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The Highly Troubled Ethical Environment of the Life Insurance Industry: Has it Changed Significantly from the Last Decade and if so, why?

Robert W. Cooper
Garry L. Frank

ABSTRACT. This paper presents the findings of two surveys conducted in April 2003 of Chartered Life Underwriters (CLUs) and Chartered Financial Consultants (ChFCs) who are members of the Society of Financial Service Professionals. The first survey of 3000 CLUs and ChFCs – the life insurance industry's most highly regarded professionals – was aimed at identifying the key ethical issues faced by professionals working in the life insurance industry today. A comparison of these findings with those of earlier studies conducted in 1990 and 1995 suggests that while the key ethical issues facing those working in the life insurance business today are essentially the same as those encountered during industry's highly troubled ethical environment of the early 1990s, these issues are perceived as presenting somewhat less serious problems than in the past. The second survey of 3000 CLUs and ChFCs was aimed at determining the extent to which these professionals perceive the industry created Insurance Marketplace Standards Association (IMSA) as having contributed to any change in the ethical environment that has taken place. The findings suggest that IMSA has played an important role in influencing senior managers to more strongly encourage and support ethical market conduct, a critical step in improving the industry's ethical environment.

KEY WORDS: Ethical market conduct, ethics issues, life insurance, professional ethics

Robert W. Cooper, Ph.D., is Employers Mutual Distinguished Professor of Insurance at Drake University. Previously, he was dean of the Huebner School at the American College where he was responsible for the CLU and ChFC professional designation programs. Bob has published widely in the fields of insurance and business ethics.

Garry L. Frank, Ph.D., is Professor of Public Administration at Drake University where he teaches a graduate course in business ethics. He has conducted extensive research regarding the ethics environment in several professions and fields of business, including accounting, nursing, insurance, actuarial science, and purchasing and supply management. His research findings have been published in a number of academic and professional journals in these fields.

Introduction

A study of the ethical environment of the life insurance industry conducted in September 1990 (Cooper and Frank, 1991) identified a number of key ethical issues that were very likely to bring about serious problems for a business based fundamentally on public trust. As shown in Table I, these key issues – some of concern to businesses and their employees in general, and others of special relevance to professionals – included among others, false or misleading representation of products or services in marketing, advertising or sales efforts; failure to identify the client's needs and recommend products and services that meet those needs; lack of knowledge or skills to competently perform one's duties; and conflicts between opportunities for personal financial gain and proper performance of one's responsibilities. Despite the wave of market conduct suits that followed resulting in huge settlements by and/or fines against several large life insurers, a similar survey of insurance professionals conducted in May 1995 (Cooper et al. 1996) indicated little significant change in the industry's troubled ethical environment. The very high positive correlation coefficient for the 32 issue means in the two studies,

TABLE I

Ethics issues

		CLU/ChFC 1990 Study (n = 437; 37%)[§]		MDRT 1995 Study (n = 339; 23%)		CLU/ChFC 2003 Study (n = 450; 15%)	
		Mean	Rank	Mean	Rank	Mean	Rank
Issue 1	Failure to provide products and services of the highest quality in the eyes of the customer	2.618	9	2.83*	9	2.47††	11
Issue 2	Failure to provide prompt, honest responses to customer inquiries and requests	2.903	8	2.92	8	2.78	6
Issue 3	Making disparaging remarks about competitors, their products, or their employees or agents	3.087	6	3.31*	4	2.71†,††	7
Issue 4	Misuse of proprietary information	2.157	12	2.41*	12	2.15††	14
Issue 5	Misuse of sensitive information belonging to others	2.035	18	2.24*	14	2.04††	16
Issue 6	Improper methods of gathering competitors' information	2.127	14	2.29	13	2.02††	18
Issue 7	False or misleading representation of products or services in marketing, advertising or sales efforts	3.530	1	3.54	1	3.00†,††	4
Issue 8	Conflicts between opportunities for personal financial gain (or other personal benefits) and proper performance of one's responsibilities	3.274	4	3.32	3	3.11††	2
Issue 9	Conflicts of interest involving business or financial relationships with customers, suppliers or competitors that influence, or appear to influence, one's ability to carry out his or her responsibilities	2.597	10	2.56	10	2.58	9
Issue 10	Conflicts of interest involving the marketing of products and services competing with those of one's own company	2.571	11	2.55	11	2.49	10
Issue 11	Conflicts of interest that involve working for a competitor, customer or supplier without approval	2.088	16	2.02	16	1.98	19
Issue 12	Misuse of company assets/property	1.715	28	1.67	24	1.70	30
Issue 13	Insider trading/other security trading problems	2.009**	19	1.67	24	2.13**	15
Issue 14	Giving excessive gifts or entertainment	1.711	29	1.57	30	1.76**	23
Issue 15	Receiving excessive gifts or entertainment	1.520	31	1.44	31	1.64**	31
Issue 16	Offering or soliciting payments or contributions for the purpose of influencing customers or suppliers	1.703	30	1.70	22	1.74	27
Issue 17	Offering or soliciting payments or contributions for the purpose of influencing government officials	1.759	24	1.67	24	1.77	22
Issue 18	Offering or soliciting payments or contributions for the purpose of obtaining, giving or keeping business	1.916	21	1.88	18	1.87	21

