

**STATE OF LOUISIANA
OFFICE OF FINANCIAL INSTITUTIONS
BATON ROUGE, LOUISIANA**

May 16, 2002

**POLICY NO. DI-02-02
(B,SB,SL,HC)**

SALES OF INSURANCE PRODUCTS

PURPOSE: To provide guidance to examiners regarding a financial institution or parent company's offering insurance products

TO WHOM THIS POLICY APPLIES: All state-chartered banks and thrifts, their subsidiaries, parent companies, or subsidiaries of their parent companies

GENERAL

The four federal banking agencies have jointly issued a rule on Consumer Protections for Depository Institution Sales of Insurance (Attachment 1). This rule duplicates many of the regulatory issues that are addressed in Louisiana statutes concerning insurance sales by financial institutions (LSA-R.S. 22:3051 through 3065, Attachment 2). However, there are a few subtle differences in the two bodies of law. A list of these differences follows:

- (1) Federal statutes apply to state and federally chartered banks and thrifts. State statutes pertaining to insurance sales by financial institutions only apply to state and federally chartered banks—thrifts are not included. The general insurance statutes (Title 22 of the Louisiana Civil Code) that set out requirements for the sale of insurance apply to all entities selling insurance, including state and federally chartered thrifts. The specific state statutes pertaining to insurance sales by financial institutions encompass best practices that all depository institutions should follow. Therefore, during an examination, examiners will review banks, thrifts, their subsidiaries, parent companies, or subsidiaries of their parent companies for compliance with both state and federal regulations. Any violations found during a thrift examination, however, will be considered contraventions of this policy rather than a violation of law.
- (2) Louisiana statutes specifically **exclude** credit insurance, insurance placed by the financial institution when the debtor breaches the contractual obligation to provide that insurance, private mortgage insurance, and annuities from the statute pertaining to financial institution sales¹. Therefore, the **state** requirements, such as disclosures and separation of activities, do not apply to the sale of these types of insurance products. A financial institution or its wholly-owned insurance agency must still be licensed to sell

¹ LSA-R.S. 22:3053(A)(2)

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these types of insurance products, but it is not subject to the state statutes pertaining to financial institution sales².

Federal law does not exclude any specific types of insurance products and specifically includes annuities. Therefore, the required federal disclosures and separation of activities apply to all aspects of insurance and annuities sales.

- (3) The disclosures given to a customer that are required by state and federal laws are slightly different. The state requirements are contained in LSA-R.S. 22:3059. The federal requirements are contained in Section 343.40 of the FDIC's Rules and Regulations for nonmember banks and savings banks, Section 208.84 of Regulation H for member banks, and Section 536.40 of the OTS' Rules and Regulations for savings and loan associations.

State and federal laws both require disclosures (1) that the product is not insured by the Federal Deposit Insurance Corporation (FDIC) or other federal agency, (2) that it is not a deposit or other obligation of the financial institution, and (3) that the customer is not required to purchase the insurance through the financial institution and the customer's choice of another insurance provider will not affect the financial institution's credit decision or credit terms in any way. However, each agency has an additional disclosure requirement. State law also requires a disclosure that the financial institution does not guarantee performance by the insurer issuing the policy. Federal law also requires a disclosure in the case of an insurance product or annuity that involves an investment risk to specifically note that there is investment risk associated with the product, including the possible loss of value.

As noted in item #1 above, the additional State disclosure need not be disclosed in a sale of the exempted types of insurance products or annuities; however, all of the federal disclosures must be disclosed for every sale of an insurance or annuity product.

Also, in the additional federal disclosure noted above regarding insurance products that involve an investment risk, the FDIC includes whole life policies in this type of product. Therefore, this additional disclosure is required in the sale of all whole life policies as well as annuities.

- (4) There is also a subtle difference between the required timing of the above disclosures for the sale of insurance. State law³ requires that the solicitation of a customer for the purchase or sale of insurance shall not be conducted by any person directly responsible for making the loan before such time as the final decision regarding the acceptance or denial of that specific loan is made and communicated in writing to the customer. State law⁴ also requires that the written disclosures listed in Item #2 above are signed by the customer at the time a written application for insurance is made. The financial institution must give the customer these disclosures when it first informs the customer

² LSA-R.S. 22:3051-3065

³ LSA-R.S. 22:3056

⁴ LSA-R.S. 22:3059(A)

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that required insurance is available from the financial institution if (1) insurance is required in order to obtain a loan, (2) loan approval is contingent on the customer's obtaining acceptable insurance, or (3) the customer obtained insurance required in connection with the loan from another insurance provider and the financial institution is soliciting the sale of insurance to replace the customer's existing coverage.

