

NAVIGATING THE SAFE HARBORS OF GLB

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In November 1999, barriers that once prevented banks,¹ insurers, and investment companies from expanding into each other's businesses were removed when President Clinton signed the Gramm-Leach-Bliley Act ("GLB") into law.² Companies may now offer banking, insurance and securities products under one roof.

GLB takes a "functional approach" to regulation of the activities of these multi-faceted organizations. Regulatory authority is based on the type of activity involved, rather than the type of institution that engages in that activity. Accordingly, regardless of who is engaging in insurance activities, those activities are subject to regulation by state insurance authorities.

The "Safe Harbors"

GLB explicitly recognizes "the primacy and legal authority of the states to regulate the insurance activities of all persons," including state and national banks.³ However, GLB prohibits states from interfering with a bank's ability to participate in insurance sales, solicitation or cross-marketing activities,⁴ effectively codifying the U.S. Supreme Court's decision in *Barnett Bank v. Nelson*, 517 U.S. 25 (1996). GLB permits states to impose restrictions on the insurance sales activities of banks only if those restrictions are "substantially the same as but no more burdensome or restrictive" than the thirteen Safe Harbors provisions.⁵

State insurance law will not be preempted if it falls within one of the following Safe Harbors:

- Prohibits rejection of an insurance policy required in connection with a loan because it was sold by an unaffiliated agent.⁶
- Prohibits imposition of extra charges on insurance policies required in connection with a loan that is purchased from an unaffiliated agent.⁷
- Prohibits misrepresentations regarding the insured or guaranteed status of any insurance product.⁸
- Requires that commissions can be paid only to licensed insurance agents.⁹
- Prohibits payment of referral fees to non-licensed individuals where those fees are based on whether the referral results in a transaction.¹⁰
- Prohibits release of insurance information to third parties without the express written consent of the customer.¹¹
- Prohibits use of health information obtained from insurance records without the express written consent of the customer.¹²
- Prohibits tying arrangements.¹³
- Requires the disclosure, prior to any insurance sale, that the product is (1) not a deposit, (2) not insured by the FDIC, (3) not guaranteed by the financial institution or its subsidiaries or affiliates, and (4) where appropriate, involves investment risk, including loss of principle.¹⁴
- When insurance is required in connection with a loan, requires disclosure that the purchase of insurance from an unaffiliated agent will not affect the loan decision or the credit terms.¹⁵
- Requires completion of credit and insurance transactions through separate documents.¹⁶

- Prohibits inclusion of insurance premiums in a primary credit transaction without the express consent of the customer.¹⁷
- Requires maintenance of separate insurance books and records that must be made available to state insurance regulators for inspection.¹⁸

The Safe Harbors apply to state laws and regulations already in effect and any that may be enacted in the future.

NAIC Activity

In an effort to ensure compliance with and uniformity among the states in their regulation of the insurance sales activities of banks, the National Association of Insurance Commissioners (the “NAIC”) began to explore ways to incorporate into an NAIC Model Act restrictions on bank insurance sales activities requirements that satisfy GLB’s Safe Harbors.

The insurance and banking industries argued that additional action by the NAIC and individual states was unnecessary, since most states already regulate insurance sales activities – including activities conducted by or on behalf of a bank. Several national insurance trade associations maintained that “existing state law addresses *every* aspect of the subject matter of the Safe Harbors.”¹⁹

Nevertheless, the NAIC concluded that that additional action would help states with weak or silent regulation related to bank insurance sales. “Without a model, we open the door for federal intrusion. It is essential that we establish uniform state authority on consumer protection that meets the federal government’s requirements on Safe Harbors.”²⁰ In June 2001, the NAIC amended its Unfair Trade Practices Model Act (the “UTPA”) to include provisions related to GLB’s Safe Harbors.²¹ Section 5 of the UTPA regulates each of the thirteen areas of permissible state regulation protected by the Safe Harbors.

State Activity & Preemption

Although no state has adopted Section 5 of the UTPA, a few states including Indiana, Illinois and Ohio, have proposed legislation to mirror Section 5. Many in the insurance and banking industries continue to emphasize that no additional regulation is needed. However, in states where action on this issue appears likely, the industry endorses verbatim enactment of Section 5 of the UTPA. There is concern that virtually any deviation from the language of the Model could have significantly detrimental effects on bank insurance activities.