TABLE I

(Continued)

		CLU/ChFC 1990 Study (n = 437; 37%)[§]		MDRT 1995 Study (n = 339; 23%)		CLU/ChFC 2003 Study (n = 450; 15%)	
		Mean	Rank	Mean	Rank	Mean	Rank
Issue 19	Offering or soliciting payments or contributions for the purpose of persuading employees of another company to fail to perform, or improperly perform, their duties	1.426	32	1.37	32	1.39	32
Issue 20	Offering or soliciting payments or contributions for the purpose of influencing legislation or regulations	1.909	22	1.74	20	1.96**	20
Issue 21	Inaccuracy of books, records or reports	2.093	15	1.99	17	2.32*,**	13
Issue 22	Abuse of expense accounts	1.984**	20	1.69	23	2.03**	17
Issue 23	Antitrust issues	1.902**	23	1.66	27	1.76	23
Issue 24	Relations with local communities	1.755	25	1.86	19	1.73	28
Issue 25	Office/agency closings and layoffs	2.154	13	2.16	15	2.33	12
Issue 26	Discrimination	1.749	26	1.63	29	1.76	23
Issue 27	Drug and alcohol abuse	2.070**	17	1.74	20	1.72†	29
Issue 28	Employee theft	1.715	27	1.64	28	1.75	26
Issue 29	Lack of knowledge or skills to competently perform one's duties	3.296	3	3.21	5	3.08†	3
Issue 30	Failure to identify the customer's needs and recommend products and services that meet those needs	3.423	2	3.42	2	3.16†,††	1
Issue 31	Failure to be objective with others in one's business dealings	2.947	7	2.94	7	2.71†,††	7
Issue 32	Misrepresenting or concealing limitations in one's abilities to provide services	3.116	5	2.99	6	2.95	5

*Significantly greater than the CLU/ChFC 1990 study value at the 0.05 level.
**Significantly greater than the MDRT 1995 study value at the 0.05 level.
†Significantly less than the CLU/ChFC 1990 study value at the 0.05 level.
††Significantly less than the MDRT 1995 study value at the 0.05 level.
§Number of survey respondents and approximate survey response rate.

0.9763, indicated that the order of the issues was very similar overall despite the passage of 5 years between the studies. As shown in Table I, not only were the same 2 issues (Issues 7 and 30) ranked first and second, respectively, in both studies, but also the same 10 issues (Issues 1–3, 7–9, and 29–32) were perceived by the respondents to both surveys as presenting the greatest ethical problems to those working in the life insurance business. Only two statistically significant differences (at the 0.05 level) were found between the means for these 10 key ethical issues in the 2 studies – Issue 1 (failure to provide products and services of the highest quality in the eyes of the customer) and Issue 3 (making disparaging remarks about competitors, their products, or their employees or agents) were perceived as presenting significantly greater problems in 1995 than in 1990.

