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MEMORANDUM

TO: NORTH CAROLINA LICENSED INSURANCE AGENTS

FROM: David Curtis Smith, Esq.

DATE: September 21, 2005

RE: Rebating Decision

In the last few weeks, the North Carolina Department of Insurance announced its decision concerning the way that North Carolina's anti-rebating statute will apply to the conduct of agents and brokers throughout our state.

Background. This issue has been a hot one nationally among agents. Understand that none of North Carolina's complaints driving NCDOI attention to this issue comes from customers. Nationally, this issue is rarely one where clients complain that they were being served poorly by their agents as a result of promised services for their current or prospective agents. Instead, the Department's enforcement action on this issue is driven exclusively by other agents complaining about the use of various incentives and services in competitive situations.

The Ruling. The Department's hearing officer ruled that agents and brokers are prohibited from providing to their (group or individual) clients "any service" or giving "any thing of value wherein those services or goods are neither (a) referenced specifically or generally in the contract of insurance, nor (b) are advertising in nature." In short, if you give any thing of value to your clients that is not either included in the insurance contract or some item of nominal value which is designed to advertise your agency (e.g. coffee mugs, t-shirts, etc.), it is prohibited.

Given the very, very broad language of this decision, I do not believe it is unreasonable to expect the Department to apply this statute and ruling to prohibit the purchasing of meals for client meetings, providing services to your clients that they would normally have to pay for themselves (e.g. COBRA administrative services) or from providing any service or thing to your clients at no cost or subsidized by the agent with commission income.

One additional point: it would appear that the decision would not apply to self-funded groups due to the federal ERISA exemption.

Based on this ruling, it is my advice that you need to do the following:

1. Communicate with your clients that North Carolina law prohibits you from providing anything of value to your clients as an inducement to maintain a business relationship with your agency.
2. Determine what impact this decision has on your business and how you need to comply to avoid any scrutiny from the Department on questionable practices.
3. If you are currently providing services to your clients (e.g. COBRA administrative services, etc.), you need to stop immediately or, alternatively, bill your clients and collect from them the fees currently being paid by your agency for those services. It is my understanding that the decision also prohibits your providing those services to your clients through the use of your employees or a subsidiary.
4. You need to take a careful look at your agency's marketing materials to ensure that there are no written promises which might result in the appearance of rebating, as the Department defines it.

Next steps. There are a couple of issues of which you need to be aware. I have begun some discussions with the Department and the Attorney General's office to determine the boundaries of this decision. At this point, I am trying to get a clear answer on some basics of understanding of what their intended approach will be for future enforcement. At this time, I suspect that the Department's enforcement will continue on the "squeaky-wheel" approach that has driven their enforcement in the past: complaints will be investigated.

Agents impacted by this decision are in the final stages of determining whether or not we will appeal this decision to the Wake County Superior Court. That decision will be made this week. I do think that there are significant competitive exemptions contained in federal law which might minimize the impact of this decision. These are also being weighed.

Additionally, there are a number of agents interested in finding a way to change the statute to allow agents to continue to provide certain services to their clients. If you are interested in that effort, please let me know.

Conclusion. In short, the breadth of the Department's decision was surprising and will have a significant impact on your business for the coming months, particularly as clients expect certain services from their insurance agencies. I would urge caution because I do believe that the Department may seek now to fully enforce this decision and the best way to do that would be to seek revocation or suspension of agent licensures with fines.

If you have any questions, please give me a call or email me.