



Financial Security...for Life.

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January 22, 2018

Submitted Electronically to [jmatthews@naic.org](mailto:jmatthews@naic.org)

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700 West State Street, 3rd Floor  
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The Honorable Doug Ommen  
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**Subject: 11/24/17 Chair's Draft "Suitability and Best Interest Standard of Conduct in Annuity Transactions"**

Dear Director Cameron and Commissioner Ommen:

These comments are submitted on behalf of the American Council of Life Insurers (ACLI)<sup>1</sup> regarding the November 24, 2017 Chair's draft (Draft) of proposed revisions to the National Association of Insurance Commissioners (NAIC) Suitability in Annuity Transactions (Annuity Suitability) Model Regulation. ACLI commends the Annuity Suitability Working Group (Working Group) for its efforts to enhance the Annuity Suitability Model Regulation to incorporate a best interest standard of care for annuities. We recognize that the draft will continue to evolve and look forward to providing additional comments as the NAIC coordinates its work with federal agencies.

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<sup>1</sup>The American Council of Life Insurers (ACLI) is a Washington, D.C.-based trade association with approximately 290 member companies operating in the United States and abroad. ACLI advocates in state, federal, and international forums for public policy that supports the industry marketplace and the policyholders that rely on life insurers' products for financial and retirement security. ACLI members offer life insurance, annuities, retirement plans, long-term care and disability income insurance, and reinsurance, representing 95 percent of industry assets, 93 percent of life insurance premiums, and 98 percent of annuity considerations in the United States. Learn more at [www.acli.com](http://www.acli.com).

## **Importance of a Uniform Best Interest Standard of Care**

ACLI supports a uniform best interest standard of care that applies to individualized recommendations to retail customers regarding the purchase, exchange or replacement of an annuity or security. Accordingly, ACLI supports reasonable and appropriately tailored rules that require all annuity producers to act in the best interest of their customers.

Consumers seeking guaranteed lifetime income in retirement will benefit from a harmonized best interest standard of care for annuities. This can be achieved only through a coordinated effort among state insurance regulators, the Securities and Exchange Commission (SEC), the Financial Industry Regulatory Authority (FINRA), and the Department of Labor (DOL). ACLI is encouraged that the NAIC has recognized the importance to consumers of a harmonized standard of care across all regulatory platforms, and plans to coordinate with the DOL, the SEC and FINRA in an effort to secure harmonization before any revisions to its Annuity Suitability Model Regulation are given final approval.

We are equally encouraged by recent pronouncements made by the DOL and SEC regarding the importance of coordination between state and federal agencies toward a harmonized standard. In delaying key aspects of its regulation last November, the DOL specifically noted that without a delay, its original timeline would not accommodate the desire to coordinate with the SEC, FINRA and NAIC in development of revisions to its rule. Similarly, SEC Secretary Clayton has publicly stressed the importance of clarity, consistency “and, in areas overseen by more than one regulatory body, coordination” in the development of standards of conduct. The SEC has released an agenda that calls for a proposal by October 2018.

## **ACLI Guiding Principles**

Our evaluation of the Draft was guided by the following principles, approved by ACLI’s Board, that support a best interest standard of care for annuities and securities:

- 1) A recommendation must reflect care, skill, prudence, and diligence.
- 2) A person making a recommendation must address material financial conflicts of interest.
- 3) Consumers should know the types and scope of services they will receive as well as the types of compensation to be received by the person making the recommendation.
- 4) The standard is to apply when a recommendation is made with no further or ongoing obligation to the consumer unless otherwise agreed to.
- 5) Rules must be neutral to business model, product type, and compensation approach such as commissions or sales charges, or other fees or variable compensation.
- 6) The fact that an advisor or firm only offers or recommends proprietary or a limited range of products or product types or receives commissions or other variable compensation is not inconsistent with a best interest standard.
- 7) The best interest standard must not require a recommendation of the least expensive or "best" product available.

