



Transmitted Via E-Mail to Jolie Matthews (jmatthews@naic.org) & Jennifer McAdam (jmccadam@naic.org)

October 1, 2019

The Honorable Jillian Froment
Director, Ohio Department of Insurance
Chair, NAIC Annuity Suitability Working Group

Re: 9/17/19 Draft of Proposed Revisions to the Suitability in Annuity Transactions Model Regulation

Dear Director Froment:

These comments are submitted on behalf of the undersigned trade groups (Joint Trades) in response to the National Association of Insurance Commissioners (NAIC) Annuity Suitability Working Group (Working Group) September 17, 2019 draft of proposed revisions to the Suitability in Annuity Transactions Model Regulation (Model Regulation) (9/17/19 Draft). We remain committed to a harmonized best interest standard of care for annuities across all regulatory platforms that enhances protections for consumers seeking guaranteed lifetime income in retirement. We appreciate the efforts of the Working Group to achieve such harmonization reflected in the 9/17/19 Draft.

Our members support a transactional best interest standard of conduct for recommendations of annuities that will provide a clear objective standard for compliance and regulatory oversight of best interest obligations under the Model Regulation. Accordingly, we support the 9/17/19 Draft's proposed new framework for the Model Regulation that would require financial professionals to "act in the best interest of the consumer" by complying with four "buckets" of obligations (care, disclosure, conflict of interest, and documentation obligations). This framework is in broad alignment with the Securities and Exchange Commission (SEC) Regulation Best Interest (Reg BI), which we believe will go a long way toward ensuring a harmonized standard of care across all regulatory platforms.

While the 9/17/19 Draft provides a strong framework and aligns well with SEC Reg BI in many key respects, we do have some concerns with the 9/17/19 Draft that are explained below and

addressed in the attached “redline” of the 9/17/19 Draft.¹ Our comments cover several key points, which we will explain below. In addition, we have suggested several technical changes in the redline and we can provide more detail and explanation as needed.

Section 1. Purpose

We have proposed modifications this Section to clarify that the required standard of conduct does not guarantee an outcome. This language is included in New York’s Regulation 187, and we believe it would be appropriate to include this important clarification in the Model Regulation as well.

We have added a sentence to Section 1(A) that reads: *The best interest standard set forth in this regulation requires a producer to adhere to a standard of conduct but does not guarantee an outcome.*

Section 4. Exemptions

We have suggested deleting language regarding a specific exemption for certain direct response solicitations. We believe that this amended Model Regulation is intended to apply only to solicitations where there is a recommendation.

Section 4(A) reads: ~~Direct response-s Solicitations, sales or purchases of an annuity where there is no recommendation based on information collected from the consumer pursuant to this regulation based on information collected from the consumer pursuant to this regulation.~~

Section 5. Definitions

“Consumer Profile Information”

We are suggesting three modifications to this definition. We have deleted paragraphs (3) and (5) as the language used was duplicative of the language used earlier in the definition. We have also deleted the final phrase in paragraph (11) (~~including variability in premium, death benefit or fees~~) because we have added a definition of “Non-guaranteed elements” (see below).

“Material conflict of interest” and “Non-cash compensation”

We agree with the construct that the Working Group has suggested with these definitions. We have suggested modifications to Section 5(I)(2) and Section 5(J) for clarity.

Section 5(I)(2) reads: *“Material conflict of interest” does not include cash compensation or non-cash compensation. “Material conflict of interest” also does not include health insurance, office rent, office support, retirement benefits, or employee benefits provided to employees (including, but not limited to, statutory employees).”*

And Section 5(J) reads: *“Non-cash compensation” means any form of compensation that is not cash compensation, including, but not limited to, merchandise, gifts, prizes, travel*

¹ Please note that for ease of review, we started with the 9/17/19 Draft, “accepted” all changes marked in that draft and then added our comments against that “clean” document.

expenses, meals, and lodging. “Non-cash compensation” does not include health insurance, office rent, office support, retirement benefits, or employee benefits provided to employees (including, but not limited to statutory employees).”

“Non-guaranteed elements”

As mentioned, above, we have suggested adding a new definition, “Non-guaranteed elements.” In the interest of ensuring consistency across NAIC model regulations, this definition is taken directly from the NAIC Annuity Disclosure Model Regulation.

“Non-guaranteed elements” means the premiums, credited interest rates (including any bonus), benefits, values, dividends, non-interest based credits, charges or elements of formulas used to determine any of these, that are subject to company discretion and are not guaranteed at issue. An element is considered non-guaranteed if any of the underlying non-guaranteed elements are used in its calculation.

“Recommendation”

We are suggesting a modification to simplify and clarify that the recommendation is the advice provided, while at the same time ensuring that the requirements of the Model Regulation apply regardless of the result of the advice being given.

As amended in the redline, Section 5(L)² reads: *“Recommendation” means advice provided by a producer to an individual consumer ~~that was intended to result or does results into a~~ to purchase, an exchange or a replacement of an annuity in accordance with that advice.*

Working Group Request for Comments on the definition of “Recommendation”

Whether the Draft Should Address In-force Sales.

The Joint Trades strongly urge the Working Group not to modify the definition of “Recommendation” or make any other modification to the Model Regulation to extend its requirements to in-force annuity transactions or transactions beyond the purchase, exchange or replacement of an annuity. We are concerned that doing so will have a detrimental impact on consumers and could negatively impact access to affordable products and information about annuities.

First, owners of annuities can act on contractual provisions without a recommendation and it is likely to be difficult, if not impossible, for an insurer to prohibit a consumer from exercising a contractual right. Recommendations could have been made many years previously at the time of sale of the contract, such as, a recommendation to consider adding a rider at year 6 of the contract to generate income; making additional purchase payments; re-allocating investment allocations under variable annuity contracts and certain fixed index annuity contracts; withdrawing cash value from an annuity contract; adding, replacing or terminating riders under an annuity contract; and modifying beneficiaries. The client is then free to take future action on his/her own without meeting with a

² In the renumbered document, it is Section 5(M).

producer again. Additionally, there are instances where a customer has provided prior express authorization for certain types of transactions and many transactions are implemented directly by the consumer online or through the mail, as permitted by the consumer's contract, with no producer or insurer involvement.

