delinquency proceeding commenced by the insurance commissioner if there has been a finding of financial impairment or in a voluntary dissolution proceeding.
7. Comply with deceptive, false or fraudulent acts or practices laws, except if the state seeks an injunction regarding the conduct, it must be from a court of competent jurisdiction.
8. Comply with an injunction issued by a court of competent jurisdiction, upon a petition by the state insurance commissioner alleging that the group is in hazardous financial condition or is financially impaired.
9. Provide the following notice, in 10-point type, in any insurance policy:

#### NOTICE

**This policy is issued by your risk retention group (RRG). Your RRG may not be subject to all of the insurance laws and regulations of your state. State insurance insolvency guaranty funds are not available for your RRG.**

A state may require that a person acting, or offering to act, as a producer or broker for an RRG obtain a license from that state, except a state may not impose any qualification or requirement that discriminates against a nonresident producer or broker.

#### Risk Purchasing Groups

The second type of entity allowed to operate under the RRA is a risk purchasing group (RPG). RPGs are vehicles for any insurer to market on a group basis, with the ability to discriminate as to rates for those groups. But as with RRGs, RPGs are only allowed to place liability coverage. RPGs are formed so that similar risks may pool purchasing power. RPGs are purchasing entities, not insurers, and are not generally subject to state insurance laws.

Insurance departments generally do not actively regulate RPGs. The insurer writing for an RPG is subject to all insurance laws, with few exceptions. The transaction of insurance for an RPG in a state generally follows a traditional transaction based on the form of the insurer in relation to that state. Hence, if the insurer is licensed in the state, then producer licensing and, if applicable, appointment procedures apply. If the insurer is a writer of surplus lines, then the traditional surplus lines producer licensing rules apply. As with RRGs, a state may require that a person acting, or offering to act, as a producer or broker for a purchasing group obtain a license from that state. A state may not impose any qualification or requirement that discriminates against a nonresident producer or broker.

## **Chapter 28**

### **Third-Party Administrators**

A third-party administrator (TPA) is an entity that directly or indirectly underwrites, collects charges or premium from, or adjusts or settles claims on residents of a state, in connection with life, annuity or health coverage offered or provided by an insurer, unless accepted by statute.

When an employer offers its employees a self-funded health care plan—the employer helps finance the health care costs of its employees—the employer often contracts with a TPA to administer the plan. The employer may also contract with a reinsurer to pay amounts in excess of a certain threshold in order to share the risk for potential catastrophic claims experience.

In most states, a TPA is required to register with the state. Some states require a bond. The TPA is required to answer inquiries from the state insurance department, but, if the TPA is working for a self-funded Employee Retirement Income Security Act (ERISA) plan, a state has limited authority to take enforcement action against the TPA. An insurer may also act as a TPA for certain customers. This can be confusing to a consumer who has an identification card that has a name similar to a well-known health insurance company. The consumer often thinks coverage is provided by that insurance company instead of the employer plan.



## Chapter 29

### Title Insurance Agents

Title insurance is insurance indemnifying against financial loss from defects in title of real property arising from conditions of title that exist on the date of issuance of the policy. While most insurance coverage indemnifies insureds against loss caused by future events, title insurance is unique, as it focuses on the elimination of risk before the policy is issued. Title insurance policies are typically purchased when real property is conveyed or financed. Insureds pay one premium for coverage that has no expiration. In many states, title insurance has essentially replaced abstracts of title, and it is often required as a condition for obtaining a loan secured by a lien on real property.

Title insurance policies commonly guarantee or indemnify the fee title of owners or the lien priority of a lender from losses or damages from liens, encumbrances, defects or unmarketability of title, or adverse claims to title in the real property, and defects in the authorization, execution or delivery of an encumbrance on the real estate. Coverage is subject to standard exceptions, as well as specific exclusions listed on a schedule attached to the policy limiting the extent of the insurer's liability. Coverage is often expanded or amended through endorsements attached to the policy.

Two types of title insurance policies are commonly issued: the owner's policy and the lender's policy. The owner's policy ensures that the title to the real property is vested as described in the policy, the title is marketable, and there is a right of access to the property and against defects in or lien or encumbrances on the title. Title insurance does not require a written application. Policies are often ordered by real estate agents or lenders. The title insurance agent issues a commitment or binder, basically revealing the current state of title to the property and agreeing to insure the property, provided that the requirements in the commitment are met to the satisfaction of the title insurer.

The effective date of the policy is typically the date that transactional documents—deed, deed of trust, etc.—are recorded in the public real estate records. Losses under the policy are subject to the limits listed on the title page, plus any costs of defense. The policy limit of an owner's policy is generally the purchase price of the real property, and the policy limit of a lender's policy is generally the original amount of the loan. Losses from title defects are rare, and loss ratios for insurers are relatively low. The goal of a title insurer is to find defects in title prior to issuing a policy; consequently, expense ratios are fairly high due to the cost of title research.

Most states place monoline restrictions on title insurers. Monoline restrictions prohibit title insurers from issuing any line of insurance other than title insurance. Rates and rate setting processes vary by state. Some states regulate only the risk premium, while other states regulate an all-inclusive premium, which generally includes all costs of issuing the policy, search expenses, and the risk premium.

Functions of title insurance agents include conducting title searches, performing underwriting functions, preparing and issuing title insurance commitments and policies, maintaining policy records, and receiving premiums. In addition, many title agents perform real estate closings and provide settlement and escrow services.