## **Overview of Key ACLI Questions and Concerns with the 11/24/17 Chair's Draft**

ACLI supports the key concepts that underlie many of the Draft's proposed revisions to the Annuity Suitability Model Regulation. At the same time, the Draft gives rise to some significant questions and concerns that require further consideration. For your convenience, we have attached to this letter a detailed mark-up that provides specific suggestions to modify the Draft to address our questions and concerns, the most significant of which are as follows (*the section references below align with ACLI's detailed mark-up*):

### **Section 1. "Purpose" (Retention of Suitability Requirements in Conjunction with Proposed New Best Interest Standard)**

In Section 1 and throughout the rest of the Draft, the best interest standard is added, but suitability as a separate concept remains. As we learned throughout the debate on the DOL's fiduciary rule, there appears to be significant misunderstanding and confusion regarding suitability as a standard of care. There would be benefits to using only the term "best interest" as the harmonized standard of care. We have proposed changes to accomplish this goal. For example, ACLI suggests that use of the term "suitable" generally be eliminated, and, more specifically that where appropriate, consistent with the goals discussed above, we propose substitution of the word "suitable" with generally what it means, to "further the consumer's insurance needs and financial objectives." For example, instead of a "suitable product" we propose modification to refer to a product that furthers the consumer's insurance needs and financial objectives.

To align the text with the stated purpose of the revised Model Regulation, i.e., to provide a best interest standard of conduct with respect to annuity and securities "recommendations," throughout the attached mark-up, as appropriate, we have proposed substituting "transaction" with "recommendation" (as a "transaction" may not always result from a "recommendation").

### **Section 2. "Scope"**

ACLI appreciates the rationale for the scope of the Model Regulation to include solicitation and negotiation of annuities because parts of the Model Regulation apply to activities, such as training or systems of supervision, that precede a "recommendation." However, in general, ACLI believes the vast majority of the Model Regulation's requirements should only be imposed in connection with "recommendations" to purchase annuities that may result in cash or non-cash compensation. In the attached mark-up of the Draft, we propose changes along these lines as necessary. For example, we propose removing negotiation from the definition of cash compensation as producers are not compensated for negotiations.

### **Section 5.B. "Best Interest"**

ACLI proposes that the term "Best Interest" be defined as follows:

*"Best interest: A recommendation is in the "best interest" of the consumer if, at the time the recommendation is made, the insurance producer, or the insurer where no producer is involved, acts with reasonable diligence, care, skill and prudence; bases the annuity recommendation on the client's insurance needs and financial objectives as set forth in the Consumer Profile Information; and places the client's interest above the financial interest of the insurance producer or insurer.*

- (1) *To act in the "Best interest" does not mean a producer or insurer is required to recommend the least expensive annuity product, or the annuity product with the highest stated interest rate or income payout rate, or the single "best" annuity product available in the marketplace at the time of the annuity recommendation, but based on the insurance producer's judgment, or the insurer's judgement where no producer is involved, acting with reasonable diligence, care, skill and prudence, the recommendation is made in the consumer's best interest.*
- (2) *The mere receipt by an insurance producer, or the insurer where no producer is involved, of any cash or non-cash compensation for or related to a recommendation is not inconsistent with the requirements of this Regulation.*
- (3) *The fact that an insurance producer, or the insurer where no producer is involved, offers or recommends proprietary or a limited range of annuity products (including underlying sub-accounts) or product types is not inconsistent with the requirements of this Regulation.*
- (4) *The fact that an insurance producer, or the insurer's representative where no producer is involved, receives health, retirement, or other employee benefits provided by an insurer is not inconsistent with the requirements of this Regulation, nor does it need to be specifically disclosed as a material conflict of interest, or additional cash or non-cash compensation.*

For greater consistency with other regulatory regimes' standards and with the Draft's provision in current Section 8(3) concerning prohibited practices, our formulation of the definition of "best interest" would eliminate the reference to "first and foremost." Our language would also make it clear that the best interest requirement is applicable at the time of the recommendation, in conformity with the Purpose section and other provisions of the draft (as opposed to "issuance"). ACLI's proposal would further conform with the standards in other regulatory regimes by making it clear that the receipt of compensation, the offering of proprietary or a limited range of annuity products, and the receipt of health, retirement, or other employee benefits are not inconsistent with the requirements of the Model Regulation.