Customers that we serve could very likely react disapprovingly if a producer or insurer performs a best interest review, when the customer is simply contacting the insurer or producer in an effort to exercise a contractual right. We are unaware of any reports or allegations of consumer harm arising out of recommendations of in-force transactions that could not be effectively regulated under existing rules.

Second, logistically, it is difficult to determine whether a recommendation was made to an existing client for an in-force contract at the producer level (because insurers often are not involved in those conversations with clients) or to differentiate between in-force transactions that are or are not subject to the requirements of the Model Regulation. This could delay processing a request and possibly harm the client. Such a delay could also jeopardize compliance with certain legal requirements, such as same day pricing rules under the federal securities laws. We do not believe it is reasonable to expect insurers to investigate every customer-initiated in-force transaction to determine if a recommendation was made. Additionally, most annuity contracts would not permit the insurer to reject or delay a requested transaction while it attempts to determine whether the transaction was recommended.

Third, extension to in-force transactions would necessitate fundamental structural modifications to the Model Regulation and would create significant operational challenges.

It is unlikely that the insurer could obtain all the necessary documentation, including the consumer profile information, from the producer to fulfill its supervisory duties under Section 6.(C). After its supervisory review, if the insurer determines that the transaction does not effectively address the consumer's financial situation, insurance needs, and financial objectives, it will be difficult for the insurer to determine how to properly unwind the transaction, particularly if the consumer was exercising existing contractual rights.

Last, application of the Model Regulation to in-force transactions would undercut the fundamental concept set forth in Section 6.A.(1)(i) that the Model Regulation does not create an "ongoing monitoring obligation."

For these reasons, we respectfully recommend that the Working Group refrain from expanding the scope to in-force transactions.³

³ However, if the Working Group ultimately concludes to extend the Model Regulation to in-force annuity transactions, we strongly urge the Working Group to conduct a detailed review of the 9/17/2019 Draft to map out the obligations on insurers and producers if the Model Regulation were to apply to different types of post-issuance recommendations. We strongly believe a different standard of conduct should be applied to in-force transactions than the best interest standard laid out in the Model Regulation applicable to new sales transactions.

Whether to Include a Timeframe for Review of a Consumer's "Consumer profile information"

We urge against inclusion of a required timeframe for review of a consumer's "Consumer profile information." The producer already is required to request consumer profile information in connection with a recommendation and to have a reasonable basis to believe the recommended annuity would effectively address the consumer's financial situation, insurance needs, and financial objectives in light of the consumer's consumer profile information.

We note that the impetus for the Working Group to explore the possibility of a requirement for the periodic review of the profile information appeared to be federal securities law requirements applicable to broker-dealers. Under SEC Rule 17a-3(a)(17) of the Securities Exchange Act of 1934, there is a requirement to "furnish" the broker-dealer customer, no less than every 36 months, the customer's account record information that is on file. The furnishing requirement does not, however, apply if there have been no recommendations related to the account during the preceding 36 months.

For these reasons, we recommend that the Model Regulation not include an additional provision specifying a time frame for a producer's review of the consumer profile information.

Section 6. Duties of Insurers and Producers

Our members broadly support the intent and construction in Section 6. We appreciate the effort that the Working Group made in crafting this section. We offer a few suggestions.

We have recommended the addition of a phrase to the last sentence of Section 6(A) so the sentence reads: *A producer is deemed to comply with this subsection by satisfying the following obligations regarding care, disclosure, conflict of interest and documentation, independent of the performance of the recommended annuity:*

Section 6.A. (1) Care Obligation

We have made four suggestions for modifications to Section 6(A)(1).

- The suggested change to Section 6(A)(1)(a)(ii) is a technical correction to clarify the language.
- The suggested changes to Section 6(A)(1)(a)(iii) have two purposes. We have suggested deleting, "over the life of the contract" as we are concerned that that could be interpreted as requiring an on-going duty. We have added "provided to the producer" to make clear that producers can only evaluate the information they actually receive from consumers.
- The suggested change in Section 6(A)(1)(j)(ii) is to delete the word, "substantially." Use of that word is inconsistent with the standard in Sections 6(A)(1)(iii) ("recommended option effectively addresses") and Section 6(A)(f) ("the consumer would benefit"). We also believe

Further, we recommend that the extension be limited to situations where: (i) the consumer exercises a contractual right under an existing annuity contract at the recommendation of the producer; and (ii) the producer receives new sales compensation, that is separate and distinct from compensation provided to a producer when, after, the initial premium or deposit under an annuity, the consumer pays further premiums or deposits pursuant to the annuity.

that word to be too subjective. We further note that replacement transactions would also continue to be subject to the existing requirements under the NAIC Life Insurance and Annuities Replacement Model Regulation.

- The suggested change in Section 6.A.(1)(j)(iii) is to bring the time frame closer in line to the current replacement requirements in most states.

In addition to these suggested changes, our members have asked what information the regulatory community is expecting the producer to share or gather with the use of the phrase, “characteristics of the insurer” in Section 6(A)(1)(e). We believe that producers can consider, for example, factors such as reputation, service record and financial strength.

Section 6.A.(2) Disclosure Obligation

We have suggested adding a new paragraph (v) to Section 6.A.(2)(a) that requires the disclosure of any material conflict of interest, in alignment with Reg BI. We have suggested a conforming change be made to Appendix A.

We have also suggested several additional technical, clarifying changes to Section 6.A.(2) and (3).

Working Group Request for Comments – “Materially Participated”

The Joint Trades are concerned that the proposed language rendering the Model Regulation applicable to any producer who “materially participated” in the transaction is too vague, and will create too much uncertainty in the marketplace as to when a producer is considered to have “materially participated” in a transaction and thus is subject to the Model Regulation. The articulated purpose for the provision was to ensure that more senior producers were not shielding themselves from responsibility by using junior producers to technically make a recommendation. The Joint Trades believe that a state insurance regulatory authority will always have jurisdiction over, and ample tools to sanction, a senior producer in those circumstances without needing to rely on this provision. The Joint Trades urge that this language not be included in the Model Regulation.

