

## Center for Economic Justice Independent Insurance Agents & Brokers of America

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Market Conduct Examination Guidelines Working Group  
National Association of Insurance Commissioners  
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*Delivered via email to Petra Wallace at [pwallace@naic.org](mailto:pwallace@naic.org)*

Dear Chairman Hughes:

On behalf of the Center for Economic Justice (CEJ) and the Independent Insurance Agents & Brokers of America (IIABA), we write to comment on the proposed revisions to Chapter 23 of the *Market Regulation Handbook* (Conducting the Life and Annuity Examination). Our comments are intended to highlight our concerns with the new text in Standard 9 regarding compliance with comparable standards – referencing the recommendations or sales pursuant to the safe harbor provision contained in the Suitability in Annuity Transactions Model Regulation.

Our organizations are concerned because the proposed revisions to this standard suggest an expansive interpretation that is inconsistent with the plain text of the model and because there is no guidance for an examiner regarding when the comparable standard can be relied upon or how to interact with or enforce that comparable standard. The proposed language would permit certain marketplace actors to opt for a different regulatory framework than that contained in the model, exacerbate concerns related to the creation of an unlevel playing field among competitors, and represent a move toward optional federal regulation and away from the concept of functional regulation that the NAIC has historically embraced.

Embracing such an interpretation would also create a myriad of practical problems from a market regulation perspective and create troubling regulatory gaps and ambiguities. Instead of regulatory coordination across different products, different sellers and different regulatory agencies, the proposed examiner guidance would create regulatory silos, gaps and lack of coordination.

One notable problem with the standard as proposed is that it broadly suggests that licensees can opt out of their obligations under the model regulation and evade its requirements by complying with the Securities and Exchange Commission's Regulation Best Interest. The safe harbor provision, however, is more nuanced and can only be relied upon in certain instances. Perhaps most notably, the safe harbor provision does not apply and is not available to broker-dealers and registered representatives who recommend or sell annuities that are not securities (e.g. annuities). Some of the reasons why this is the case are outlined below:

- A producer can only take advantage of the safe harbor provision if the recommendation or sale is "made in compliance with comparable standards" (see

Section 6(E)(1)), but there is no comparable standard that exists when a broker-dealer or registered representative recommends or sells an annuity that is not a security. The relevant definition of “comparable standard” found in Section 6(E)(5)(a) provides that broker-dealers and registered representatives may only rely on the safe harbor and avoid the model’s requirements when they comply with “applicable SEC and FINRA rules pertaining to best interest obligations and supervision of annuity recommendations and sales.”

- This text makes clear that the safe harbor, for purposes of broker-dealers and registered representatives only<sup>1</sup>, is limited to instances when a SEC or FINRA rule applies to a particular annuity recommendation (i.e. when the annuity at issue is a security). Since there are no SEC or FINRA rules that are applicable to or that pertain when an annuity is not a security, the safe harbor cannot apply and is not available to broker-dealers and registered representatives in these narrow instances.
- The safe harbor provision also requires any person seeking to rely on the safe harbor to actually comply with the comparable standard in question, and this is simply unachievable for a broker-dealer or registered representative recommending or selling an annuity that is not a security. It is impossible for a person recommending an annuity that is not a security to somehow comply with rules, such as Regulation Best Interest, that are specific to and limited to securities. Regulation Best Interest is tailored to securities transactions, and it applies to those “making a recommendation of any securities transaction or investment strategy involving securities” and to customers “receiv[ing] a recommendation of any securities transaction or investment strategy involving.” It does not apply to insurance or to annuities that are not securities, and a person not selling a security cannot comply with it.
- In the broker-dealer and registered representative context, the model requires any financial professional seeking to take advantage of the safe harbor to comply with federal securities rules that apply to the particular annuity product in question. The reality is that (1) there are no applicable federal securities rules that apply to transactions involving annuities that are not securities and (2) a person recommending or selling an annuity that is not a security cannot conceivably comply with such securities rules. This means broker-dealers and registered representatives cannot satisfy the conditions of the safe harbor when offering annuities that are not securities and must therefore comply with the model regulation.