#### **Section 5. K. "Non-Cash Compensation"/Section 7. Non-Cash Compensation Disclosure Requirement**

As reflected in the attached mark-up of the Draft, ACLI proposes to amend the definition of non-cash compensation to include additional examples of non-cash compensation, currently provided in Section 7.

We propose that Section 7 be deleted, and that the disclosure requirement relating to non-cash compensation be reinserted as a new subsection (3) in Section 6.C. We believe it will be clearer to include all the compensation disclosure requirements in the same section. In new Section 6.C.(3), we propose a requirement to disclose the "types" of non-cash compensation the producer would or would be eligible to receive.

To address concerns that \$100 may not be the appropriate threshold for disclosure and that the inclusion of any specific dollar amount as a threshold could lead to different thresholds in different states, we propose that the definition of “non-cash compensation” refer to non-cash compensation “worth more than a de minimis amount.”

#### **Section 5.L. “Reasonable Cash Compensation”**

ACLI proposes that the term “Reasonable cash compensation” be modified to read as follows: “cash compensation that is not excessive, based on the facts and circumstances at the time of recommendation. Relevant factors would include known compensation market ranges, and the complexity, features and benefits of the product. No single factor is dispositive in determining whether cash compensation is reasonable.”

Our proposed definition would be more consistent than the currently proposed definition with the approach taken in the preamble to the DOL rule and in other regulatory systems. Also, the phrase in the currently proposed definition “volume of production” lacks clarity and, together with the prohibition in current Section 8(1), could be construed as effectively prohibiting forms of compensation that are in the market today.

#### **Section 5. O. “Consumer Profile Information”**

We propose that the term “Suitability Information” be renamed “Consumer Profile Information,” as a term of art consistent with other regulatory schemes, that will work better from a harmonization perspective. We propose modification to subsection (1) of Section 6. D. to require disclosure of “the potential for changes in nonguaranteed elements” and to remove this phrase from subsection (11) of the definition of “Consumer Profile Information,” as the gathering of such information would precede the discussion of any particular annuity product and whether there are any nonguaranteed elements to consider.

#### **Section 6.B.(2) Requirement to Evaluate Types of Financial Products**

As currently written, Section 6.B.(2) could be construed to require producers to “evaluate types of financial products” beyond those which they offer or are appropriately registered or licensed to sell. A producer should only be required to consider the types of products he or she is authorized to sell, as reflected in our proposed modifications to this provision in the attached mark-up of the Draft.

#### **Section 6.C.(2). Required Disclosure of Cash Compensation above 3%**

ACLI supports disclosure of information relating to cash compensation. However, the 3% threshold for disclosure in Section 6.C.(2) gives rise to a number of questions and concerns. The manner in which the 3% threshold is intended to be calculated is unclear. If intended to provide a safe harbor, what would the safe harbor cover? We are also concerned that this provision would become unwieldy as different states might apply differing threshold amounts. ACLI proposes substitution of the current language of this provision with language consistent with ACLI’s best interest policy that supports disclosure of a description of cash compensation.

## **Section 6.F. Circumstances Under Which There is No Obligation to Determine Whether an Annuity is Suitable**

The intent of this section is unclear. It would require the insurer to determine “the annuity is reasonable prior to issuance” under the specified circumstances, effectively creating a third standard in addition to the suitability and the best interest standards, that is tied to “issuance,” rather than a recommendation of an annuity. It is unclear what is meant by the phrase “circumstances actually known to the insurer” and the subjective word “reasonable.”

We propose modification to address the apparent goal of this provision – to provide relief from the requirement of the Model Regulation when no recommendation is made and the consumer insists on the purchase of an annuity. We believe the original construction of this provision addresses this more clearly and recommend going back to that construction.