Section 6.B. – Transactions not based on a recommendation

We have suggested reverting to the language in Section 6.B.(1) to the language in the current version of the Model Regulation. We are concerned that the proposed changes to this subsection would inadvertently deprive insurers of the relief intended to be granted by this provision under the specified circumstances even if a producer is involved.⁴

Section 6.C. Supervision system

We have proposed modifying deleting Section 6.C.(1) entirely as the substance of that paragraph is covered in following paragraph and subparagraphs.

⁴ The definition of “producer” includes an insurer only “where no producer is involved.”

We have modified Section 6. C.(2). Many producers are appointed with multiple insurers. An insurer does not have the requisite knowledge or control over a producer to gauge the producer's compliance with the requirements of subsection A and the other specified subsections in connection with other insurers' products.

In addition, consistent with our modification to Section 1.A., we added a sentence to the end of Section 6.C.(2)(e) to make it clear the insurer is not required to warrant the producer is acting in the consumer's best interest.

Finally, we also have proposed modifying Section 6.C.(2)(e) to more precisely reference the standard we believe insurers' supervision system can and should be expected to satisfy. Specifically, we have modified subparagraph (e) to read:

The insurer shall establish and maintain reasonable procedures to detect recommendations ~~that~~ where there is not a reasonable basis to determine the recommendation would effectively address the particular consumer's financial situation, insurance needs and financial objectives are not in compliance with subsections A, B, D and E. This may include, but is not limited to, confirmation of the consumer's consumer profile information, systematic customer surveys, interviews, confirmation letters and programs of internal monitoring. Nothing in this subparagraph prevents an insurer from complying with this subparagraph by applying sampling procedures, or by confirming the consumer profile information after issuance or delivery of the annuity. An insurer is not required to warrant the producer is acting in the consumer's best interest;

We urge that subparagraph (f) be deleted. When a producer is engaged in activities relating to the sale of other insurers' products, an insurer does not have the requisite knowledge or control over the producer to gauge compliance with the disclosure requirements of Section 6.A.(2). Moreover, Section 8, as proposed to be modified below, provides that an insurer is responsible for compliance with the disclosure and other requirements of the Model Regulation by producers who sell the insurer's products.

We have suggested changes to subparagraph (h). Our purpose is to:

- (i) Make it applicable to sales contests etc. based on the sales of specific annuities of the insurer. We eliminated the reference to "specific types of annuities" as that may be overly broad as applied in the context of annuities. We clarified the section only applies to the insurer as the insurer does not have control over the business of third party entities; and
- (ii) In line with SEC Reg BI, clarify the requirements of this section (a) do not apply to compensation practices based on total annuity products sold; (b) would not prevent the offering of proprietary products, placing material limitations on the menu of products or incentivizing the sale of such products through its compensation practices, so long as the incentive is not based on the sale of a specific annuity product of the insurer within a limited period of time; and (c) are not intended to prohibit the receipt of employee benefits by employees.

As modified, subparagraph (h) reads: The insurer shall establish and maintain reasonable procedures to identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation provided by the insurer that are based on the sales of specific annuities or specific types of annuities within a limited period of time; and the requirements of this subsection: (i) do not apply to compensation practices based on total annuity products sold; (ii) would not prevent the offering of only proprietary products, placing material limitations on the menu of products or incentivizing the sale of such products through its compensation practices, so long as the incentive is not based on the sale of a specific annuity product of the insurer within a limited period of time; and (iii) are not intended to prohibit the receipt of health insurance, office rent, office support, retirement benefits or employee benefits by employees (including, but not limited to statutory employees).

Section 7. Producer Training

We added a new subparagraph to account for producers who have had required training before the effective date of the amended Model Regulation.

As modified, the paragraph reads: A producer who has completed an annuity training course approved by the department of insurance prior to [insert effective date of amended regulation] shall, within six (6) months after [insert effective date of amended regulation], complete either:

- (a) a new four (4) credit training course approved by the department of insurance after [insert effective date of amended regulation], or
- (b) an additional one-time one (1) credit training course approved by the department of insurance and provided by the department of insurance-approved education provider on appropriate sales practices, replacement and disclosure requirements under this amended regulation.

Section 8. – Compliance Mitigation: Penalties

We have proposed modifying Section 8.A. to clarify that insurers only are responsible for the action or inaction of our producers “in connection with the insurer’s annuity products” and not for activities relating to the sale of another insurer’s products over which the insurer has no control.

As modified: An insurer is responsible for compliance with this regulation by the insurer and the producer in connection with the insurer’s annuity products. If a violation occurs, either because of the action or inaction of the insurer or its producer, the commissioner may order:

Appendix A – Producer Relationship Disclosure Form

Our members generally support the creation of this document. As requested, we have offered some initial changes in our submitted redline. We do urge: 1) the elements of this disclosure be finalized after the content of the amended Model Regulation is finalized; 2) that regulators and interested

parties work with together to make the document more readable, approachable and meaningful for our customers; and 3) the Working Group to consider combining Appendix A and Appendix B.

The Joint Trades appreciate and thank the Working Group for its continued consideration of our concerns and would be glad to answer questions relating to any of the above. We worked diligently with our members to provide meaningful input within the deadline. We may have additional thoughts that we will share, as appropriate and as time permits.

Regards,

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DRAFT
Proposed Joint Trades Modifications
Rev 9/30/19

Draft: 9/17/19

Model #275

Comments are being requested on this draft. The revisions to this draft reflect changes made from the existing model. Comments should be sent only by email to Jolie Matthews at jmatthews@naic.org by Monday, Sept. 30, 2019.

**SUITABILITY IN ANNUITY TRANSACTIONS
MODEL REGULATION**

Table of Contents

Section 1.	Purpose
Section 2.	Scope
Section 3.	Authority
Section 4.	Exemptions
Section 5.	Definitions
Section 6.	Duties of Insurers and Producers
Section 7.	Producer Training
Section 8.	Compliance Mitigation; Penalties
Section 9.	Recordkeeping
Section 10.	Effective Date
Appendix A.	Producer Relationship Disclosure Form
Appendix B.	Consumer Refusal to Disclose All or Partial Consumer Profile Information

Section 1. Purpose

- A. The purpose of this regulation is to require producers to act in the best interest of the consumer when making a recommendation of an annuity and to require insurers to establish and maintain a system to supervise recommendations so that the insurance needs and financial objectives of consumers at the time of the transaction are effectively addressed. The best interest standard set forth in this regulation requires a producer to adhere to a standard of conduct but does not guarantee an outcome.
- B. Nothing herein shall be construed to create or imply a private cause of action for a violation of this regulation.