Concerned with the industry's shabby image, possible regulatory repercussions and potential company and officer liability, in 1994 a major trade association proposed the establishment of the Insurance Marketplace Standards Association (IMSA) to implement an Ethical Market Conduct Program

aimed at helping life insurance companies maintain high ethical standards in the marketplace (Cooper, 1998). With 2003 not only being a little more than a decade after the 1990 ethical issues study of the life insurance industry was conducted but also five years after the first companies were permitted to use their IMSA certifications publicly, two surveys of 3000 Charted Life Underwriters (CLUs) and Charted Financial Consultants (ChFCs) each were conducted in 2003 to update the perceptions of life insurance professionals regarding both the key ethical issues encountered in the industry today and the impact of IMSA on the ethical environment of the life insurance sector of the financial services industry. The findings of these studies conducted with the cooperation of the Society of Financial Service Professionals help to answer a number of questions regarding the troubled ethical environment of the life insurance industry to include:

- Do insurance professionals perceive the industry's ethical environment as having changed significantly from the past?
- If so, what role is IMSA, a rather unique creation of the industry itself, perceived as having played in that change?

The changing ethical environment of the life insurance industry

The 2003 ethical issues survey of 3000 CLUs and ChFCs who were members of the Society of Financial Service Professionals was identical to the surveys of 1173 CLUs and ChFCs and 1500 Million Dollar Roundtable (MDRT) members (nearly all of whom were CLUs and/or ChFCs) conducted in 1990 and 1995, respectively. As in the 2 earlier surveys, the participants in the 2003 CLU/ChFC study were presented with the 32 ethics-related statements (referred to as ethical issues for simplicity) listed in Table I and were asked to rate each issue on a 5-point scale where 5 meant that it was a major problem in the life insurance industry at the time the survey was conducted and 1 meant that it was not a problem. As shown in Table I, the response rate for the 2003 survey, 15%, was considerably less than those for the two earlier surveys. While this is too low to permit generalizations to be made regarding the views of all Society members, the findings are grounded in a sufficient number of responses to provide a sense of the ethical environment currently encountered in the life insurance industry.

Table I shows the 32 issue mean ratings for each of the 3 surveys based on the individual ratings given to each issue by all the respondents to the particular survey. The table also shows the rank of each issue based on the size of the issue's mean rating.

As indicated in Table I, four issues received mean ratings greater than 3.0 (the midpoint on the rating scale) in the 2003 CLU/ChFC survey. These four issues also were rated 4 or 5 by 35% or more of the respondents. In descending order, the four top-ranked issues are:

- Issue 30 – failure to identify the customer's needs and recommend products and services that meet those needs.
- Issue 8 – conflicts between opportunities for personal financial gain (or other personal benefits) and proper performance of one's responsibilities.
- Issue 29 – lack of knowledge or skills to competently perform one's duties.
- Issue 7 – false or misleading representation of products or services in marketing, advertising or sales efforts.

Two of these top rated issues – Issues 7 and 8 – are related to the ethical responsibilities of businesses and their employees in general. The other two – Issues 29 and 30 – are ethical issues of special relevance to professionals. Thus, the CLUs and ChFCs responding to the survey viewed situations involving both business and professional responsibilities as presenting key ethical challenges to those working in the life insurance industry today.

Table I provides for a comparison of the mean ratings and ranks for the 32 issues in the 1990 survey of CLUs and ChFCs and the 1995 survey of MDRT members as well as the 2003 survey of CLUs and ChFCs. Examination of the issue ranks for the three surveys indicates some shifting in the order of the issue means. There is, however, considerable similarity in the list of the most problematic ethical issues identified in 1990, 1995 and 2003. For example, the 4 top-ranked issues in the 2003 survey are the same issues as those that ranked in the top 4 in the 1990

survey and are among the top-5 ranked issues in the 1995 survey. Also, the same issues ranked in the top 8 in all three surveys. These 8 top-ranked issues include the following four issues of interest to businesses and their employees in general:

- failure to provide prompt, honest responses to customer inquiries and requests.
- Issue 3 – making disparaging remarks about competitors, their products, or their employees or agents.
- false or misleading representation of products or services in marketing, advertising or sales efforts.
- Issue 8 – conflicts between opportunities for personal financial gain (or other personal benefits) and proper performance of one's responsibilities.