## **Section 6.H. Supervision System**

There is significant concern that this section fails to make clear the supervisory obligations of insurers with respect to producers who are able to sell products of multiple insurers. Our proposed modifications to this section in the attached mark-up to the Draft would clarify that an insurer is only responsible for the insurer’s products that the producer is authorized to sell, and that an insurer is not responsible to know what other products a producer is authorized to sell or what relationships that a producer may have, or to have familiarity with other insurers’ products.

We also propose modification to subsection 1(d) and (e) to take into account that while it is possible for an insurer to review the application to determine whether an annuity furthers the consumer’s insurance needs and financial objectives, determining whether a producer acted in the best interest of the consumer is not feasible as part of the application review process. We propose the addition of a new subsection 1(f) to more clearly address this concern.

## **Section 6.J. FINRA Requirements**

This section appears to substitute the current safe harbor for sales made in compliance with the FINRA suitability requirements with a safe harbor only for sales made in compliance with FINRA “best interest standards.” However, FINRA has not yet adopted specific “best interest standards.” This gives rise to concern that sales made in compliance with the suitability requirements in FINRA Rule 2330 may no longer be deemed to meet the requirements of the Model Regulation. To address this concern, we propose modification to this section to insert references to “suitability/best interest” standards.

## **Section 6.K. Need for Clarification of No Continuing Best Interest Duty**

ACLI has proposed language to make it clear that nothing in Section 6 imposes a continuing obligation on an insurer or insurance producer after the recommended annuity is issued. Such a provision is consistent with standard of conduct obligations in other regulatory regimes.

**Section 8 Credit for Prior Training Classes**

We propose the addition of a new Section 8.B.(9) to recognize that various components of the revised Model's training requirements may have already been met or may be met by a producer taking more than one training course so long as the courses have components substantially similar to those required by the provisions of this subsection and the producer has received training in the required topics.

**Section 9 Compliance**

In current Section 9, we propose modifications to distinguish between an insurer's responsibilities under the Model Regulation and the producer's responsibilities under the Model Regulation. As we discussed above in Section 6.H., there are elements of the revised Model Regulation for which a producer's activities may stand alone outside the purview of the insurer (for example, undisclosed Conflicts of Interest, or failure to disclose a contest or award offered by an intermediary and unknown to the insurer).

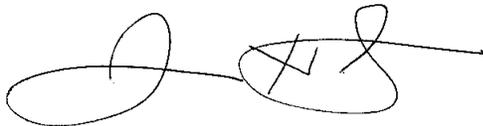
**Section 12 Effective Date**

As we cannot effectively gauge the time needed to implement the requirements of the revised Model Regulation until it nears completion, we propose deletion of the six-month requirement and insertion of a blank line for future consideration and discussion.

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Again, ACLI thanks the Working Group for the opportunity to submit these comments and for its consideration of our views. We would be glad to answer questions relating to any of our comments above or our specific proposed modifications to the Draft set forth in the attached mark-up. We look forward to continuing to work with the Working Group as it continues its efforts to modify the Annuity Suitability Model Regulation to provide a best interest standard of care for annuities.

Sincerely,



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- Cc: The Honorable Julie Mix McPeak, Tennessee Insurance Commissioner and NAIC President
- The Honorable Eric Cioppa, Maine Insurance Superintendent and NAIC President-Elect
- The Honorable Raymond G. Farmer, South Carolina Insurance Director and NAIC Vice President
- The Honorable Gordon I. Ito, Hawaii Insurance Commissioner and NAIC Secretary-Treasurer
- Mr. Michael F. Consedine, NAIC Chief Executive Officer

Draft: 11/24/17  
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](mailto:jmatthews@naic.org).