Drafting Note: The language of subsection B comes from the NAIC Unfair Trade Practices Act. If a State has adopted different language, it should be substituted for subsection B.

Drafting Note: Section 989J of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank Act”) specifically refers to this model regulation as the “Suitability in Annuity Transactions Model Regulation.” Section 989J of the Dodd-Frank Act confirmed this exemption of certain annuities from the Securities Act of 1933 and confirmed state regulatory authority. This regulation is a successor regulation that exceeds the requirements of the 2010 model regulation.

Section 2. Scope

This regulation shall apply to any sale or recommendation of an annuity.

Section 3. Authority

This regulation is issued under the authority of [insert reference to enabling legislation].

Drafting Note: States may wish to use the Unfair Trade Practices Act as enabling legislation or may pass a law with specific authority to adopt this regulation.

Section 4. Exemptions

Unless otherwise specifically included, this regulation shall not apply to transactions involving:

- A. ~~Direct response~~ solicitations, sales or purchases of annuities where there is no recommendation based on information collected from the consumer pursuant to this regulation;
- B. Contracts used to fund:
 - (1) An employee pension or welfare benefit plan that is covered by the Employee Retirement and Income Security Act (ERISA);
 - (2) A plan described by sections 401(a), 401(k), 403(b), 408(k) or 408(p) of the Internal Revenue Code (IRC), as amended, if established or maintained by an employer;
 - (3) A government or church plan defined in section 414 of the IRC, a government or church welfare benefit plan, or a deferred compensation plan of a state or local government or tax-exempt organization under section 457 of the IRC; or
 - (4) A nonqualified deferred compensation arrangement established or maintained by an employer or plan sponsor;
- C. Settlements of or assumptions of liabilities associated with personal injury litigation or any dispute or claim resolution process; or
- D. Formal prepaid funeral contracts.

Section 5. Definitions

- A. “Annuity” means an annuity that is an insurance product under State law that is individually solicited, whether the product is classified as an individual or group annuity.
- B. “Cash compensation” means any discount, concession, fee, service fee, commission, sales charge, loan, override, or cash benefit received by a producer in connection with the recommendation or sale of an annuity from an insurer, intermediary, or directly from the consumer.
- C. “Consumer profile information” means information that is reasonably appropriate to determine whether a recommendation addresses the consumer’s financial situation, insurance needs and financial objectives, including, at a minimum, the following:
 - (1) Age;
 - (2) Annual income;
 - (3) ~~Financial situation and needs, including debts and other obligations;~~
 - (4) Financial experience;
 - (5) ~~Financial objectives;~~
 - (6) Intended use of the annuity;
 - (7) Financial time horizon;
 - (8) Existing assets or financial products, including investment, annuity and insurance holdings;
 - (9) Liquidity needs;
 - (10) Liquid net worth;
 - (11) Risk tolerance, including willingness to accept non-guaranteed elements in the annuity, ~~including variability in premium, death benefit or fees;~~

- (12) Financial resources used to fund the annuity; and
- (13) Tax status.
- D. “Continuing education credit” or “CE credit” means one continuing education credit as defined in [insert reference in State law or regulations governing producer continuing education course approval].
- E. “Continuing education provider” or “CE provider” means an individual or entity that is approved to offer continuing education courses pursuant to [insert reference in State law or regulations governing producer continuing education course approval].
- F. “FINRA” means the Financial Industry Regulatory Authority or a succeeding agency.
- G. “Insurer” means a company required to be licensed under the laws of this state to provide insurance products, including annuities.
- H. “Intermediary” means an entity contracted directly with an insurer or with another entity contracted with an insurer to facilitate the sale of the insurer’s annuities by producers.
- I. (1) “Material conflict of interest” means a financial interest of the producer in the sale of an annuity that a reasonable person would expect to influence the impartiality of a recommendation.
- (2) “Material conflict of interest” does not include cash compensation or non-cash compensation. “Material conflict of interest” also does not include health insurance, office rent, office support, retirement benefits or employee benefits provided to employees (including, but not limited to, statutory employees).
- J. “Non-cash compensation” means any form of compensation that is not cash compensation, including, but not limited to, merchandise, gifts, prizes, travel expenses, meals, and lodging. “Non-cash compensation” does not include health insurance, office rent, office support, ~~and~~ retirement benefits or employee benefits provided to employees (including, but not limited to, statutory employees).
- K. “Non-guaranteed elements” means the premiums, credited interest rates (including any bonus), benefits, values, dividends, non-interest based credits, charges or elements of formulas used to determine any of these, that are subject to company discretion and are not guaranteed at issue. An element is considered non-guaranteed if any of the underlying non-guaranteed elements are used in its calculation.
- ~~K.L.~~ “Producer” means a person or entity required to be licensed under the laws of this state to sell, solicit or negotiate insurance, including annuities. For purposes of this regulation, “producer” includes an insurer where no producer is involved.
- M.L. (1) “Recommendation” means advice provided by a producer to an individual consumer ~~that was intended to result or does results in to~~ a purchase, ~~an~~ exchange or ~~a~~ replacement of an annuity in accordance with that advice.
- (2) Recommendation does not include general communication to the public, generalized customer services assistance or administrative support, general educational information and tools, prospectuses, or other product and sales material or information.