Federal law⁵ requires that disclosures made in connection with the initial purchase of an insurance product or annuity are made orally **and** in writing before the completion of the initial sale of an insurance product or annuity. Federal law⁶ also requires disclosures made in connection with the application for credit when an insurance product or annuity is solicited, offered, or sold. Disclosures must be made orally **and** in writing at the time an application is made. Oral disclosures are not required if the sale is conducted by mail⁷. The written disclosure may be mailed within three business days if a sale is conducted by telephone⁸. In all cases, the institution must acquire a written acknowledgment by the consumer that the consumer received the disclosures.⁹

- (5) In advertisements, the disclosures required by state and federal law are also slightly different. The state requirements are contained in LSA-R.S. 22:3059(C). The federal requirements are contained in Section 343.40(d) of the FDIC's Rules and Regulations for nonmember banks and savings banks, Section 208.84(d) of Regulation H for member banks, and Section 536.40(d) of the OTS' Rules and Regulations for savings and loan associations. State and federal law both require disclosures (1) that the insurance product is not insured by the FDIC or other federal agency and (2) that the insurance product is not a deposit or other obligation of, or guaranteed by, the financial institution. However, state law also requires a disclosure regarding (1) whether the insurance agent is employed by the financial institution or by a third party and (2) that an insurance company, and not the financial institution, is underwriting the insurance product.

Federal law also requires a disclosure in the case of an insurance product or annuity that involves investment risk, that there is an investment risk, including the potential that principal may be lost and that the product may decline in value. Neither requires such

⁵ Section 343.40(a) of the FDIC's Rules and Regulations for nonmember banks and savings banks, Section 208.84(a) of Regulation H for member banks, and Section 536.40(a) of OTS' Rules and Regulations for savings and loan associations.

⁶ Section 343.40(b) of the FDIC's Rules and Regulations for nonmember banks and savings banks, Section 208.84(b) of Regulation H for member banks, and Section 536.40(b) of OTS' Rules and Regulations for savings and loan associations.

⁷ Section 343.40(c)(2) of the FDIC's Rules and Regulations for nonmember banks and savings banks, Section 208.84(c)(2) of Regulation H for member banks, and Section 536.40(d)(2) of OTS' Rules and Regulations for savings and loan associations.

⁸ Section 343.40(c)(3) of the FDIC's Rules and Regulations for nonmember banks and savings banks, Section 208.84(c)(3) of Regulation H for member banks, and Section 536.40(c)(3) of OTS' Rules and Regulations for savings and loan associations.

⁹ Section 343.40(c)(7) of the FDIC's Rules and Regulations for nonmember banks and savings banks, Section 208.84(c)(7) of Regulation H for member banks, and Section 536.40(c)(7) of OTS' Rules and Regulations for savings and loan associations.

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disclosures if the advertisements or promotional materials are of a general nature describing or listing the services or products offered by the institution.

Again, regarding the additional federal disclosure noted above involving insurance products that involve an investment risk, the FDIC includes whole life policies in this product. Therefore, this additional disclosure is required in the advertisement of all whole life policies as well as annuities.

- (6) Regarding the physically distinct areas for insurance sales, lending, and deposit-taking functions, state law requires that the area involving insurance sales be separate from the lending area. Federal law requires separation between insurance sales and the area where retail deposits are routinely accepted from the general public. Both bodies of law allow separation to the extent possible in the event that physical separation is not practical. Again, while federal law does not exempt any form of insurance products, state law specifically excludes credit insurance, insurance placed by the financial institution when the debtor breaches the contractual obligation to provide that insurance, private mortgage insurance, and annuities. Therefore, these forms of insurance do not have to be separated from the loan area.

EXAMINATION PROCEDURES:

During examinations of financial institutions or their parent companies, examiners will conduct a review of insurance sales activities to determine compliance with both state and federal regulations. At the start of an examination, preferably as a part of the pre-examination packet, every financial institution or parent company that is involved in the sale of insurance products will be asked to complete a questionnaire (Attachment 3). Examiners will review the responses to the questionnaire to determine the institution's level of involvement and preparedness in these areas. During the examination, examiners will verify the responses to the questionnaire by inquiring about or observing the actual practices of the institution. Compliance with the examination considerations detailed below and federal and state regulations will be verified.