An Example of the Preemption Analysis

The Safe Harbors establish the standard by which existing and new state laws governing bank insurance sales, solicitation and cross-marketing activities will be evaluated. The first example of how GLB, including its Safe Harbors, may impact state insurance laws relates to a challenge to West Virginia’s Insurance Sales Consumer Protection Act (the “West Virginia Act”). Enacted in 1997, the West Virginia Act restricts insurance sales, solicitation, and cross-marketing activities of financial institutions. In May 2000, the West Virginia Bankers Association requested an opinion from the Office of the Comptroller of the Currency (the “OCC”) regarding whether Section 104 of GLB preempts certain provisions of the West Virginia Act.²² The OCC’s opinion on the West Virginia Act provides the first example of the scrutiny that state insurance laws may face if they are challenged as violative of the GLB Safe Harbors.²³

While many banking organizations argued that some or all of the provisions of the West Virginia Act were preempted, agents groups asserted that all provisions fell within the Safe Harbor provisions of GLB or “did not prevent or significantly interfere with the ability of a financial institution to engage in any insurance sales, solicitation or cross-marketing activity.”²⁴

The OCC’s Preemption Opinion,²⁵ issued on September 24, 2001, found that federal law preempts some, but not all, provisions of the West Virginia Act. The OCC determined that the federal law *does not* preempt the following provisions of the West Virginia Act with respect to national banks:

- A prohibition against requiring or implying that the purchase of an insurance product from a financial institution is required as a condition of a loan.²⁶
- A prohibition on a financial institution offering an insurance product in combination with other products unless all of the products are available separately.²⁷
- A requirement that, where insurance is required as a condition of obtaining a loan, the insurance and credit transactions be completed independently and through separate documents.²⁸

The OCC Opinion states that GLB *does* preempt the following provisions of the West Virginia Act with respect to national banks:

- A requirement that financial institutions use separate employees for insurance solicitations.²⁹
- Restrictions on the timing of bank employees' referral or solicitation of insurance business from customers who have loan applications pending with the bank.³⁰
- Restrictions on sharing with bank affiliates information acquired by a financial institution in the course of a loan transaction to solicit or offer insurance.³¹
- A requirement that financial institutions segregate the place of solicitation or sale of insurance from the deposit-taking and lending areas.³²

The OCC also determined that one provision of the West Virginia Act was preempted *in part*. The provisions prescribing the content of the disclosures that a financial institution must make in connection with the solicitation of an insurance product, and the requirement that a financial institution that sells insurance obtain a written acknowledgment, in a separate document, from its insurance customer that certain disclosures were provided are not preempted. However, the provisions regarding the manner and timing of certain required disclosures are preempted.³³

In addition to providing insight into the OCC's views on how GLB applies to specific types of state insurance laws, the OCC's Opinion is important reading because it provides a framework for a preemption analysis of state insurance laws. The OCC indicates that Section 104 of GLB requires a three-step analysis to determine whether a state law is preempted.

1. Is the preemption standard in Section 104 of GLB applicable? That is, which provision in subsection of Section 104 governs?³⁴
2. If the state law pertains to insurance sales, solicitation, or cross-marketing, does the particular provision falls within one or more of the thirteen Safe Harbors in GLB?³⁵ A state law that is covered by a Safe Harbor, or that is "substantially the same as but no more burdensome or restrictive than"³⁶ a Safe Harbor, is protected from federal preemption under the standard in Section 104(d)(2)(A).³⁷
3. If the state law pertains to insurance sales, solicitation, or cross-marketing but is not protected by a Safe Harbor, is it preempted under the *Barnett* standard incorporated in Section 104? "This determination ... depends on the effect that the state law has on a national bank's ability to exercise its federally authorized power to engage in insurance agency activities and on the scope of that effect."³⁸

Applying this three-step analysis to the West Virginia Act, the OCC focused on how each challenged provision of the statute affected a national bank's ability to engage in insurance sales, solicitation, and cross-marketing activities, and on the nature and extent of that effect. The OCC also considered whether each provision imposes requirements that had the same, or substantially the same, effect on a national bank as requirements imposed by federal law. According to the OCC Opinion, if federal law imposes a restriction on a national bank's ability to exercise its insurance powers that is similar to a restriction included in state law, a federal court is unlikely to find that the state statute "prevents or significantly interferes with the bank's exercise of those powers within the meaning of the *Barnett* standards."³⁹