Some observers may note that Section 6(E)(1) indicates that the safe harbor is available to financial professionals “that satisfy a comparable standard even if such a standard would not otherwise apply to the product or recommendation at issue.” This text, however, does not help those arguing for an expansive interpretation of the manner in which the safe harbor applies to broker-dealers and registered representatives. This paragraph makes clear that compliance with a comparable standard is necessary, and, as noted above, there is no comparable standard for broker-dealers or registered representatives who recommend or sell annuities that are not securities.

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<sup>1</sup> The safe harbor subsection of the model regulation addresses three categories of financial intermediaries – (1) broker-dealers and registered representatives, (2) investment advisors, and (3) plan fiduciaries or fiduciaries. Notably, the provisions related to broker-dealers and registered representatives are the only one of the three to limit the application of the safe harbor in a manner that requires any purported comparable federal standard and regulatory framework to actually apply to the annuity being recommended or sold.

In short, the model regulation in its current form clearly applies to all recommendations and sales of annuities that are not securities by broker-dealers and registered representatives. For this reason and because of the adverse consequences that would result from the adoption of an alternative interpretation, we urge you not to adopt a market conduct standard that is inconsistent with the model regulation's text.

Adopting a market conduct standard that defies the plain text of the underlying model regulation in transactions in which broker-dealers and registered representatives recommend annuities that are not securities would also create a host of practical problems. Such an outcome is not only bad and unwarranted public policy, but it presents the following and many other unanswered questions:

- How does a securities-specific and securities-only regulation conceivably apply to a transaction involving a product that is not a security?
- Securities regulators will have no jurisdiction over a transaction in which an annuity that is not a security is sold, so who determines if compliance with this securities framework is satisfied? Are insurance regulators qualified to interpret a securities-specific regulation? What happens if there are disagreements about compliance? Are insurance regulators obligated to defer to views of their securities counterparts? Can insurance regulators take enforcement action for noncompliance with a securities-specific standard if securities officials have not taken action themselves (an especially relevant question since securities regulators will not have jurisdiction over such transactions)?
- Are licensees who sell fixed annuities and claim to comply with Regulation Best Interest able to avoid compliance with all elements of the model regulation, including the disclosure obligations that require the use of an insurance-specific notice and the robust documentation requirement?
- The proposed standard states that nothing in the safe harbor provision limits the ability of insurance regulators to enforce the requirements of the model and investigate suspected violations, but how can that occur in practical terms?

The proposed revisions to this standard start with a reference to the safe harbor section of the model regulation and list comparable standards. However, this first paragraph does not explain or identify what products sold by what types of entities can rely upon which comparable standards. As noted above, the second paragraph of the proposed revision suggests a massively expansive interpretation of the safe harbor provisions without any meaningful guidance to examiners for how to determine if a comparable standard applies and, if so, how to determine if the requirements of that comparable standard have been met. As written, it appears the only activity for an examiner is to ask if the producer or insurer is relying on a comparable standard and if the response is yes, then the examiner's inquiry is finished. The last paragraph of the proposed revisions offers no help:

*Review the insurer's system of monitoring sales made in compliance with comparable standards and applicable state annuity suitability statutes, rules and regulations. An insurer may demonstrate compliance in this area by:*

- *Monitoring the relevant conduct of the financial professional seeking to rely on the safe harbor or the entity responsible for supervising the financial professional using information collected in the normal course of an insurer's business; and*
- *Providing to the entity responsible for supervising the financial professional seeking to rely on the safe harbor information and reports that are reasonably appropriate to assist such entity to maintain its supervision system.*

The review procedures relate to an insurer's supervisory responsibility of a producer not to whether a comparable standard applies or how to examine compliance with that comparable standard. Further, the proposed guidance for insurers is limited to procedural activities and not substantive outcomes. The model regulation requires an insurer not to issue an annuity unless there is a reasonable basis to believe the annuity would effectively address the particular consumer's needs (set out in Standard 16).

CEJ and IIABA thank you for the opportunity to submit these joint comments and for your consideration of our perspective regarding this important issue, and we again urge you not to adopt the revisions to Standard 9 as drafted. If we can provide you with any additional information or assistance in advance of your next meeting, please feel free to contact us.

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