The other four issues ranked among the top 8 in all 3 studies were the following issues of special relevance to professionals:

- Issue 29 – lack of knowledge or skills to competently perform one's duties.
- Issue 30 – failure to identify the customer's needs and recommend products and services that meet those needs.
- Issue 31 – failure to be objective with others in one's business dealings.
- Issue 32 – misrepresenting or concealing limitations in one's abilities to provide services.

In Figure 1, the means for the four issues ranked in the top 8 that are of interest to businesses and their employees in general are plotted for each of the 3 studies. Solid lines indicate statistically significant differences (at the 0.05 level) between the connected means and dashed lines indicate where no statistically significant differences were found. Figure 2 depicts the same information for the four issues of special relevance to professionals.

Figures 1 and 2 suggest that from a statistical standpoint, there has been significant improvement in most of the eight ethical issues perceived as presenting the greatest market conduct problems for the life insurance industry during the first half of the last decade. As shown in Figure 1, the 2003 CLU/ChFC study means for 3 of the four issues of interest to businesses and their employees in general (Issues 3, 7 and 8) were significantly less than the means for the 1990 CLU/ChFC study and/or the 1995 MDRT study. Similarly, Figure 2 indicates that the 2003 CLU/ChFC study means for 3 of the four issues of special relevance to professionals (Issues 29–31) were significantly less than the means for the 1990 CLU/ChFC study and/or the 1995 MDRT study. Also, while not statistically significant, Figure 1 shows that the 2003 CLU/ChFC study mean for Issue 2 is lower than in either of the earlier two studies, and Figure 2 shows the same situation for Issue 32.

These findings suggest that although the same 8 ethical issues are still seen as being the most problematic for the life insurance industry today, they are perceived as presenting somewhat less of a problem today than in the troubled 1990s. What role is IMSA perceived as having played in bringing about this improvement in the industry's ethical environment?

The perceived role of IMSA

As mentioned earlier, with efforts by individual insurance companies, professional associations and insurance regulators failing to improve the life insurance industry's troubled ethical environment by the mid-1990s, the industry created IMSA in 1996 to implement the Ethical Market Conduct Program, a voluntary program aimed at helping insurers improve the ethical environments of their own companies and thus, that of the industry in general. As illustrated in Figure 3, Cooper and Frank (1999, p. 50) describe the Ethical Market Conduct Program as follows:

> ...an insurance company choosing to participate is expected to adopt the Principles and Code of Ethical Market Conduct and then go through a two-step assessment process, involving a self-assessment followed by an independent assessment conducted by an IMSA-approved assessor. Upon satisfactory completion of the assessment process and the IMSA application process, the company is conferred membership in IMSA for a period of three years. Once membership expires, the company must repeat the certification process to renew its membership.

