

"To Disclose or Not to Disclose":

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**To Disclose or Not to Disclose:
That Is the Question**

Only a modern day Rip Van Winkle would be unaware of the huge settlements the courts are extracting from insurance companies accused of misleading sales or marketing practices. Market conduct may be the most talked about ethical concern of the industry. In a recent survey, Million Dollar Round Table members identified "false or misleading representation of products or services in marketing, advertising, or sales efforts" as the key ethical issue facing life insurance companies today.¹ Testimony from congressional hearings details clear examples of such misrepresentation. Some agents misrepresent whole life policies as retirement savings plans and premiums as monthly deposits, or tout "cash accessibility without penalty" when in truth there are significant penalties for cashing in the policy.

To avoid further litigation, companies turn to their compliance departments to take responsibility for overseeing sales practices. This leads to stringent supervision of sales materials, compliance memos, and training programs. Honest agents feel constrained, offended, and insulted. It becomes clear that relying strictly on compliance procedures and the mandates of compliance departments is not sufficient to curb misrepresentation, and that is for several reasons.

To begin, compliance concerns tend to concentrate on ethically minimal behavior. Total reliance on ethically minimal behavior leads to moral mediocrity and leaves no room for slippage. Compliance also utilizes external control rather than depending on the agent to internalize habits of honesty in selling. Hopefully most individual agents will aim higher than the letter of the law laid down by compliance and try

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to act in accord with the spirit of the law that they have internalized. Finally, even with all the compliance guidance in the world, there are some cases where individual agents will need to make up their own minds. In such cases, the individual agents need to know how to determine if their practices are ethically acceptable.

Recent malpractice suits make it clear that there are two areas where agents are held accountable: (1) suitability, i.e. providing suitable products; and (2) disclosure, i.e. failing to give sufficient disclosure. The professional pledge taken by CLUs to look out for the best interest of the client obliges the agent to find a suitable policy to fill the needs of the client. This requires, of course, that the agent have the competence to ascertain what policies or products best suit the client's needs as well as the will power or moral fiber to overcome the lure of recommending a less suitable policy that pays a higher commission. Meeting the suitability requirement also necessitates that agents learn enough to maintain their level of competence. Still, barring the temptation to sell a less suitable product for a higher commission, the suitability requirement seems to be an issue of competency more than one of ethics.

From an ethical point of view, disclosure is a much more complicated issue for the insurance agent. How much is the agent ethically obliged to disclose? It is an accepted principle in effective salesmanship (not to be confused with ethical salesmanship) to not

say anything negative about the product one is selling and certainly not to disclose shortcomings unnecessarily. For example, if you are selling your home, is it necessary to point out all the minor defects that only you living in the home know? If you do, you probably succeed in discouraging every prospect from buying it. If you are selling yourself during a job interview, should you point out your flaws to your prospective employer? I know of no job counsellor who suggests that.

How much does one need to disclose and to what extent can failure to disclose be construed as market misconduct? To get at that question I invite you to reflect for a moment on two things: how selling is a market transaction, and how lack of disclosure might be similar to lying.

Selling insurance is, among other things, a market transaction. In the ideal market transaction, two people decide to exchange goods because they hope the exchange will make both better off. That is the genius of the market and the defense of our free market system: Freedom of exchange that leads to the overall improvement of the traders' lot. Ideally there is perfect information about the worth of what is being given and gotten in return. Such a trade, freely entered into with full information, should maximize satisfaction on both sides.

However, if one of the parties is misled into believing a product is something it is not because of misrepresentation, the effect of both sides being better off is undermined. Deception usually leads to the deceived party getting something different and less valuable than what they expected. The deceived party most likely would not have freely entered into the exchange had the full truth about the product been presented. So the conditions for an ideal trade include the freedom or autonomy of the participants and full knowledge of the perti-

ment details of the product, which are required if we are to have what is often called "informed consent." One could say that a choice based on inadequate information is no choice at all. An individual's consent cannot be presumed to be given if he or she is either forced into an exchange or lacks adequate knowledge about the product for which the bargain is struck.

Since misrepresentation is a lie, it may be helpful to look at what a lie is and see what is wrong with lying. When asked what lying is, some people answer that it is saying something false. Saying something false, however, is not always lying. The essence of lying is found in its purpose. When lying, besides just making false statements, one is attempting to get the other person to act in a certain way. As a result, lying can be seen as a deceptive activity meant to evoke a certain response that would not have occurred if the truth were told. Simply put, we lie and deceive others to get our way.

Let's apply this notion of lying for the purpose of changing behavior to deceptive sales. A deceptive sale is an activity with a goal of getting the buyer to do what the seller thinks they probably wouldn't do if the truth were known. The agent tells the client the insurance policy is a savings plan. From an economic point of view, such a procedure violates the ideal market principle of perfect information. More importantly, from a moral point of view, the seller takes away the buyer's real choice in the situation, thereby using the buyer for the seller's own ends.