~~NOTE: THE WORKING GROUP IS REQUESTING COMMENTS ON REVISING THE DEFINITION OF “RECOMMENDATION” TO ADDRESS IN FORCE SALES BY ADDING LANGUAGE EXPANDING THE DEFINITION TO INCLUDE WHEN A MODIFICATION IS MADE OR THE CONSUMER ELECTS A CONTRACTUAL OPTION, WHICH GENERATES CASH OR NON-CASH COMPENSATION FOR THE PRODUCER PROVIDING THE ADVICE. THE WORKING GROUP ALSO REQUESTS COMMENTS ON WHETHER TO INCLUDE A TIME FRAME FOR A PRODUCER TO REVIEW A CONSUMER’S CONSUMER PROFILE INFORMATION. CURRENTLY FINRA REQUIRES A REVIEW OF SUCH INFORMATION AT LEAST EVERY 3 YEARS. THE WORKING GROUP IS ALSO REQUESTING COMMENTS ON WHETHER THE DRAFT SHOULD ADDRESS IN FORCE SALES.~~

~~MN.~~ “Replacement” means a transaction in which a new annuity is to be purchased, and it is known or should be known to the proposing producer, or to the proposing insurer whether or not a producer is involved, that by reason of the transaction, an existing annuity or other insurance policy ~~or contract~~ has been or is to be any of the following:

- (1) Lapsed, forfeited, surrendered or partially surrendered, assigned to the replacing insurer or otherwise terminated;
- (2) Converted to reduced paid-up insurance, continued as extended term insurance, or otherwise reduced in value by the use of nonforfeiture benefits or other policy values;
- (3) Amended so as to effect either a reduction in benefits or in the term for which coverage would otherwise remain in force or for which benefits would be paid;
- (4) Reissued with any reduction in cash value; or
- (5) Used in a financed purchase.

Drafting Note: The definition of “replacement” above is derived from the NAIC Life Insurance and Annuities Replacement Model Regulation. If a State has a different definition for “replacement,” the State should either insert the text of that definition in place of the definition above or modify the definition above to provide a cross-reference to the definition of “replacement” that is in State law or regulation.

N. “SEC” means the United States Securities and Exchange Commission.

Section 6. Duties of Insurers and Producers

A. **Best Interest Obligations.** A producer, when making a recommendation of an annuity, shall act in the best interest of the consumer under the circumstances known at the time the recommendation is made, without placing the producer’s or the insurer’s financial interest ahead of the consumer’s interest. A producer is deemed to comply with this subsection by satisfying the following obligations regarding care, disclosure, conflict of interest and documentation, independent of the performance of the recommended annuity:

- (1) (a) **Care Obligation.** The producer, in making a recommendation shall exercise reasonable diligence, care and skill to:
 - (i) Know the consumer’s financial situation, insurance needs and financial objectives;
 - (ii) Understand the products the producer is authorized and licensed to recommend or sell~~available recommendation options after making a reasonable inquiry into options available to the producer~~;
 - (iii) Have a reasonable basis to believe the recommended option effectively addresses the consumer’s financial situation, insurance needs and financial objectives~~over the life of the product~~, as evaluated in light of the consumer profile information provided to the producer; and
 - (iv) Communicate the basis or bases of the recommendation.
- (b) The requirements under subparagraph (a) of this paragraph include making reasonable efforts to obtain consumer profile information from the consumer prior to the recommendation of an annuity.
- (c) The requirements under subparagraph (a) of this paragraph require a producer to consider the types of products the producer is authorized and licensed to recommend or sell that address the consumer’s financial situation, insurance needs and financial objectives. This

does not require analysis or consideration of any products outside the authority and license of the producer or other possible alternative products or strategies available in the market at the time of the recommendation.

- (d) The requirements under this subsection do not create a fiduciary obligation but create a regulatory obligation as established in this regulation.
 - (e) The consumer profile information, characteristics of the insurer, and product costs, rates, benefits and features are those factors generally relevant in making a determination whether an annuity effectively addresses the consumer's financial situation, insurance needs and financial objectives, but the level of importance of each factor under the care obligation of this paragraph may vary depending on the facts and circumstances of a particular case. However, each factor may not be considered in isolation.
 - (f) The requirements under subparagraph (a) of this paragraph include having a reasonable basis to believe the consumer would benefit from certain features of the annuity, such as annuitization, death or living benefit or other insurance-related features.
 - (g) The requirements under subparagraph (a) of this paragraph apply to the particular annuity as a whole and the underlying subaccounts to which funds are allocated at the time of purchase or exchange of an annuity, and riders and similar producer enhancements, if any.
 - (h) The requirements under subparagraph (a) of this paragraph do not mean the annuity with the lowest one-time or multiple occurrence compensation structure shall necessarily be recommended.
 - (i) The requirements under subparagraph (a) of this paragraph do not mean the producer has ongoing monitoring obligations under the care obligation under this paragraph, although such an obligation may be separately owed under the terms of a fiduciary, consulting, investment advising or financial planning agreement between the consumer and the producer.
 - (j) In the case of an exchange or replacement of an annuity, the producer shall consider the whole transaction, which includes taking into consideration whether:
 - (i) The consumer will incur a surrender charge, be subject to the commencement of a new surrender period, lose existing benefits, such as death, living or other contractual benefits, or be subject to increased fees, investment advisory fees or charges for riders and similar product enhancements;
 - (ii) The replacing product would ~~substantially~~ benefit the consumer in comparison to the replaced product over the life of the product; and
 - (iii) The consumer has had another annuity exchange or replacement and, in particular, an exchange or replacement within the preceding ~~60~~36 months.
- (2) Disclosure obligation.
- (a) Prior to or at the time of the recommendation or sale of an annuity, the producer shall prominently disclose to the consumer on a form substantially similar to the "Producer Relationship Disclosure Form" in Appendix A:
 - (i) A description of the scope and terms of the relationship with the consumer and the role of the producer in the transaction;
 - (ii) Any limitations the producer or the insurer has concerning the following:
 - (I) The type of products that the producer is authorized and licensed to recommend or sell; and

- (II) Whether only products issued by a specific insurer or an otherwise limited range of annuity products may be offered;
- (iii) A description of the sources and types of cash compensation and non-cash compensation to be received by the producer ~~including whether the producer is to be compensated~~ for the sale of ~~the~~ recommended annuity including whether the producer is to be compensated (A) by commission as part of premium or other remuneration received from the insurer, intermediary or other producer, ~~or (B) or~~ by fee as a result of a contract for advice or consulting services; ~~and~~
- (iv) A notice of the consumer's right to request additional information regarding cash compensation described in subparagraph (b) of this paragraph; and
- (v) Any material conflict of interest.

