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Press Release

Attorney General Announces \$5 Million Settlement Requiring Sweeping Reforms With Fortune 500 Company

November 14, 2007

Attorney General Richard Blumenthal today announced The Principal Financial Group (Principal) has agreed to pay \$5 million and adopt sweeping business reforms to resolve allegations that it illegally paid millions of dollars in concealed compensation to brokers in order to ensure access to lucrative pension plan business.

Principal, a FORTUNE 500 company, will pay \$4.4 million into a fund to provide restitution to certain pension plan customers across the nation that may have been harmed by the alleged scheme. The company will also pay a \$600,000 civil penalty to Connecticut.

Since at least 1998, in connection with certain Single Premium Group Annuity and Single Premium Guaranteed Immediate Annuity (SPGA) contracts, Principal has paid approximately \$3.2 million in undisclosed compensation to a group of brokers, including BCG Terminal Funding Company, Brentwood Asset Advisors, LLC, Dietrich and Associates, Inc., Sharp Benefits, Inc. and USI Consulting Group, which is located in Glastonbury.

These arrangements provided a select group of brokers - who collectively controlled a significant share of the market in the placement and sale of SPGA contracts - with compensation beyond specified disclosed "commissions" in connection with the sale, marketing or placement of SPGAs.

In Principal's own words, the arrangements were "a means of adding some additional compensation without having to be completely up-front" with the pension plan sponsors about the compensation provided to brokers.

"This national settlement provides both significant restitution and sweeping reforms," Blumenthal said. "Principal's schemes potentially inflated pension plan costs for private and public pension plans nationwide. Principal paid hidden commissions to brokers disguised as expense reimbursement agreements, marketing agreements or administrative costs."

Blumenthal said, "Principal promises its customers 'We'll Give You an Edge,' but its hidden payments edged out competitors and harmed consumers. This scheme potentially denied consumers the best deal and competitors a fair chance.

"More than the money, today's settlement provides sweeping business reforms by Principal - detailed disclosures to consumers about compensation arrangements, and a ban on concealed compensation to brokers. These profound protections should be the industry wide model.

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"Principal has cooperated with my office and has agreed to continue cooperating throughout this ongoing investigation. This agreement is a recognition of the company taking responsibility for its actions."

Due to the complexities associated with a pension plan's administrative requirements and legal obligations, many plan sponsors rely on an experienced pension broker to guide and navigate the plan to make the right annuity choice. The plan expects the broker to act for the benefit of the plan sponsor.

Brokers are generally compensated in one of two ways - a fee negotiated between the plan sponsor and the broker, which is paid directly by the plan to the broker, or a commission agreed to by the plan sponsor and paid by the selected insurance company, which builds the commission into the final annuity premium.

While certain brokers claimed to act for the benefit of the plan and to obtain the best product at the best price, their recommendations were often motivated by the additional, undisclosed compensation they received from Principal.

In some cases, the compensation exceeded the disclosed specified "commission" by more than 100 percent. The agreements provided additional compensation to the brokers without revealing higher commission costs to clients.

These secret payment arrangements were at times called "Expense Reimbursement Agreements" (ERAs), "Marketing Agreements" or "Service Agreements."

In letters to brokers in June 2000, Principal said that after careful evaluation of "the nature of the agreement," Principal decided to terminate ERAs and that, "since the ERA will no longer be used, the total amount of commission will be fully disclosed to the customer."

However, under pressure from brokers unhappy with the elimination of ERAs, Principal agreed to develop new ways to funnel hidden compensation - in addition to the disclosed commissions - to numerous brokers.

Principal's revamped broker compensation scheme was disguised in various new ways - as "administrative and consulting" costs or "Marketing Agreements" and "Service Agreements."

As an internal Principal email states, "I'm still thinking we can have something pretty similar to current ERAs, but just not call it an ERA."

Principal paid the brokers additional compensation apart from specified "commissions" in 83 SPGA cases throughout the United States. The pension plans included a diverse set of private, public and non-profit establishments, including Macristy Industries, Inc. of New Britain and Bead Industries, Inc. of Milford.

In 1999 and 2000, Bead purchased two separate SPGA contracts from Principal with Sharp Benefits as the broker. In both cases, Principal and Sharp Benefits affirmatively represented to Bead that Sharp Benefits' "compensation" would be "not greater than 3 percent of the total premium."

In reality, Sharp Benefits obtained four percent. The extra one percent was the result of the ERA that Sharp Benefits had in place with Principal. In one of the contracts Principal was not the lowest bidder. Between the two Bead contracts - collectively worth \$2.8 million - Principal paid Sharp Benefits more than \$28,000 in hidden compensation, above and beyond the disclosed \$85,000 in

commission.

In one of the most egregious examples, Principal was the successful bidder on a \$297 million placement for Bull HN Information Systems of Massachusetts, one of the largest SPGAs placed in 2002. The sale was handled through Brentwood Asset Advisors (based in California and Florida). Although Principal disclosed to Bull HN that the compensation to be paid to Brentwood "will not be greater than" a "flat \$125,000," in reality Principal paid Brentwood an additional undisclosed \$594,734.50, which also unknown to Bull HN, was built into the cost of its SPGA premium.

Under today's settlement, Principal must, by early January 2008, identify customers eligible for restitution and calculate the amount each will receive from the SPGA restitution fund.

In the sale and placement of SPGAs to pension plans, Principal has also agreed to:

- impose a four-year ban on any broker compensation apart from the disclosed commissions for SPGA products and lines of business.
- provide written disclosures to brokers and customers in its initial SPGA proposals - prior to binding - of all compensation and commissions paid to the broker, and receive written consent of each of its customers to such terms.
- provide, by the end of the calendar year, written disclosure to pension plan customers of all compensation and commissions paid to or to be paid to the broker in relation to that customer's SPGA.
- post a disclosure on its website - in a format to be approved by Blumenthal's office - of its compensation practices and policies.
- implement written standards of conduct regarding compensation and commissions paid to brokers, and appropriate employee training.

Blumenthal thanked those in his office who worked on the investigation - Assistant Attorney General Erik Zwicker and Paralegal Lori Measer, under the direction of Assistant Attorney General Michael Cole, Chief of the Attorney General's Antitrust Department.

[Full version of Settlement Agreement](#) - (PDF-66KB)

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