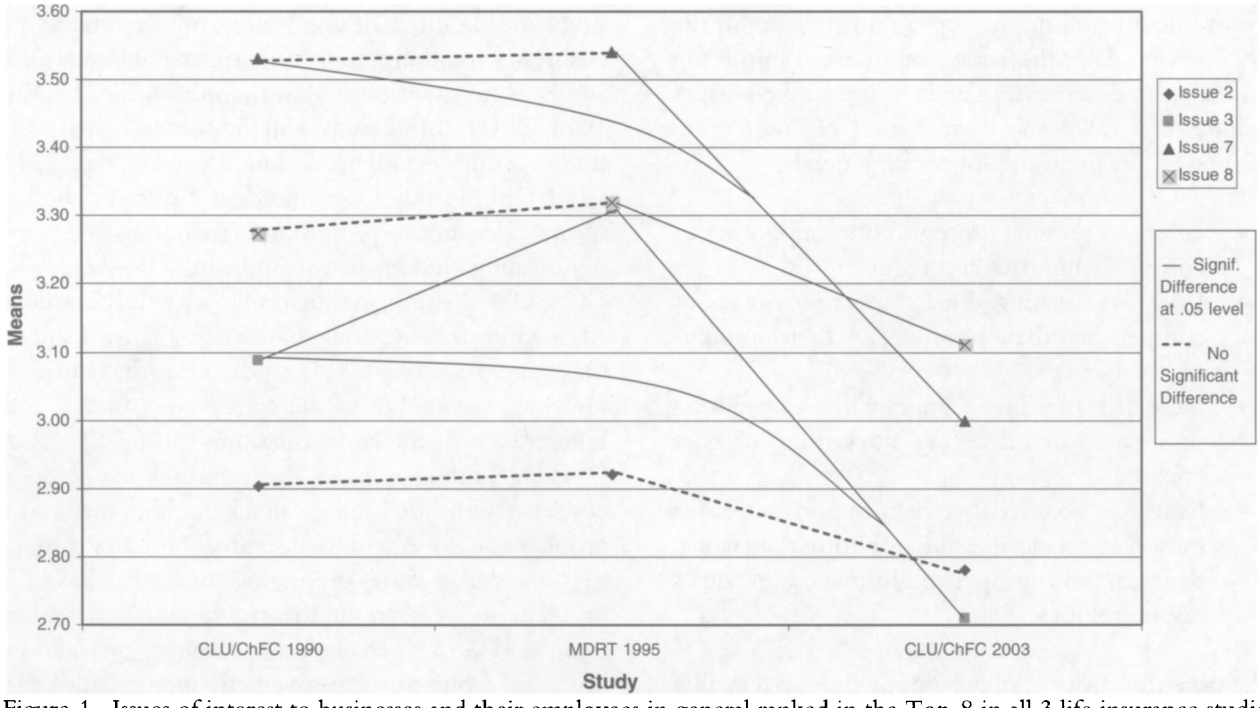

Figure 1. Issues of interest to businesses and their employees in general ranked in the Top-8 in all 3 life insurance studies (Issue 2, 3, 7 and 8 means).