Drafting Note: If a state approves forms, a state should add language to subparagraph (a) reflecting such approvals.

- (b) Upon request of the consumer, the producer shall disclose:
 - (i) A reasonable estimate of the amount of cash compensation to be received by the producer, which may be stated as a range of amounts or percentages, provided, however, that producers who are employees of an insurer and are not directly compensated for the sale of particular annuity products, shall only be required to provide a description of general compensation practices relevant to the producer; and
 - (ii) Whether the cash compensation is a one-time or multiple occurrence amount, and if a multiple occurrence amount, the frequency and amount of the occurrence, which may be stated as a range of amounts or percentages; and
- (c) Prior to or at the time of the recommendation or sale of an annuity, the producer shall have a reasonable basis to believe the consumer has been informed of various features of the annuity, such as the potential surrender period and surrender charge, potential tax penalty if the consumer sells, exchanges, surrenders or annuitizes the annuity, mortality and expense fees, investment advisory fees, any annual fees, potential charges for and features of riders or other options of the annuity, limitations on interest returns, potential changes in non-guaranteed elements of the annuity, insurance and investment components and market risk.

Drafting Note: If a State has adopted the NAIC Annuity Disclosure Model Regulation, the State should insert an additional phrase in subparagraph (c) above to explain that the requirements of this section are intended to supplement and not replace the disclosure requirements of the NAIC Annuity Disclosure Model Regulation.

- (3) Conflict of interest obligation. A producer shall identify and avoid or otherwise reasonably manage material conflicts of interest, including material conflicts of interest related to a ~~material~~ ownership interest the producer has in an insurer whose annuities the producer is licensed and authorized to recommend or sell.
- (4) Documentation obligation. A producer shall at the time of recommendation or sale:

- (a) Make a written record of any recommendation and the basis for the recommendation subject to this regulation;
- (b) ~~If applicable, obtain~~ Obtain a ~~customer-consumer~~ signed statement on a form substantially similar to the “Consumer Refusal to Disclose All or Partial Consumer Profile Information” form in Appendix B documenting:
 - (i) A customer’s refusal to provide the consumer profile information, if any; and
 - (ii) A customer’s understanding of the ramifications of not providing his or her consumer profile information or providing insufficient consumer profile information; and
- (c) ~~If applicable, obtain~~ Obtain a ~~customer-consumer~~ signed statement acknowledging the annuity transaction is not recommended if a customer decides to enter into an annuity transaction that is not based on the producer’s recommendation.

Drafting Note: If a state approves forms, a state should add language to subparagraph (b) of this paragraph reflecting such approvals.

~~**NOTE: THE PROVISION BELOW IS STILL UNDER CONSIDERATION. THE WORKING GROUP IS REQUESTING COMMENT ON IT.**~~

~~[?]. Any requirement applicable to a producer under this section shall apply to every producer who has materially participated in the making of a recommendation and received compensation as a result of the sales transaction, regardless of whether the producer has had any direct contact with the consumer, provided that product wholesaling or product support based on generic client information, or the provision of education or marketing material, does not constitute participating in the making of a recommendation.]~~

B. Transactions not based on a recommendation.

- (1) Except as provided under paragraph (2), ~~neither~~ a producer ~~nor an insurer~~ shall have ~~no~~ any obligation to a consumer under subsection A(1) related to any annuity transaction if:
 - (a) No recommendation is made;
 - (b) A recommendation was made and was later found to have been prepared based on materially inaccurate information provided by the consumer;
 - (c) A consumer refuses to provide relevant consumer profile information and the annuity transaction is not recommended; or
 - (d) A consumer decides to enter into an annuity transaction that is not based on a recommendation of the producer.
- (2) An insurer’s issuance of an annuity subject to paragraph (1) shall be reasonable under all the circumstances actually known to the insurer at the time the annuity is issued.

C. Supervision system.

- ~~(1) Except as permitted under subsection B, an insurer may not issue an annuity recommended to a consumer unless there is a reasonable basis to believe the annuity would effectively address the particular consumer’s financial situation, insurance needs and financial objectives based on the consumer’s consumer profile information.~~

(21) An insurer shall establish and maintain a supervision system that is reasonably designed to achieve the insurer's and its producers' compliance with this regulation in connection with the insurer's annuities, including, but not limited to, the following:

- (a) The insurer shall establish and maintain reasonable procedures to inform its producers of the requirements of this regulation and shall incorporate the requirements of this regulation into relevant producer training manuals;
- (b) The insurer shall establish and maintain standards for producer product training and shall establish and maintain reasonable procedures to require its producers to comply with the requirements of section 7 of this regulation;
- (c) The insurer shall provide product-specific training and training materials which explain all material features of its annuity products to its producers;
- (d) The insurer shall establish and maintain procedures for review of each recommendation prior to issuance of an annuity that are designed to ensure that there is a reasonable basis to determine that the recommended annuity would effectively address the particular consumer's financial situation, insurance needs and financial objectives. Such review procedures may apply a screening system for the purpose of identifying selected transactions for additional review and may be accomplished electronically or through other means including, but not limited to, physical review. Such an electronic or other system may be designed to require additional review only of those transactions identified for additional review by the selection criteria;
- (e) The insurer shall establish and maintain reasonable procedures to detect recommendations that where there is not a reasonable basis to determine the recommendation would effectively address the particular consumer's financial situation, insurance needs and financial objectives are not in compliance with subsections A, B, D and E. This may include, but is not limited to, confirmation of the consumer's consumer profile information, systematic customer surveys, interviews, confirmation letters and programs of internal monitoring. Nothing in this subparagraph prevents an insurer from complying with this subparagraph by applying sampling procedures, or by confirming the consumer profile information after issuance or delivery of the annuity. An insurer is not required to warrant the producer is acting in the consumer's best interest;

~~(f) The insurer shall establish and maintain reasonable procedures to assess, prior to or upon issuance or delivery of an annuity, whether a producer has provided to the consumer the information required to be provided under this section;~~