Many activities of state licensing divisions with regard to title insurance are the same as in other lines of insurance. In most states, agents are required to pass a licensing exam and fulfill ongoing continuing education (CE) requirements. In some states, the licensing division will also be responsible for receiving and filing agency appointments with insurers, bonds or letters of credit (LOCs), proof of errors and omissions (E&O) coverage, and forms disclosing controlled and affiliated business relationships. The NAIC has adopted the *Title Insurance Agent Model Act* (#230) to give guidance to state licensing directors.

Title insurance creates some unique regulatory issues, primarily due to the risk elimination nature of the insurance coverage and the business relationships between title insurance agents and those who refer title insurance business. The entity referring the title insurance business is often viewed as the customer rather than the insured due to the nature of real estate transactions. Entities that regularly refer title insurance business—mortgage brokers, lenders, realtors and attorneys—are referred to as producers of title insurance business. Note that “producer of title insurance,” as used in this context, carries a very different meaning from “insurance producer.”

Controlled and affiliated business relationships refer to business relationships between title insurance agents and producers of title insurance business. Many states require that controlled and affiliated business relationships be

disclosed to both the insured and the insurance department in writing. Many states also prohibit title insurance agents from providing rebates, referral fees, inducements or financial incentives to producers of title insurance business. In addition to state laws, rebates and referrals related to most residential real estate transactions are prohibited under the federal Real Estate Settlement Procedures Act (RESPA).

## Chapter 30

### Vatical and Life Settlement Providers and Brokers

The *Vatical Settlements Model Act* (#697) defines a viatical settlement as a transaction in which the owner of a life insurance policy sells the right to receive the death payment due under the policy to a third party. Typically, the owner/insured receives a cash payment, and the buyer agrees to make any remaining premium payments on the policy.

In 1993, the NAIC adopted the *Vatical Settlements Model Regulation* (#698) and Model #697 to provide a regulatory structure to protect consumers involved in viatical settlements. Model #697 was revised in 2003 and 2004 to address the issue of healthy consumers who might want to sell their insurance policy on the secondary market, better known as “life settlements.”

Licensing requirements vary as a result of the several versions of Model #697. Under the 1993 version of Model #697, a viatical settlement broker was required to have an underlying life producer license before being able to apply for and receive a viatical settlement broker license. This provision was not uniformly adopted.

The 2003 version of Model #697 provided for licensing procedures of individuals who were not licensed life insurance producers by requiring continuing education (CE) to maintain the license. The 2003 version was modified in 2004 to allow for licensed life insurance producers to notify or register with the state insurance regulator, as prescribed by the insurance commissioner if they were engaging in the business of settlements, and exempted life insurance producers from the viatical settlement brokers’ examination and the CE requirements.

The 2003 and 2004 versions of Model #697 also required the viatical settlement broker to maintain financial responsibility in the form of an errors and omissions (E&O) policy, surety bond, cash deposit, or a combination of any of the three. It also placed fiduciary responsibility requirements on the broker. The 2003 and 2004 versions of Model #697 required brokers to disclose the method by which compensation was calculated and the amount of compensation. It is essential that the viatical broker meet the licensing requirements of the state where the transaction occurs.

The 2003 version of Model #697 also provided for licensing procedures for viatical settlement providers.

Model #697 was revised in 2007 to address, among other things, transactions that have been called stranger-originated life insurance (STOLI) or investor-originated life insurance (IOLI). These transactions are related to a life insurance policy exhibiting any one of three characteristics prior to or within two years of policy issue:

1. Non-recourse premium financing.
2. Guarantee of settlement.
3. Settlement evaluation.

Settlement of such policies is prohibited for five years.

Other key revisions include:

1. New consumer disclosures related to viatical settlement compensation.
2. A new consumer disclosure requiring a statement that the viatical settlement broker exclusively represents the viator and owes a fiduciary duty to the viator, including a duty to act in the best interest of the viator.
3. Allowing life agents to sell without a viatical license, but special conditions apply.

Additional revisions include:

Under specified circumstances, a life insurance producer may operate as a viatical settlement broker. The life insurance producer is deemed to meet the viatical settlement broker licensing requirements. The revisions also permit a person licensed as an attorney, certified public accountant (CPA), or financial planner accredited

by a national recognized accrediting agency, who is retained to represent the viator and whose compensation is not paid directly or indirectly by the viatical settlement provider, to negotiate viatical settlement contracts on behalf of a viator without having to obtain a viatical settlement broker's license.

To receive and maintain a license, the 2007 revisions require a viatical settlement provider or broker to demonstrate evidence of financial responsibility through a surety bond, a deposit of cash, certificates of deposit, securities, or any combination thereof in the amount of \$250,000. The surety bond must be issued in the favor of the state and must specifically authorize recovery by the insurance commissioner on behalf of any person in the state who sustained damages as the result of erroneous acts, failure to act, conviction of fraud, or conviction of unfair practices by the provider or broker. The insurance commissioner may ask for evidence of financial responsibility at any time the insurance commissioner deems necessary. The revisions make it clear that a provider or broker that is licensed in more than one state is not required to file multiple bonds in each state. Some problems have arisen with implementing the bonding requirements of Model #697. Regulated entities argue that it is impossible to obtain a bond as described in Model #697.

The revisions also require an individual licensed as a viatical settlement broker to complete, on a biennial basis, 15 hours of training related to viatical settlements and viatical settlement transactions. A life insurance producer who is operating as a viatical settlement broker is not subject to this requirement.



National Association of Insurance Commissioners

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