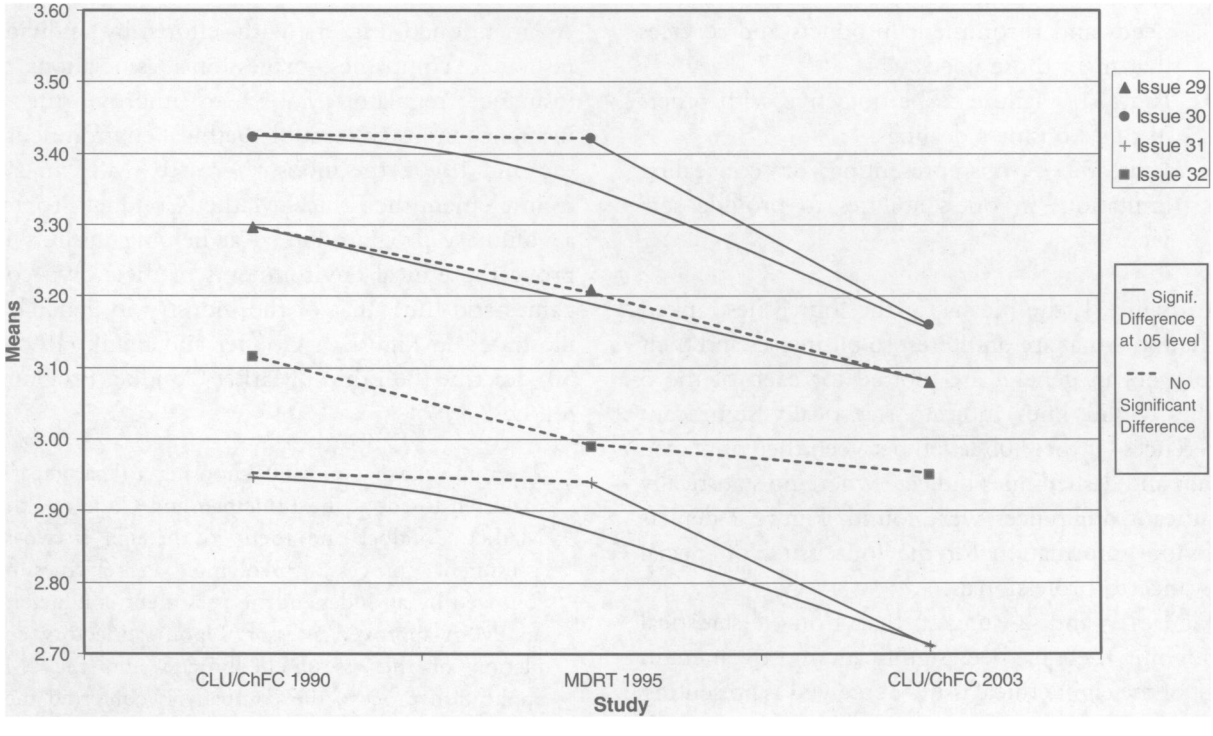

Figure 2. Issues of special relevance to professionals ranked in the Top-8 in all 3 life insurance studies (Issue 29, 30, 31 and 32 means).

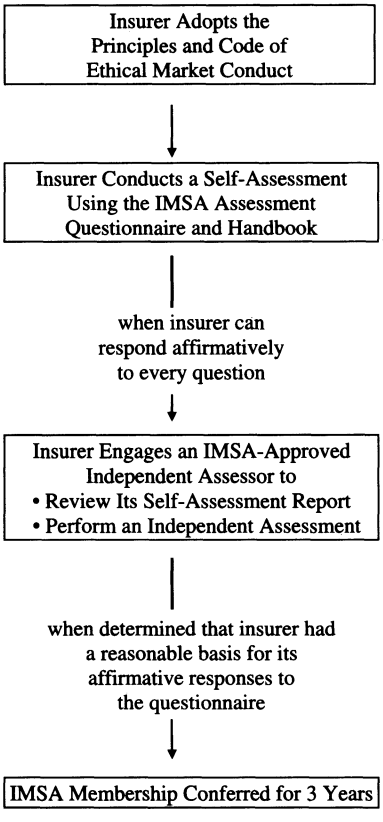

Figure 3. Qualifying for IMSA membership (from Cooper and Frank, 1999).

Shortly after the first 155 life insurance companies had completed the Ethical Market Conduct Program's assessment requirements and were permitted to announce their IMSA membership to the public on April 1, 1998, 2000 CLUs and ChFCs were surveyed (Cooper and Frank, 1999) to gather information on how these life insurance professionals perceived IMSA's program *would* impact various factors related to improvement in the industry's ethical environment. The same type study was replicated five years later in April 2003 when 3000 CLUs and ChFCs selected at random from among the regular members of the Society of Financial Service Professionals were surveyed to gather information on how they perceived IMSA's Ethical Market Conduct Program *had* impacted the same factors related to improvement in the industry's ethical environment. In each survey, the participants were presented with the 9 possible outcomes listed in Table II and asked to indicate the extent to which they perceived IMSA's program would contribute/had contributed to the outcomes by rating each of them on a 5-point scale where 5 means "very significantly" and 1 means "not at all." Responses to the 1998 and 2003 surveys were 539 (27%) and 410 (14%), respectively. While these response rates are too low to permit generalizations to be made regarding the views of all Society members, the findings are grounded in a sufficient number of responses to provide a sense of how life insurance professionals view IMSA's role in improving the industry's ethical environment.

Table II shows the 9 outcome mean ratings for 1998 and 2003 surveys based on the individual ratings given to each outcome by all the respondents to the particular survey. The table also shows the rank of each outcome based on the size of the outcome's mean rating. Referring to the table, a few key points emerge. First, comparison of the means for each possible outcome indicates that the 1998 survey mean was significantly greater than the 2003 study mean for each of the 9 outcomes. This suggests that at its inception, IMSA's Ethical Market Conduct Program was anticipated to have a greater impact on each of the possible outcomes than it is perceived to have had after five years in operation. This undoubtedly reflects the finding reported earlier that while there appears to have been some improvement in the industry's ethical environment since the mid-1990s, the issues presenting the greatest ethical problems for those working in the industry today are the same as those that were the key issues in 1990 and 1995. Also, the voluntary nature of the Ethical Market Conduct Program has limited IMSA's impact on the industry's ethical environment. Only about 20% of the more than 1000 companies in the life insurance industry have joined IMSA and while those member companies write about 65% of the life insurance policies each year, 80% of the companies writing 35% of the life insurance business in the U.S. still provides a sizable source for the various key market conduct problems identified in the 2003 issues survey.

