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Insurers said to steer reps to in-house wares

By Gary S. Mogel
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NEW YORK — Many insurers are providing incentives to their advisers to sell proprietary products, despite claiming to have "open architecture" platforms, according to industry observers.

MetLife Inc. in January was sued for allegedly providing secret incentives to its advisers to meet quotas for sales of its proprietary mutual funds and life insurance policies (InvestmentNews, Feb. 19).

Several former advisers of AXA Financial Inc. in New York have reported to InvestmentNews that they received proprietary-product incentives — mainly commission "goals" that in effect were quotas which had to be met to keep their jobs — to sell AXA variable annuities and other products."Regulators are concerned that insurers are using incentive programs that may lead a salesperson to steer business or dummy-up quotes," said Julie McPeak, executive director of the Kentucky Office of Insurance in Frankfort, speaking on behalf of the Kansas City, Mo.-based National Association of Insurance Commissioners. Such conduct could be "fraud" or "breach of fiduciary duty" on the part of insurer and adviser, subjecting them to fines and lawsuits, she noted.

NASD has issued "conduct rules" against monetary and other incentives, such as paid vacations, for selling proprietary securities. But many insurers —including those selling VAs and other securities regulated by NASD — have found more creative ways to reward their sales forces.

"Many insurers have set up bogus reinsurance companies and other arrangements that reward top producers who are given equity stakes in these third-party entities," said an attorney in Washington, who asked not to be identified, as some of his former clients are insurers. "These advisers pretend to be independent, but they are actually steering clients into the products that reward them through these hidden-compensation arrangements," he added.

Quotas

MetLife was sued because it was the insurer with which the potential lead plaintiff in the proposed class action did business, noted William Federman, a partner with Federman & Sherwood in Oklahoma City, the plaintiff's law firm. But other insurers have similar incentives, he noted.

MetLife spokeswoman Holly Sheffer said that the New York-based company would not comment, citing the continuing litigation.

Another insurer favoring its proprietary products is AXA, according to several former AXA advisers, who asked not to be identified. AXA is a "VA warehouse that encouraged its advisers to push its proprietary products," said one of the advisers.

"The overwhelming majority of [our sales] are third-party products," AXA spokeswoman Jo Ann Tizzano said in an e-mail statement. Products from hundreds of insurance and investment companies are available on the company's platform, she added.

"Quotas and annuities go hand in hand," said another former AXA adviser. AXA had a "goal" for its advisers of a certain dollar amount in gross direct commissions per quarter, and it would have been extremely difficult, if not impossible, to meet that goal without selling the insurer's proprietary VAs, the adviser added.

"Details of our compensation arrangements are proprietary," Ms. Tizzano said in the statement. "Compensation programs for our financial professionals are designed to meet applicable sales incentive rules, including [Washington-based] NASD's current equal-weighting rules. Moreover, in line with regulations and emerging best practices, our financial professionals disclose to clients how they are compensated."

Favoring proprietary products is a variation of the contingent-

commission controversy, which involved insurer incentives for insurance brokers to place business based on compensation instead of what was in the client's best interests, Ms. McPeak said.

Penalties often depend on the type of license held by the salesperson, she added. For instance, an agent of the insurer may be able to favor a proprietary product, but a broker or a consultant — as a financial adviser who purports to act in the client's best interest — is held to a higher standard, Ms. McPeak added.

Incentives breed bias

Advisers tell clients they are unbiased product evaluators, but the fact is that many of them are biased, said Stuart Lucas, chairman of Wealth

Strategist Network LLC, a Chicago wealth management education company.

"In open-architecture environments, advisers should disclose all incentives in writing to the client to make sure the incentives don't influence the advice," he said.

"Insurance companies' higher payouts for proprietary products are not as well documented as the use of proprietary funds by the major brokers," said Andrew Stoltmann, a securities attorney and partner with Stoltmann Law Offices PC in Chicago. The payouts could be unethical or constitute unlawful concealment if they are not disclosed to clients, he added.

Advisers who steer clients into proprietary products "may be exposed to material-omission allegations if the proprietary product has a higher payout," said Chris Bebel, a securities attorney and partner at an eponymous law firm in Houston. Most advisers are "reluctant" to disclose the higher payout to clients, he added.

"Advisers often wind up selling the proprietary products, because they flock like moths to a flame to products paying greater compensation," Mr. Stoltmann said.

Insurers offer open-architecture platforms because they want their advisers to create the illusion of comparison and choice for clients, according to Bill Singer, a securities attorney with Lawrenceville, N.J.-based Stark & Stark. "It is difficult to sell in a vacuum. If there is no comparison and choice, the consumer becomes suspicious," he said.

Julie McPeak: Regulators are concerned that insurers are using incentive programs.

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