Any deficiencies noted with respect to the practices of the insurance area, including those that may have contributed to an apparent violation of the Louisiana Insurance Code (LIC), will be noted in the report under Item #7 of the Risk Management Assessment page. Deficiencies with respect to the examination considerations noted below will be cited in the report of examination as apparent contraventions of this OFI policy statement. Apparent violations of federal law will also be cited. The EIC will prepare a separate memo summarizing any apparent violations of the LIC. This memo will be sent, along with the examination report, to the attention of the Review Examiner and will include a complete description of the actions that caused the apparent violation, any corrective action taken, and management's response to the violation. The Review Examiner will review all deficiencies regarding the insurance code or complaints, and forward material violations or deficiencies to the Review Examiner specializing in insurance activities. The Review Examiner specializing in insurance activities will forward the material deficiencies, especially if left uncorrected, to the Louisiana Department of Insurance (LDI) via an official memo from this

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office. The Review Examiner specializing in insurance activities will maintain contact with the LDI until the deficiency is resolved.

The examiners will also review the institution's file on complaints to ascertain appropriate disposition. The Examiner-in-Charge (EIC) will prepare a separate memo to the appropriate Review Examiner regarding any uncorrected or repeated complaints of a serious nature.

EXAMINATION CONSIDERATIONS:

As with any activity conducted by a financial institution, the board should adopt a policy delineating its plans and procedures for offering insurance products. Examiners will review the policy to determine the level of guidance that management has provided in this area. At a minimum, the policy should give proper guidance in the following areas:

- (1) A list of the types of insurance to be offered
- (2) A list of the insurance companies with which the bank/thrift will do business
- (3) The roles of employees, dual employees, and third party vendors in the sales activity
- (4) Accommodations for a distinctive setting for the sales activity
- (5) Procedures to ensure that proper disclosures are given to all customers in accordance with both state and federal laws and regulations

Additionally, examiners will review the following:

- (1) Financial Capacity – Periodically, management should review the financial capacity of all insurance companies with which the institution does business. Information, such as the AM Best rating, financial statements, and examination reports for most insurance companies may be obtained from the LDI. This information for out-of-state insurance companies may also be obtained from the website of the other states' insurance departments.
- (2) Fidelity Coverage -- Prior to engaging in any insurance sales program, management should review the applicability and adequacy of the fidelity coverage with respect to such activities and notify the blanket bond carrier of plans to engage in these activities and the specifics of their arrangements. Subsequent reviews should be conducted annually and documented in writing. Written assurance should be obtained from the carrier that the institution's insurance coverage for employees includes staff representing third-party vendors.
- (3) Licensure and Distribution of Income – LSA-R.S. 22:3055 and Section 343.60 of the FDIC's Rules and Regulations (for non-member banks and savings banks), Section 208.86 of Regulation H (for member banks), or Section 536.60 of the OTS' Rules and Regulations (for savings and loan associations) require proper licensure to sell or offer to sell insurance products. The entities that must be properly licensed before commissions may be shared include financial institutions, their subsidiaries, parent companies, or their subsidiaries. However, in accordance with LSA-R.S. 22:1117(A)(2), if all sales (including the sale of credit-related insurance products) are

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made through an insurance agency owned by the financial institution (either directly by the institution or through a subsidiary), the financial institution does not have to be licensed because this prohibition does not apply to the distribution of profits to the owners of an insurance agency.

Different types of licenses are offered by the LDI depending on the types of insurance products being solicited. While the institution may offer many different types of insurance products, an employee who only offers a certain product need only be licensed to sell that product. However, management should ensure that employees licensed to sell a particular product do not cross over and sell another type of product for which they are not licensed.

- (4) Commissions/Referrals – LSA-R.S. 22:1117(A) provides that no commission or brokerage may be paid to an unlicensed person. Unlicensed employees of a **financial institution may not** receive commissions, brokerage, or other consideration for services as an insurance agent. However, unlicensed employees of the institution may provide clerical assistance, including the collection of insurance premiums, when authorized by a licensed agent.