Second, review of the ranks of the 9 possible outcomes for both studies in Table II indicates that the respondents to both surveys perceive IMSA's Ethical Market Conduct Program as having its greatest impact in influencing senior managers of life insurance companies to more strongly encourage and support

TABLE II

Impact of IMSA's ethical market conduct program on various aspects of the life insurance marketplace

	Possible outcomes of IMSA's ethical market conduct program	Anticipated impact of IMSA – 1998 survey		Perceived impact of IMSA during its first five years – 2003 survey	
		Mean rating†	Rank	Mean rating†	Rank
1.	Improving the public's trust in the life insurance industry	3.20*	7	2.38	8
2.	Improving the ethical environment in which you market individually-sold life insurance and annuity products	3.23*	6	2.68	6
3.	Improving market conduct in the life insurance industry as a whole	3.24*	5	2.79	5
4.	Improving the ethical environment/culture in the principal life insurance company(ies) that you represent in the sale of individual life insurance and annuity products	3.32*	3	3.03	3
5.	Improving the ethical environment/culture in life insurance companies in general	3.25*	4	2.85	4
6.	Improving the market conduct of other life insurance producers against whom you compete in the sale of individual life insurance and annuity products	2.90*	8	2.37	9
7.	Improving the market conduct of life insurance producers in general	2.89*	9	2.46	7
8.	Influencing the senior managers of the principal life insurance company(ies) that you represent to more strongly encourage and support ethical market conduct	3.60*	1	3.20	1
9.	Influencing the senior managers of life insurance companies in general to more strongly encourage and support ethical market conduct	3.58*	2	3.08	2

*Significantly greater than the 2003 survey mean at the 0.05 value.

†Means exclude the responses of those CLUs/ChFCs who indicated either that they had never heard of IMSA's Ethical Market Conduct Program until receiving this survey, or that they learned of the Program while reading the cover letter for the survey.

ethical market conduct (Outcomes 8 and 9). The ethics literature has long recognized the critical role of senior managers in both setting the ethical tone and bringing about change in the ethical environment of the organizations they lead (Sims, 1992). This finding with respect to IMSA's program having its greatest impact on the actions of senior managers is especially important in view of its relationship to the next most important factor identified in both the 1998 and 2003 studies – improvement in the ethical environment/culture of life insurance companies (Outcomes 4 and 5) – which, in turn, is essential to the improvement of the ethical environment for the industry as a whole (Outcomes 2 and 3).

Disappointing, however, is the low ranking in both studies of the perceived impact of IMSA's Ethical Market Conduct Program on improving the market conduct of life insurance producers (Outcomes 6 and 7) since the issues identified as causing the greatest ethical problems for the

industry both in the 1990s and today involve improper conduct of life insurance producers in dealing with clients. The low ranking of both the anticipated and actual impact of IMSA's program on improving the public's trust in the life insurance industry (Outcome 1) is certainly consistent with its perceived impact on improving the market conduct of the members of the industry who deal directly with the public.

With the voluntary nature of its Ethical Market Conduct Program and the leveling out (or possibly even slight decline) of its membership in recent years, IMSA is likely to have limited ability to bring about further improvement in the life insurance industry's ethical environment in the future. IMSA's role would be strengthened significantly if state legislators and insurance regulators were to make membership mandatory for life insurers and were to give IMSA authority to levy significant penalties on market conduct violators similar to the National Association of Security Dealers (NASD) in the investment field. In view of the continuing difficulties that state insurance regulators have experienced in dealing with market conduct problems in the life insurance industry, perhaps private regulation of insurer market conduct coupled with continued state regulation of insurer financial solvency is an option worthy of consideration by the government.

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Robert W. Cooper
2389 NW 162nd Lane,
Clive, IA 50325,
USA
E-mail: robert.cooper @drake.edu

Garry L. Frank
College of Business and Public Administration,
Drake University,
2507 University Avenue,
Des Moines, IA 50311-4505,
USA
E-mail: galafrank@aol.com