January 22, 2018

TO:

The Honorable Dean Cameron Director,
Idaho Department of Insurance
Chairman, NAIC Annuity
Suitability (A) Working Group
700 West State Street, 3rd Floor
Boise, Idaho 83720-0043

The Honorable Doug Ommen
Commissioner, Iowa Insurance Division
Vice Chairman, NAIC Annuity
Suitability (A) Working Group
Two Ruan Center
601 Locust 4th Floor
Des Moines, IA 50309-3738

Submitted Electronically -- jmatthews@naic.org

Re: Comments on Suitability in Annuity Transactions Model Regulation (#275) Draft Revisions

Director Cameron and Commissioner Ommen:

The Association for Advanced Life Underwriting ("AALU") appreciates the opportunity to comment on the draft revisions to the National Association of Insurance Commissioners ("NAIC") Suitability in Annuity Transactions Model Regulation (#275) (the "Draft Model"). Given the importance of annuities to the financial security of working Americans, we commend the NAIC Annuity Suitability (A) Working Group ("Working Group") for seeking public comments as the NAIC considers a "best interest" standard of conduct in these transactions.

AALU is the leading organization of life insurance professionals—our 2,200 members are primarily producers engaged in providing life insurance planning and annuity solutions for individuals, families, and businesses nationwide. As life insurance industry professionals, we work in the best interest of our clients every day, enabling individuals and families from all economic brackets to maintain independence in the face of potential financial catastrophe, and to build and guarantee retirement income.

The DOL Fiduciary Rule is a Flawed Model:

While we uphold the principle that the recipients of advice regarding annuities and other financial products and services should receive advice in their best interest, poorly executed regulations (no matter how well intentioned) may negatively affect the very people they are intended to help. This is exactly the unfortunate result of the U.S. Department of Labor's ("DOL") fiduciary regulation and associated prohibited transaction exemptions (collectively, the "DOL Rule"), which has increased costs and reduced access to advice and to investment products since becoming applicable on June 9, 2017. There are a number of cautionary lessons for the NAIC and the Working Group based on the DOL fiduciary rule process.

Virginia: 11921 Freedom Drive | Suite 1100 | Reston, VA 20190 | 703.641.9400
Washington, DC: 101 Constitution Ave, NW | Suite 703 E | Washington, DC 20001 | 202.772.4638
www.aalu.org

- **Focus on Compensation Rather than Content**

The negative outcome of the DOL Rule is especially pronounced with respect to guaranteed income products and annuities because of the DOL Rule's bias against traditional forms of compensation in the insurance marketplace. Specifically, the DOL Rule generally prohibits commission-based compensation, compensation that varies between products or issuers, and compensation related to recommending a proprietary or affiliated investment product. The Rule then allows some of this prohibited compensation to be received, but only through compliance with detailed conditions of complicated exemptions. The DOL Rule's emphasis on compensation methods ultimately overshadows the actual content of the recommendation—the content is irrelevant if the compensation is not compliant.

To DOL's credit, it has recognized these very real concerns about its Rule. In response, it extended the Transition Period to July 2019. This prevented some of the most onerous conditions from going into effect on January 1, 2018, such as the replacement of the "reasonable" fee condition in a key exemption with the "level or "neutral" fee condition. In extending the Transition Period, DOL explained that it would use the time between now and July 2019 to coordinate with other regulators, including the Securities and Exchange Commission ("SEC") and the NAIC, to review the effects of the Rule, and to develop changes to the DOL Rule.

We urge the Working Group to recognize that it should be the content of the advice, not the structure of the compensation arrangement, that determines best interest. The fact that a producer earns a commission, or that this commission may vary from one product to another, does not prevent that producer from making a recommendation in the best interest of the client.

We urge the Working Group to recognize that the approach taken by the DOL Rule (which DOL itself is reevaluating and will likely change) is not right for the Model Rule. A best interest standard of care is about developing a recommendation that is based on the needs of the consumer, not about prohibiting traditional compensation arrangements already closely supervised by NAIC members.

Accordingly, we ask that the Working Group clarify that the best interest standard in the Draft Model does not affect, prohibit, or otherwise prevent the receipt of forms of compensation to producers currently permitted by law. Further, we ask that the Working Group clarify that the receipt of such permitted compensation is not evidence of a violation of the best interest standard.

Overlapping Jurisdictions Require Coordinated Efforts to Prevent Harm to Consumers:

The reality in the annuity marketplace is that the standards of multiple regulators may simultaneously apply to the same annuity transaction—for example, state insurance law, state and Federal securities laws, and the DOL Rule could all be implicated in a single transaction involving the sale of a variable annuity to an IRA owner. Where these standards conflict or impose significant new conditions, consumers ultimately bear the burden through reduced access to annuity products, or through higher costs, or both.

The prospects for such conflicting standards are very real. There is a flurry of activity addressing the standards for recommending annuities and other insurance products, including:

- **NAIC –**The Working Group put forward the Draft Model in November for public comment to consider whether to adopt a new Model Rule.
- **SEC—**The SEC plans on proposing in the next several months a new uniform fiduciary standard (a best interest standard of care). This best interest standard likely would be applicable to variable annuities and other insurance products that are also securities.
- **FINRA—**The new SEC standard would govern FINRA policies, almost certainly resulting in changes to FINRA rules (replacing or modifying the suitability standard).

- **DOL**—The DOL Rule is already in effect, but DOL is reviewing and revising its best interest standard and will likely propose amendments this year. The DOL Rule applies to annuities (and other investments) sold to ERISA plans or IRAs, or purchased pursuant to a recommendation to use a distribution from a plan or IRA.

This simultaneous activity must be coordinated to avoid a negative outcome for consumers. We urge the Working Group to coordinate very closely with these other regulatory entities as it considers adopting a best interest standard.

One of the reasons the current DOL Rule is flawed is that the agency pressed forward on promulgating a final rule without fully coordinating with appropriate regulatory entities. We are encouraged by recent comments from the DOL, SEC, and NAIC supporting such coordination, but we ask that the NAIC not move forward on a Model Rule without clear consensus among these entities. This is especially important for the NAIC given the role of its members as the primary regulators of the insurance marketplace.

- **Reasonable Implementation Period Essential**

The experience of AALU's members in implementing the DOL Rule makes it very clear that if the NAIC adopts a Model Rule, it must provide for more than six months to implement the necessary changes.

The amount of work necessary to implement a change in the standard of care is remarkable. Not only must training materials be developed and thousands of producers trained and certified, but the infrastructure behind developing and processing applications must be redesigned, and new compliance procedures developed and implemented. These are significant undertakings that cannot be easily completed in just six months as in the Draft Model.

The DOL Rule ultimately provided 14 months for implementation, and even at that, DOL found it necessary to adopt an enforcement policy that explained it would not pursue enforcement actions against service providers who made errors despite having worked diligently and in good faith to implement the Rule. Six months would simply not be enough time to address changes an NAIC Model Rule might require.

Conclusion

Our members are committed to acting in the best interest of the clients. However, the best interest of our clients will not be served if multiple regulators develop simultaneously applicable but uncoordinated or conflicting rules. It is vital that the Working Group and the NAIC take the time to work with the SEC, FINRA, and DOL to reach consensus on the right approach to a best interest standard that encourages the appropriate use of annuities and other applicable products, that makes it possible for producers to continue to provide the highest level of service and assistance to their clients, and that protects consumers from those who would do them harm.

We appreciate the opportunity to comment, and look forward to working with the Working Group and the NAIC. We would be happy to answer any questions you may have.

Sincerely,

David J. Stertzer
Chief Executive Officer
AALU