In May 2000, the Massachusetts Bank Insurance Law became the focus of discussion related to federal preemption. The Massachusetts Bankers Association has asked the OCC to render an opinion on whether GLB preempts three particular provisions in this state law:

1. The “Referral Prohibition,” forbids a non-licensed bank employee from referring prospective insurance customers to an agent or broker unless the customer initiates the inquiry.⁴⁰
2. The “Referral Fee Prohibition,” bars non-licensed bank employees from receiving any additional compensation for making referrals, even if the compensation is not conditioned upon the sale of insurance.⁴¹
3. The “Waiting Period Requirement” prohibits banks from making an insurance solicitation in connection with a loan application until after the loan has been approved – and in some circumstances not until the customer has accepted the bank’s written commitment to extend credit.⁴²

The OCC has not yet issued an opinion with respect to preemption of the Massachusetts law.

Conclusion

On its face, GLB appears simply to codify the standards established in *Barnett* regarding state regulation of the insurance activities of banks and other financial institutions. States retain primary regulatory authority over the insurance activities of banks, and may impose restrictions on bank insurance sales, solicitation and cross-marketing activities, so long as those restrictions fall within GLB’s Safe Harbors. The OCC’s analysis of the West Virginia Insurance Sales Consumer Protection Act provides specific guidance regarding the OCC’s views about the scope of states’ authority. However, the NAIC’s adoption of a new section of the Unfair Trade Practices Model Act, and recent activity by some states to enact corresponding statutory provisions may complicate this issue. Even if new state laws fall within the Safe Harbors, if these laws vary from one another, they may have the effect of complicating efforts by the financial services industry to fully avail themselves of the sales and cross-marketing opportunities promised by GLB and the *Barnett* decision.

Endnotes

1. The term “bank” as used in this article means all “depository institutions,” as defined in section 34 of the Federal Deposit Insurance Act. “Bank” includes state and national banks and state and federal savings associations.
2. Gramm-Leach-Bliley Act, Pub.L.No. 106-102, 113 Stat. 1338 (1999) (hereinafter “GLB”).
3. H.R. Rep.No. 106-434, at 156 (1999) (a joint statement expounding on the operation of state law); GLB § 104(c), 15 U.S.C. 6701(c). The Federal Reserve Board serves as the “umbrella regulator” of the parent holding company.
4. GLB § 104(d)(1), 15 U.S.C. § 6701(d)(1).
5. GLB § 104(d)(2)(B), 15 U.S.C. § 6701(d)(2)(B). Sec. 305 of GLB also required federal banking regulators to adopt “insurance customer protection regulations,” applicable to insurance sales activities of banks and persons acting on behalf of banks. These rules, the “Consumer Protections for Depository Institution Sales of Insurance,” apply only in states that either have no comparable regulation, or where the federal rules afford greater customer protection. 65 Fed. Reg. 75822 – 75848 (Dec. 4, 2000) (codified at 12 CFR pts. 14, 208, 343, and 536).
6. GLB § 104(d)(2)(B)(i), 15 U.S.C. § 6701(d)(2)(B)(i).
7. GLB § 104(d)(2)(B)(ii), 15 U.S.C. § 6701(d)(2)(B)(ii).
8. GLB § 104(d)(2)(B)(iii), 15 U.S.C. § 6701(d)(2)(B)(iii).

