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NAIC Life Insurance and Annuities (A) Committee
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***RE: Suitability in Annuity Transactions Model Regulation #275
Questions***

This letter is submitted by the principals of ten leading Independent Marketing Organizations (IMOs), which comprise approximately 40% of the fixed indexed annuity sales in the independent market. Our organizations have been consistently engaged in the development of an appropriate standard of care for annuity sales for the past several years. Both as individual companies and as members of trade associations, our organizations have actively participated in in-person meetings and submitted comment letters concerning the work of the NAIC Annuity Suitability (A) Working Group. We applaud the Working Group for asking specific questions as the specifics are what will ultimately make this Model Regulation a success or failure. We are foremost concerned with the specifics of *how* an independent insurance professional can comply. Vagueness and broad sweeping political language does not benefit any party—consumer or industry. The questions you have posed will also be the questions that an independent insurance professional will ask. We hope our responses will help the Working Group produce clear and concise answers.

Topic: Conflict of Interest

Question 1: What constitutes a material conflict of interest when recommending annuities?
Question 2: When a material conflict of interest exists, how should an insurer and/or a producer avoid or otherwise reasonably manage the conflict?

The NAIC's exposure draft dated May 30, 2019 defines a "material conflict of interest" as "a financial interest of the producer, or the insurer where no producer is involved, in the sale of an annuity that a reasonable person would expect to influence the impartiality of a recommendation." We believe this definition adequately captures the scope of what the NAIC Working Group is trying to accomplish.

Considering this definition, compensation should be addressed in the care and disclosure obligations of the model rule—not in the conflict of interest obligation. If an insurance professional complies with the care obligation, that producer would not recommend one product over another solely to earn a higher commission. Furthermore, if an insurance professional makes a compliant recommendation and complies with the disclosure obligations, any additional duties shall only serve to limit consumer choice of annuity products.

The SEC and other parties have suggested an extensive list of possible methods to manage, mitigate, or avoid conflicts of interests including: manipulation of incentives; implementing

supervisory procedures, adjusting compensation for those who fail to adequately manage conflicts, and limiting the types of customers that can receive a certain product.

However, those suggestions do not fit the structure of independent annuity distribution. An independent insurance professional may work with many different insurance carriers and independent marketing organizations to carry a wide assortment of product offerings. The independent professional does not control insurer compensation policy. Requiring an independent professional to perform any “institutional” action, as listed above, would result in confusion and uncertainty. Ultimately, such institutional actions are not necessary. As long as the care obligation is met and there is adequate disclosure, management or mitigation of compensation will not have any bearing on the recommendation.

In practical application, certain elements of the regulation that go beyond the care obligation limit what products are available to the consumer. While we understand the need to include many of these conditions, if the care obligation is satisfied, it affords protection to the consumer that the recommendation is in their best interest. This regulation is meant to protect the consumer, something that we are passionate about, and therefore we need to be careful to not overburden the system with a regulation that would do the opposite.

Furthermore, the specific contents of any required disclosure should be aligned with the SEC. While it is important to have alignment with the SEC to ensure the burden of compliance can be met by all in a reasonable manner, it does not make sense for less risky products such as fixed annuities as compared to variable annuities and securities, to have more stringent standards.

Topic: Care Obligation

Question 1: Should the care obligation of a producer include “prudence”?

The word “prudence” should be removed from the draft for two reasons. The first is that the intent behind the language is already covered by “diligence, care, and skill” and is therefore redundant. Second, the word prudence creates a legal uncertainty that could result in unintended consequences.

Including prudence in the draft is unnecessary. The intent of this draft is to protect the customer while still allowing the industry to operate effectively. Including prudence does nothing to further either of those goals. Black’s Law Dictionary defines prudence as “acting circumspect or judicious in one’s dealings; cautious.” There is not any behavior that would fall under this definition of prudence that is not already protected against under the language “diligence, care, and skill.” For that reason, its inclusion is redundant.

As to the second point, the legal ramifications of including prudence are potentially severe. It has been made clear that this group does not want to impose a fiduciary standard, however including prudence in the draft opens up the possibility of creating an unintended fiduciary obligation. This obligation stems from ERISA. In ERISA, the “prudence” referred to is a fiduciary level of prudence and part of the fiduciary obligation outlined in the Act. 29 U.S.C.A. §1104 (1974). Since the Act became effective in 1974, prudence has been tied to a fiduciary obligation that is a much higher and unworkable standard for the industry. If we really want to avoid a fiduciary obligation, then we must not include prudence in the draft.

The SEC, in Regulation Best Interest, agreed that the inclusion of prudence was potentially dangerous and chose to remove it. While most of the Working Group has agreed that we do not want to follow the SEC for no other reason than to be cohesive, their arguments are well reasoned and applicable to our draft. It makes sense to create a consistent standard as long as it satisfies our requirements, which this does. Furthermore, as fixed annuity products involve significantly less risk than securities, it does not make sense for the Working Group to impose more stringent standards on them than the SEC did with securities in Reg. BI.

Question 2 “Reasonable for an ordinary producer in a similar circumstance to recommend.” Is this an appropriate standard for a producer when making a recommendation?

We believe that this standard is unnecessary. The standard of “having a reasonable basis for the sale” should be sufficient to appropriately determine what was reasonable when making a recommendation. Furthermore, it is not unusual for producers to make different recommendations based on the same set of facts and circumstances. We do not want to create a standard that would result in a “battle of experts,” which is what could occur if this language was included.

Question 3 “Provide an oral or written description of the basis of the recommendation to the consumer.” When considering this requirement for a producer, is it appropriate to allow both oral and/or written descriptions?

It is appropriate to allow either oral or written descriptions. We want this to be a workable standard for all types of individuals, therefore any place that we can insert a little bit of flexibility to allow for the best transition to compliance without cutting people out of the market is beneficial to all.

Respectfully, our organizations would appreciate the opportunity to further discuss these issues in-person with the members of the NAIC (A) Committee and Working Group. We are confident that the current exposure draft can be amended so that a critical mass of stakeholders can be satisfied with the ultimate result. We believe in the efforts of the NAIC and that, together, we can develop a new model that will enhance the experience of our clients and promote the many benefits of fixed indexed annuities and working with insurance professionals.

Sincerely,

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