When Innovation Meets Regulation: InsurTech and State Licensing Laws

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The rise of InsurTech — which brings technological innovations to the business of insurance — is having a significant impact on the insurance industry, including through advancements in cybersecurity tools, the introduction of blockchain, and the use of big data for underwriting and claims. Yet many worry that complex insurance regulations will slow or even prevent further innovation. This article is the second in a series discussing the regulatory issues impacting InsurTech. As innovations continue to transform the insurance industry, so too will regulatory issues continue to arise. A number of InsurTech companies have attempted to enhance the consumer experience by increasing efficiency and convenience, such as by offering mobile apps, providing on-demand services, and implementing rewards programs. Forming relationships with these businesses can be a boon to insurance companies as well, enabling them to offer new products and services, modernize their marketing, increase internal efficiencies, and attract and retain customers. And while InsurTech impacts multiple aspects of the insurance business, it has the potential to — and, indeed, has significantly changed — how insurance is sold and marketed. But innovation in this area comes with unique challenges. The insurance industry is highly regulated, and these regulations — enacted before new technology existed — affect not only insurance companies but their industry partners as well. Each state has its own licensing requirements, necessitating that insurance producers obtain licenses in each state in which they sell, solicit, or negotiate insurance, an issue further complicated by digital sales that cross state lines. The National Association of Insurance Commissioners (NAIC) promulgated the Producer Licensing Model Act (Model 218) to require the licensing of producers. Many states have adopted the NAIC's Model Act in whole or in part, and, consistent with the model, all states require producers to be licensed in that state in order to sell, negotiate, or solicit insurance. Whether it is necessary to obtain a producer license has long been a question for insurance-related actors. The answer depends, in large part, on what it means to sell, solicit, and negotiate insurance. This, however, is not always clear, and can vary by state. The NAIC model defines selling insurance as "exchang[ing] a contract of insurance by any means, for money or its equivalent, on behalf of an insurance company." What it means to solicit or negotiate insurance can be even more nuanced. NAIC Model 218 defines "solicit" as "attempting to sell insurance or asking or urging a person to apply for a particular kind of insurance from a particular company," while "negotiate" means "the act of conferring directly with or offering advice directly to a purchaser or prospective purchaser of a particular contract of insurance concerning any of the substantive benefits, terms or conditions of the contract, provided that the person engaged in that act either sells insurance or obtains insurance from insurers for purchases." Regulators have commonly found that a person is "soliciting, negotiating, or selling" insurance when she engages in activities such as explaining coverage, providing recommendations about insurance, quoting insurance rates, or advising prospective consumers to buy a certain policy or obtain insurance from a particular company. However, most states do not require a license if a person's activities are limited to advertising without the intent to solicit insurance. Similarly, a license is not required for information provided by employees of an insurer or producer who perform administrative or other tasks that are only indirectly related to sales and who do not receive commissions on policies. Additionally, providing general information that does not include advice or recommendations or relaying the name and contact information of a licensed producer to a prospective policyholder may be exempt from licensure requirements. The advent of InsurTech has put these issues front and center for many startups. The industry saw one cautionary tale after multiple state regulators fined a software company that partnered with insurers to sell insurance policies to businesses using its products, finding it had allowed unlicensed employees to sell, solicit, and negotiate insurance. The activities at issue included not only the sale of policies but also presentations to potential customers about the insurance products the company offered through its partners. This ultimately led to a change in the company's business model, as it began working with outside insurance brokers. Licensing is an area of concern both for InsurTech companies that may solicit or sell insurance and for the insurance companies that partner with them, as state laws also regulate how non-licensees may be compensated. Section 13(A) of NAIC Model 218 prohibits insurers and producers from paying commissions to a person for selling, soliciting, or negotiating insurance unless the person is licensed in that state, though the NAIC Model and many states have various exceptions to the general rule. Such laws pose challenges for insurers partnering with tech startups to market and sell their insurance across new digital platforms. For example, regulators and others have recently taken a closer look at a digital property and casualty insurer that sells policies online and through an app and uses technology to provide insurance and pay claims in minutes. The company recently received approval from regulators in multiple states to sell renters and homeowners insurance policies. However, after it enabled partnering companies to offer its insurance policies on their own apps and websites last year, some began questioning whether this implicated state licensing laws. The insurer at least planned ahead: the company has stated that its compliance program helps ensure those using its platform are not themselves selling insurance and it does not pay commissions to unlicensed producers —though only time will tell if regulators agree. Still, other startups looking to enter the insurance industry would also be wise to consider — in advance — the various licensing regulations applicable in each state and what impact those regulations will have on their particular business model.

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