9. GLB § 104(d)(2)(B)(iv), 15 U.S.C. § 6701(d)(2)(B)(iv).
10. GLB § 104(d)(2)(B)(v), 15 U.S.C. § 6701(d)(2)(B)(v).
11. GLB § 104(d)(2)(B)(vi), 15 U.S.C. § 6701(d)(2)(B)(vi).
12. GLB § 104(d)(2)(B)(vii), 15 U.S.C. § 6701(d)(2)(B)(vii).
13. GLB § 104(d)(2)(B)(viii), 15 U.S.C. § 6701(d)(2)(B)(viii).
14. GLB § 104(d)(2)(B)(x), 15 U.S.C. § 6701(d)(2)(B)(x).
15. GLB § 104(d)(2)(B)(ix), 15 U.S.C. § 6701(d)(2)(B)(ix).
16. GLB § 104(d)(2)(B)(xi), 15 U.S.C. § 6701(d)(2)(B)(xi).
17. GLB § 104(d)(2)(B)(xii), 15 U.S.C. § 6701(d)(2)(B)(xii).
18. GLB § 104(d)(2)(B)(xiii), 15 U.S.C. § 6701(d)(2)(B).
19. Letter from Michael Lovendusky, Assistant General Counsel, American Insurance Association, to Nathaniel Shapo, Chair, NAIC Consumer Protections Working Group (October 26, 2000).
20. *State Regulations: No Safe Harbor Model Law For Now*. Insurance Accounting, May 29, 2000 at 8.
21. NAIC Unfair Trade Practices Model Act § 5 (2001).
22. Notice of Request for Preemption Determination, 65 Fed. Reg. 35420 (June 2, 2000).
23. National agent trade associations have challenged the OCC opinion in U.S. District Court; no decision has been issued.
24. Preemption Opinion, Department of the Treasury, Office of the Comptroller of the Currency, No. 01-22 (September 24, 2001).
25. *Id.*
26. Preemption Opinion, Department of the Treasury, Office of the Comptroller of the Currency, No. 01-22 (September 24, 2001); W.Va. Code §33-11A-8(a) (2000).
27. Preemption Opinion, Department of the Treasury, Office of the Comptroller of the Currency, No. 01-22 (September 24, 2001); W.Va. Code §33-11A-8(b) (2000).
28. Preemption Opinion, Department of the Treasury, Office of the Comptroller of the Currency, No. 01-22 (September 24, 2001); W.Va. Code §33-11A-11(a) (2000).
29. Preemption Opinion, Department of the Treasury, Office of the Comptroller of the Currency, No. 01-22 (September 24, 2001); W.Va. Code §33-11A-6 (2000).
30. Preemption Opinion, Department of the Treasury, Office of the Comptroller of the Currency, No. 01-22 (September 24, 2001); W.Va. Code §33-11A-10(a) (2000).
31. Preemption Opinion, Department of the Treasury, Office of the Comptroller of the Currency, No. 01-22 (September 24, 2001); W.Va. Code §33-11A-13(b)-(c) (2000).

32. Preemption Opinion, Department of the Treasury, Office of the Comptroller of the Currency, No. 01-22 (September 24, 2001); W.Va. Code §33-11A-13(b)-(c) (2000).
33. Preemption Opinion, Department of the Treasury, Office of the Comptroller of the Currency, No. 01-22 (September 24, 2001); W.Va. Code §33-11A-9(a)-(c) (2000). (“The manner and timing requirements for the disclosures required by the West Virginia provision are more far-reaching than Safe Harbor (x), found in Section 104(d)(2)(B)(x). Section 9(a) requires the bank to make the disclosures ‘in any advertisement or promotional material, and orally during any customer contact. Safe Harbor (x) is far more limited in scope, protecting only state law provisions that require the bank to make the disclosure prior to the sale of an insurance policy. Moreover, Section 9(1) requires disclosures to be made prominently ... in clear concise language, whereas Safe Harbor (x) covers state laws that require the disclosures to be clear and conspicuous ... where practicable. Omission of the phrase, ‘where practicable,’ eliminates an important qualification on the disclosure requirement.” Preemption Opinion, Department of the Treasury, Office of the Comptroller of the Currency, No. 01-22 (2001)).
34. Preemption Opinion, Department of the Treasury, Office of the Comptroller of the Currency, No. 01-22 (September 24, 2001).
35. *Id.*
36. GLB § 104(d)(2)(B), 15 U.S.C. § 6701(d)(2)(B).
37. Preemption Opinion, Department of the Treasury, Office of the Comptroller of the Currency, No. 01-22 (September 24, 2001); (The standard incorporated in Section 104(d)(2)(A) is that “no State may, by statute, regulation, order, interpretation, or other action, prevent or significantly interfere with the ability of a depository institution, or an affiliate thereof, to engage, directly or indirectly, either by itself or in conjunction with an affiliate or any other person, in any insurance sales, solicitation, or cross-marketing activity.”).
38. Preemption Opinion, Department of the Treasury, Office of the Comptroller of the Currency, No. 01-22 (September 24, 2001).
39. *Id.*
40. David Giusti, *The Scrap Over Massachusetts’ Bank Insurance Sales Law*, Bank Insurance Marketing, Autumn 2000 at 8.
41. *Id.*
42. *Id.*