Such use is unjust and immoral and is often called exploitation and/or manipulation. Some would say that not disclosing isn't lying, it's just not telling. But that misses the point. Any action of deliberately withholding information to get another to act contrary to the way they would with the information has the

same deceptive structure and consequence as the overt lie. It doesn't allow for an informed choice.

Must one disclose everything? Certainly some failure to disclose is wrong, but just how much must we disclose? Whenever you are tempted not to disclose something, ask yourself why you are not disclosing. If you are withholding information because you fear losing the sale if the consumer or client knows the whole story, you are manipulating.

In some situations it might be hard to decide how much to disclose. Let me introduce a brief scenario that my students quite often vehemently disagree about.

Brock Roberts, CLU, and Cosmic Life agent, needs one more sale to qualify for membership in Cosmic Life's top production club and a trip to Aruba. Marie, a client who buys all of her insurance from Brock, has a clearly established need for additional insurance. She has asked Brock for three proposals from companies with equal credit ratings. Brock presents illustrations from Cosmic Life, Stable Life, and Exciting Life. He accurately demonstrates that all three policies will fill Marie's need. If she chooses Cosmic, Brock will win the trip. Exciting Life pays a first-year commission that is much higher than that paid by the other two carriers and Stable Life has the strongest long-term financial performance history of the three companies. These facts are unknown to the client. Marie asks Brock to "recommend the best of the three." Brock recommends Cosmic to Marie and that is what she buys. Marie has no inkling that Brock is on the verge of winning an Aruba trip. Should she know this? Why or why not?²²

As I said, I get vehement disagreement about how to answer the question of whether Brock should disclose the trip. I am inclined to think that even if Brock thinks Cosmic is as good a buy

as Stable or Exciting, and even if he feels comfortable recommending it, he should still disclose the information about the trip. I am also sure that there will be a great deal of disagreement about whether he should disclose.

How is one to decide? In the face of such disagreement, I would suggest adopting the following method: Ask yourself *why* you would be reluctant to disclose the trip? If you are reluctant because you think telling the client about the trip will affect the sale, shouldn't you disclose it to give the client that option? If you are reluctant because you think telling the client won't affect the sale, since the client trusts you implicitly to do the best for her, then why be reluctant to disclose? If you are reluctant because you think too much disclosure gives too much information and will confuse the client, aren't you putting yourself in the position of deciding how much information the client can handle? And how do you determine how much? In withholding possibly relevant information aren't you creating a questionable paternalistic relationship? Why not just give Marie the information and let her decide?

In the discussions of this case, I have heard any number of reasons given for not disclosing. "No one does it." "It's not necessary, the client trusts me." "The client doesn't need all that information, they'll just get confused." "It's no business of the client's." Are these reasonable defenses of the behavior or are they rationalizations? I don't see a good reason not to disclose.

As an added consideration, one might contemplate what would happen if the client buys Cosmic Life on Brock's recommendation and it doesn't perform as well as Stable or Exciting. Later the client finds out the sale of Cosmic was tied to an all-expense-paid vacation. How will that look? Admittedly we have said that bad consequences to oneself do not

constitute the primary reason to disclose, but it does provide us with a prudential consideration to keep in mind.

If you are reluctant to tell the client you are selling insurance, ask yourself why? Perhaps you don't think an insurance policy best fits the needs of the client. In that case you should disclose because you are putting your interest before the best interest of the client. Perhaps you think the client doesn't want insurance so much as a straightforward mutual fund program. In that case you should disclose, again for the same reason. Are you glossing over the nonguaranteed aspect of cash value projections in variable products? Why? Perhaps you think that if the client realizes the growth promises are not guaranteed, they will look for another product. Once again, if that is so, it seems clear you are putting your interests above those of the client's

and using the client to further your own goals. That violates the central ethical tenet of "Do unto others what you would have done unto you." Such nondisclosure fails to respect the other and treats them merely as a means or instrument to be used for your own gratification. That is what the great ethical Immanuel Kant saw as the height of immorality.

However we resolve the issue now, the question of how much disclosure is necessary in order to avoid manipulation of a client and whether commissions and other costs should be disclosed is being talked about and will continue to be talked about intensely. Consumers will demand to know what they are buying and agents will be pressured into disclosing more and more. Old practices will be reviewed and reformed. That's how ethics usually solves these issues. For now, the

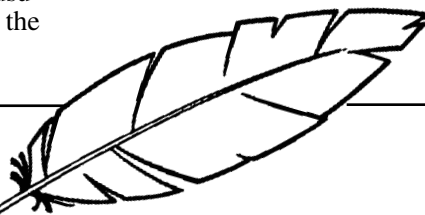
safest road, and the most ethical, is the following: When in doubt, disclose! **J** (I/R Code No. 4400.99)

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- (1) Robert W. Cooper, John P. Bell, and Garry L. Frank, "The Ethical Environment Facing Life Insurance Professionals: Views of MDRT Members," *The Journal of the American Society of CLU and ChFC*, vol. L, no. 2, (March 1996): 64.
(2) Burke A. Christensen and Ken Cooper, eds., *The Best of Strictly Speaking*, (Bryn Mawr, Pa: The American College and the American Society of CLU and ChFC, 1995) 26.
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