LSA-R.S. 22:3057 and Section 343.50(b) of the FDIC's Rules and Regulations (for non-member banks and savings banks), Section 208.85(b) of Regulation H (for member banks), or Section 536.50(b) of the OTS' Rules and Regulations (for savings and loan associations) allow an exception for financial institutions where unlicensed employees receive a flat rate fee for each referral made as long as the fee is not dependant on the successful completion of an insurance sales transaction.

- (5) Setting and Circumstances -- If insurance products are sold by any entity other than directly by the financial institution or a subsidiary of the institution, the financial institution should receive compensation or some consideration for its personnel, premises, equipment, and goodwill in connection with the insurance sales activities. Compensation and consideration may include a percentage of the commissions (as long as the financial institution is also licensed), "use" of the employee's expertise in the insurance area, or bringing on an established agent with his/her business accounts. The Board must review the justification for this compensation/consideration periodically.

In accordance with LSA-R.S. 22:3060 and Section 343.50(a) of the FDIC's Rules and Regulations (for non-member banks and savings banks), Section 208.85(a) of Regulation H (for member banks), or Section 536.50(a) of the OTS' Rules and Regulations (for savings and loan associations), a financial institution should minimize the potential for customer confusion by taking reasonable measures to physically separate the transactions involving insurance or annuities from the areas designated for loan transactions or deposit taking.

- (6) Disclosures and Advertising -- In accordance with Section 343.40(c) of the FDIC's Rules and Regulations (for non-member banks and savings banks), Section 208.84(c) of Regulation H (for member banks), or Section 536.40(c) of the OTS' Rules and

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Regulations (for savings and loan associations), if insurance products are offered for sale on the institution's website, the same written disclosures must be conspicuously placed and presented in a clear and concise manner, without the customers' being able to bypass the disclosures. Also, in accordance with these regulations, if a sale is conducted over the telephone, an oral acknowledgement of receipt of the disclosures must be documented and maintained, with reasonable efforts made to obtain a written acknowledgement from the consumer.

- (7) Complaints – All complaints regarding the sale of insurance products should be maintained in a separate file with a copy of all responses attached to the complaint.
- (8) Supervision—OFI will work with the LDI to ensure that financial institutions conduct the sale of insurance products in a safe and sound manner. Therefore, it is essential that proper disclosures are given to avoid customer confusion, sales personnel are properly licensed, and responsible sales practices are strictly enforced.

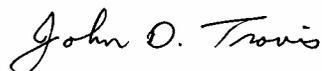
LDI will be notified of any material apparent violation of Title 22 involving financial institution sales. OFI will also enforce compliance with the provisions of the federal rule by using any regulatory, investigative, examination, or enforcement authority given the OFI by the provisions of the Louisiana Banking Law, including LSA-R.S. 6:121 et seq.

Nothing contained in this policy will limit the authority or responsibility of the LDI to regulate insurance in conformity with all applicable laws and regulations.

INSURANCE SALES IN TOWNS OF LESS THAN 5,000:

A bank or thrift may decide to organize the insurance activities through a subsidiary of the holding company. In this event, the holding company does not have to be a financial holding company.

Upon the enactment of LSA-R.S. 6:242(A)(6)(a), a state-chartered or national bank located in Louisiana is no longer restricted to selling insurance in towns with a population less than 5,000. However, insurance sold through a subsidiary of the bank holding company or thrift holding company is still restricted to towns with a population of less than 5,000 (Regulation Y (CFR 225.28)). These insurance agencies must be located in a town of less than 5,000 **and** all insurance sales must be made from locations in towns of less than 5,000.



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Attachments include the following:

- (1) Final Rule on Consumer Protections for Bank Sales of Insurance (FIL-84-2000 dated December 5, 2000)
 - Part 343 of the FDIC's Rules and Regulations for non-member banks and savings banks
 - Federal Reserve Regulation H for member banks
 - Part 536 of the OTS' Rules and Regulations for savings and loan associations
- (2) Change in Effective Date of Insurance Consumer Protection Rules (FIL-23-2000 dated March 19, 2001)
- (3) Interagency Responses to ABIA and ABA Questions on the Insurance Sales Practices Regulation (FIL-84-2001 dated September 27, 2001)
- (4) LSA-R.S. 22:3051 through 3065 (Louisiana insurance statutes)
- (5) Sales of Insurance Products Questionnaire