- ~~(f)~~ (g) The insurer shall establish and maintain reasonable procedures to identify and address potentially suspicious consumer refusals to provide consumer profile information;
- ~~(g)~~ (h) The insurer shall establish and maintain reasonable procedures to identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation provided by the insurer that are based on the sales of specific annuities or specific types of annuities within a limited period of time; and the requirements of this subsection: (i) do not apply to compensation practices based on total annuity products sold; (ii) would not prevent the offering of only proprietary products, placing material limitations on the menu of products or incentivizing the sale of such products through its compensation practices, so long as the incentive is not based on the sale of a specific annuity product of the insurer within a limited period of time; and (iii) are not intended to prohibit the receipt of health insurance, office rent, office support, retirement benefits or employee benefits by employees (including but not limited to statutory employees).
- (i) The insurer shall annually provide a written report to senior management, including to the senior manager responsible for audit functions, which details a review, with appropriate

testing, reasonably designed to determine the effectiveness of the supervision system, the exceptions found, and corrective action taken or recommended, if any.

- (3) (a) Nothing in this subsection restricts an insurer from contracting for performance of a function (including maintenance of procedures) required under this subsection. An insurer is responsible for taking appropriate corrective action and may be subject to sanctions and penalties pursuant to section 8 of this regulation regardless of whether the insurer contracts for performance of a function and regardless of the insurer's compliance with subparagraph (b) of this paragraph.
- (b) An insurer's supervision system under this subsection shall include supervision of contractual performance under this subsection. This includes, but is not limited to, the following:
 - (i) Monitoring and, as appropriate, conducting audits to assure that the contracted function is properly performed; and
 - (ii) Annually obtaining a certification from a senior manager who has responsibility for the contracted function that the manager has a reasonable basis to represent, and does represent, that the function is properly performed.
- (4) An insurer is not required to include in its system of supervision a producer's recommendations to consumers of products other than the annuities offered by the insurer.

D. Prohibited Practices. Neither a producer nor an insurer shall dissuade, or attempt to dissuade, a consumer from:

- (1) Truthfully responding to an insurer's request for confirmation of the consumer profile information;
- (2) Filing a complaint; or
- (3) Cooperating with the investigation of a complaint.

E. Safe harbor.

- (1) Sales made in compliance with SEC regulations and applicable FINRA rules pertaining to best interest obligations and supervision of annuity transactions shall satisfy the requirements under this regulation. This subsection applies to FINRA broker-dealer sales of annuities if, in connection with the sale of an annuity, the broker-dealer and the producer, who also is appropriately registered as a representative with FINRA, have complied with the business rules, controls and procedures for securities transactions. However, nothing in this subsection shall limit the insurance commissioner's ability to investigate and enforce the provisions of this regulation.

Drafting Note: Non-compliance with SEC and FINRA requirements means that the broker-dealer transaction is subject to compliance with the requirements of this regulation.

- (2) For paragraph (1) to apply, an insurer shall:
 - (a) Monitor the FINRA member broker-dealer using information collected in the normal course of an insurer's business; and
 - (b) Provide to the FINRA member broker-dealer information and reports that are reasonably appropriate to assist the FINRA member broker-dealer to maintain its supervision system.

Section 7. Producer Training

- A. A producer shall not solicit the sale of an annuity product unless the producer has adequate knowledge of the product to recommend the annuity and the producer is in compliance with the insurer's standards for product training. A producer may rely on insurer-provided product-specific training standards and materials to comply with this subsection.
- B. (1) (a) A producer who engages in the sale of annuity products shall complete a one-time four (4) credit training course approved by the department of insurance and provided by the department of insurance-approved education provider.
- (b) Producers who hold a life insurance line of authority on the effective date of this regulation and who desire to sell annuities shall complete the requirements of this subsection within six (6) months after the effective date of this regulation. Individuals who obtain a life insurance line of authority on or after the effective date of this regulation may not engage in the sale of annuities until the annuity training course required under this subsection has been completed.
- (2) The minimum length of the training required under this subsection shall be sufficient to qualify for at least four (4) CE credits, but may be longer.
- (3) The training required under this subsection shall include information on the following topics:
- (a) The types of annuities and various classifications of annuities;
- (b) Identification of the parties to an annuity;
- (c) How product specific annuity contract features affect consumers;
- (d) The application of income taxation of qualified and non-qualified annuities;
- (e) The primary uses of annuities; and
- (f) Appropriate standard of conduct, sales practices, replacement and disclosure requirements.
- (4) Providers of courses intended to comply with this subsection shall cover all topics listed in the prescribed outline and shall not present any marketing information or provide training on sales techniques or provide specific information about a particular insurer's products. Additional topics may be offered in conjunction with and in addition to the required outline.
- (5) A provider of an annuity training course intended to comply with this subsection shall register as a CE provider in this State and comply with the rules and guidelines applicable to producer continuing education courses as set forth in [insert reference to State law or regulations governing producer continuing education course approval].
- ~~(6)~~ A producer who has completed an annuity training course approved by the department of insurance prior to [insert effective date of amended regulation] shall, within six (6) months after [insert effective date of amended regulation], complete either:
- ~~(a)~~ a new four (4) credit training course approved by the department of insurance after [insert effective date of amended regulation], or
- ~~(b)~~ an additional one-time one (1) credit training course approved by the department of insurance and provided by the department of insurance-approved education provider on appropriate sales practices, replacement and disclosure requirements under this amended regulation.
- ~~(6)~~ Annuity training courses may be conducted and completed by classroom or self-study methods in accordance with [insert reference to State law or regulations governing producer continuing education course approval].

- (78) Providers of annuity training shall comply with the reporting requirements and shall issue certificates of completion in accordance with [insert reference to State law or regulations governing to producer continuing education course approval].
- (89) The satisfaction of the training requirements of another State that are substantially similar to the provisions of this subsection shall be deemed to satisfy the training requirements of this subsection in this State.
- (910) The satisfaction of the components of the training requirements of any course or courses with components substantially similar to the provisions of this subsection shall be deemed to satisfy the training requirements of this subsection in this state.
- (101) An insurer shall verify that a producer has completed the annuity training course required under this subsection before allowing the producer to sell an annuity product for that insurer. An insurer may satisfy its responsibility under this subsection by obtaining certificates of completion of the training course or obtaining reports provided by commissioner-sponsored database systems or vendors or from a reasonably reliable commercial database vendor that has a reporting arrangement with approved insurance education providers.

