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Submitted Electronically To Jolie Matthews (jmatthews@naic.org)

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COMMENT ON BEHALF OF O'NEAL LAW GROUP, P.C.
SUGGESTED REVISIONS TO THE SUITABILITY IN ANNUITY TRANSACTIONS MODEL REGULATION (#275)

Director Cameron, Commissioner Ommen, and NAIC Annuity Suitability Working Group:

My name is Ryan Brown. I am an attorney in the state of Michigan, a licensed life insurance producer in the state of Michigan, and have vast experience dealing with insurance producers, independent marketing organizations ("IMOs"), and annuity carriers. All statements contained herein are solely my own and do not represent the opinions, strategies, positions, or views of any other person or entity. I submit this comment so that you may craft the NAIC suitability model to better serve consumers.

Introduction

While the Department of Labor Fiduciary Rule ("Rule") may have been well-intended, it incorrectly attempted to regulate FIAs, which, because they are insurance products, fall within the jurisdiction of the individual fifty states. Based on my experience of working and speaking with hundreds of financial professionals, whether state regulated insurance-only producers, FINRA regulated registered representatives, or SEC or state-regulated investment advisor representatives, the Rule did get some things right. All financial professionals should disclose to their prospective clients both (1) their total compensation and (2) their conflicts of interest. One resounding concept seems to always resonate with all aspects of this debate: Full and transparent disclosure.

Disclosure and transparency prevent the typical political and philosophical arguments that will undoubtedly ensue in this debate from reaching a critical mass. Issues such as what amount of commission falls inside or outside the scope of "reasonable compensation" will not occur if disclosure becomes the main mechanism within the new suitability model. This is because disclosure of such compensation within the marketplace will move the entire industry into more competitive practices, which will simultaneously protect and benefit consumers.

Some industry-insiders believe that the FIA industry is the "wild, wild west," and in some cases, this broad statement might be correct. With that said, some annuity producers make product recommendations that would damage consumers, while some truly practice the mantra of doing what is in their clients' best interest – whether or not they legally have a fiduciary duty through either a Series 65 license or a Certified Financial Planner designation. In order to prevent this internal chaos within the FIA industry, the NAIC should make full disclosure the main theme of its upcoming suitability model.

One of the best aspects of requiring full disclosure is that it would not dissuade or prohibit incentive within the industry. Rather, disclosure and transparency almost always guarantee that informed parties will make the most rational decisions. Opaqueness permits bad actors to cheat. If the new model takes that shroud away, then the entire FIA industry will improve itself and consumers will ultimately be better off. Because that is what all of us want, the NAIC should also not make its new model so narrow that bad actors – whether financial professionals, IMOs, or insurance carriers – will be able to find "clever" loopholes. Thus, there are some concepts I would propose the new model incorporate . . . .

I. The NAIC's Suitability Model should require all FIA producers to conspicuously disclose in writing to prospective clients at the time of writing the FIA application the amount of commission s/he earns pursuant to that particular product recommendation.

This was one aspect that the Department of Labor Fiduciary Rule got right. Again, this favors transparency and disclosure. A product with a higher commission does not necessarily mean it is inferior to a product with a lower commission. Like any product consumers purchase, the best product for a person depends on his/her individual needs and objectives. The Rule required annuity producers to disclosure the commission they received from the carrier to the consumer at the time of the recommendation, and this aspect of the Rule went into effect on June 9, 2017 most widely through Prohibited Transaction Exemption 84-24 ("84-24"). Interestingly enough, neither the Fiduciary Rule nor 84-24 required a producer to disclosure such information conspicuously – something the NAIC Suitability Model should require producers to do. The NAIC has the opportunity to fill in the gaps that neither the Rule nor 84-24 could have contemplated during the rule-making process. Requiring full and conspicuous disclosure that would be viewed as such to a reasonable person will help prevent deceptive tactics and methods and will better assist consumers in making informed decisions.

II. The NAIC's Suitability Model should prevent IMOs from creating conflicts of interest by preventing them from sharing their cash-based commission override with producers.

IMOs exist to act as the conduit and intermediary between individual annuity producers and the respective annuity carriers they are duly appointed and contracted with. In addition to assisting producers with their licensing, contracting, carrier appointments, and product training, IMOs are in the business of offering marketing services so that producers can increase their businesses – thus increasing the amount of business that flows through the respective IMO. An IMO earns revenue through the commission override ("override") that annuity carriers pay them in consideration for the services the IMO performs that the carrier cannot (e.g., contracting,

licensing, marketing, sales assistance, product training, compliance, continuing education, etc.). For example, if an annuity carrier pays a producer a 6% commission, it may pay the IMO a 2% commission override. Over the past decade, IMOs have enticed producers to do business with them versus other IMOs by giving producers a portion of the override they receive. This intrinsically creates a whole other subsect of conflicts of interest that the NAIC suitability model should prevent IMOs and producers from engaging in.

Some annuity carriers mandate that the IMO override be "protected," meaning that IMOs are prevented from sharing or giving producers any portion of the commission override they receive. If an IMO were to cheat or breach this, the IMO's appointment with the carrier would be terminated. While not all annuity carriers want to protect the commission override they pay IMOs, the NAIC model has the ability and jurisdiction to prevent IMOs from creating inherent conflicts of interests to producers and should do so. The following example will help illustrate . . . .

An IMO called Acme Marketing offers several FIAs that John Smith, a producer in the State of Michigan, is duly licensed and appointed to offer his clients. Acme Marketing agrees to give John an additional two percent of its commission override if/when he sells an FIA called ABC123 to his clients, but it will not do so on its protected FIA products. By being allowed to do this, the IMO has inherently created a conflict of interest by enticing John to sell FIA product ABC123 over other products – regardless of which product may actually end up being either more suitable or in the better interest of the client.

The NAIC Suitability Model should both prevent IMOs from proactively creating these conflicts of interest by preventing IMOs from sharing their commission override with producers. Just like attorneys are not permitted to share legal fees with non-lawyers, a state can propose and prevent an IMO from sharing its revenue. Because some producers may try to categorize

themselves as IMOs in order to sidestep this suggestion (thus arguing that an IMO can share its revenue with another IMO), the NAIC may choose to broadly define IMOs as entities that engage in the ordinary business activities of assisting producers in various states with licensing, contracting, carrier appointments, product training, compliance, continue education, etc. – almost all of which virtually no producer or financial services office engages in.

Conclusion

The NAIC's upcoming revamped Suitability Model is a unique opportunity for state regulators to reign in any "wild, wild west" mentality, actions, and perception of the fixed annuity industry. Full, transparent, and conspicuous disclosure to consumers has the power to be the major mechanism to help states do so without overreaching or creating a political/philosophical debate regarding the intimacies of the financial professional-client relationship. Simultaneously preventing IMOs from sharing their commission override with producers, which inherently creates conflicts of interest to producers when recommending products to clients, will prevent producers from recommending one product over the other simply because of a possible economic benefit.

Thank you for the opportunity to comment. If any member of the NAIC's Working Group has any questions regarding this comment or requests further clarification or information, please contact me directly.

Respectfully submitted,

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