Section 8. Compliance Mitigation; Penalties

- A. An insurer is responsible for compliance with this regulation by the insurer and the producer in connection with the insurer's annuity products. If a violation occurs, either because of the action or inaction of the insurer or its producer, the commissioner may order:
 - (1) An insurer to take reasonably appropriate corrective action for any consumer harmed by a failure to comply with this regulation by the insurer, an entity contracted to perform the insurer's supervisory duties or by the producer;
 - (2) A general agency, independent agency or the producer to take reasonably appropriate corrective action for any consumer harmed by the producer's violation of this regulation; and
 - (3) Appropriate penalties and sanctions.
- B. Any applicable penalty under [insert statutory citation] for a violation of this regulation may be reduced or eliminated [, according to a schedule adopted by the co_mmissioner,] if corrective action for the consumer was taken promptly after a violation was discovered or the violation was not part of a pattern or practice.

Drafting Note: Subsection B above is intended to be consistent with the commissioner's discretionary authority to determine the appropriate penalty for a violation of this regulation. The language of subsection B is not intended to require that a commissioner impose a penalty on an insurer for a single violation of this regulation if the commissioner has determined that such a penalty is not appropriate.

Drafting Note: A State that has authority to adopt a schedule of penalties may wish to include the words in brackets. In that case, "shall" should be substituted for "may" in the same sentence. States should consider inserting a reference to the NAIC Unfair Trade Practices Act or the State's statute that authorizes the commissioner to impose penalties and fines.

Section 9. Recordkeeping

- A. Insurers, general agents, independent agencies and producers shall maintain or be able to make available to the commissioner records of the information collected from the consumer, disclosures made to the consumer, including summaries of oral disclosures, and other information used in making the recommendations that were the basis for insurance transactions for [insert number] years after the insurance transaction is completed by the insurer. An insurer is permitted, but shall not be required, to maintain documentation on behalf of a producer.

Drafting Note: States should review their current record retention laws and specify a time period that is consistent with those laws. For some States this time period may be five (5) years.

- B. Records required to be maintained by this regulation may be maintained in paper, photographic, micro-process, magnetic, mechanical or electronic media or by any process that accurately reproduces the actual document.

Drafting Note: This section may be unnecessary in States that have a comprehensive recordkeeping law or regulation.

Section 10. Effective Date

The amendments to this regulation shall take effect months after the date the regulation is adopted or on [insert date], whichever is later.

APPENDIX A

PRODUCER RELATIONSHIP DISCLOSURE FORM
(For Use by an Individual Agent/Producer)

Date: _____

INSURANCE AGENT/PRODUCER INFORMATION (“Me”, “I”, “My”)

First Name: _____ Last Name: _____

Firm Name: _____ Website: _____

Business Mailing Address: _____

Business Telephone Number: _____

Email Address: _____

Insurance License # _____

CLIENT INFORMATION (“You”, “Your”)

First Name: _____ Last Name: _____

~~INSURANCE AUTHORIZATION~~ Products Available

I am licensed and authorized to sell the following insurance products, ~~including annuities in [State] in accordance with state laws. I offer the following products:~~

- | | |
|---|---|
| <input type="checkbox"/> Fixed or Fixed Index Annuities | <input type="checkbox"/> Mutual Funds |
| <input type="checkbox"/> Variable Annuities | <input type="checkbox"/> Stocks/Bonds |
| <input type="checkbox"/> Options | <input type="checkbox"/> Certificates of Deposits |
| <input type="checkbox"/> Other Investments _____ | |
| <input type="checkbox"/> <u>Life Insurance</u> | |

I am authorized and contracted or appointed or have access to offer:

- | | |
|---|--|
| <input type="checkbox"/> Products from ONLY ONE INSURER or Insurance Holding Company Group | <input type="checkbox"/> Products from Multiple Insurers |
|---|--|

Products from Multiple Insurers although I am primarily contracted with one insurer

NOTE: THE WORKING GROUP REQUESTS COMMENTS ON WHAT ADDITIONAL INFORMATION (OR BOXES), IF ANY, SHOULD BE ADDED BELOW TO REFLECT THE PROVISIONS OF SECTION 6A(2), THE DISCLOSURE OBLIGATION, TO DESCRIBE THE SCOPE AND TERMS OF THE RELATIONSHIP BETWEEN THE PRODUCER AND THE CONSUMER.

My Relationship with You:

- One-Time Transaction
- On-Going Relationship

My Compensation Structure:

- Commissioned ~~Transaction~~
- An asset under management fee
- Other, please describe: _____

As a result of this transaction, I am likely to be compensated by the following sources for this relationship:

- Insurance Company
- ~~The Consumer~~ You
- Third parties such as an Independent Marketing Organization (IMO) related to the Insurer

- Other Sources _____

[Material Conflicts of Interest]

ADDITIONAL INFORMATION

You may obtain further information regarding the cash compensation paid to me.

NOTE: THE WORKING GROUP REQUESTS COMMENTS ON WHETHER THE CONSUMER SHOULD SIGN AND ACKNOWLEDGE THIS FORM AND/OR SHOULD THIS FORM BE RETAINED BY THE PRODUCER OR GIVEN TO THE CONSUMER, OR BOTH.

I acknowledge that the basis for the recommendation was communicated to me.

Client Signature

Date

APPENDIX B

CONSUMER REFUSAL TO DISCLOSE ALL OR PARTIAL CONSUMER PROFILE INFORMATION FORM
(For Use if Applicable)

I understand that should I decline to provide all or some of the requested information, ~~provide or should I provide~~ inaccurate information, or proceed with a transaction that is not based on a recommendation of the producer or the insurer. I am limiting the protection afforded me by the Insurance Code of this [state] regarding this purchase. I acknowledge the following:

- I **REFUSE** to provide this information at this time.
- I have chosen to provide LIMITED information at this time.
- My annuity purchase IS NOT BASED on the recommendation of this producer or the insurer.

Client Signature

Date

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