## SUITABILITY AND BEST INTEREST STANDARD OF CONDUCT IN ANNUITY TRANSACTIONS MODEL REGULATION

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### Section 1. Purpose

- A. The purpose of this regulation is to require insurers to establish a system to supervise annuity recommendations and to set forth standards and procedures for recommendations of annuity products by insurance producers and insurers, where no producer is involved, to consumers that are suitable, in their in the consumer's best interest and result in transactions involving annuity products so that the insurance needs and financial objectives of consumers at the time of the transaction are appropriately addressed.
- 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.

### Section 2. Scope

This regulation shall apply to any solicitation, negotiation, recommendation or sale 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 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;
- (4) A nonqualified deferred compensation arrangement established or maintained by an employer or plan sponsor;
- (5) Settlements of or assumptions of liabilities associated with personal injury litigation or any dispute or claim resolution process; or
- (6) 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.
  - (1) ~~"Best interest" means, at the time the annuity is issued, acting with reasonable diligence, care, skill and prudence in a manner that puts the interest of the consumer first and foremost.~~ "Best interest." A recommendation is in the "best interest" of the consumer if, at the time the recommendation is made, the insurance producer, or the insurer where no producer is involved, acts with reasonable diligence, care, skill and prudence; bases the annuity recommendation on the client's insurance needs and financial objectives as set forth in the Consumer Profile Information; and places the client's interest above the financial interest of the insurance producer or insurer.
  - (2) ~~To act in the "Best interest" does not mean a producer or insurer is required to recommend the least expensive annuity product, or the annuity product with the highest stated interest rate or income payout rate, or the single "best" annuity product available in the marketplace at the time of the annuity recommendation, but based on the insurance producer's judgment, or the insurer's judgement where no producer is involved, acting with reasonable diligence, care, skill and prudence, the recommendation is made in the consumer's best interest. "Best interest" does not mean a resulting recommendation is the least expensive annuity product, or the annuity product with the highest stated interest rate or income payout rate, available in the marketplace at the time of the annuity transaction. "Best interest" also does not mean the recommendation is the single "best" annuity product available in the marketplace at the time of the annuity transaction, but based on the insurance producer's judgment acting with reasonable diligence, care, skill and prudence, the producer believes the recommendation is in the best interest of the consumer~~
  - (2) The mere receipt by an insurance producer, or the insurer where no producer is involved, of any cash or non-cash compensation for or related to a recommendation is not inconsistent with the requirements of this Regulation.
  - (3) The fact that an insurance producer, or the insurer where no producer is involved, offers or recommends proprietary or a limited range of annuity products (including underlying sub-accounts) or product types is not inconsistent with the requirements of this Regulation.
  - (4) The fact that an insurance producer, or the insurer's representative where no producer is involved, receives health, retirement, or other employee benefits provided by an insurer is not inconsistent with the requirements of this Regulation, nor does it need to be specifically disclosed as a material conflict of interest, or additional cash or non-cash compensation.

- C. "Cash compensation" means any discount, concession, fee, service fee, commission, sales charge, loan, override or cash benefit received by a producer from an insurer, intermediary, or directly from the consumer, in connection with the ~~solicitation, negotiation, recommendation or sale~~ of an annuity.
- 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. "Insurance producer" or "producer" means a person or entity required to be licensed under the laws of this state to sell, solicit or negotiate insurance, including annuities.
- I. "Intermediary" means an entity contracted with the ~~insurance company~~insurer, or another intermediary, to facilitate the sale of an annuity.
- J. (1) "Material conflict of interest" means a financial interest of an insurance producer, or the insurer where no producer is involved, that a reasonable person would expect to affect the impartiality of the recommendation.
- (2) "Material conflict of interest" includes financial incentives or rewards offered to or received by an insurance producer, or a direct interest or ownership in an insurer by an insurance producer or an immediate family member of an insurance producer.
- ~~K.~~ "~~Negotiate~~" ~~has the meaning stated in [insert reference to state law equivalent to Section 2K of the Producer Licensing Model Act (#218)].~~
- ~~L~~K. "Non-cash compensation" means any form of compensation that is not cash compensation, received by an insurance producer from an insurer or an intermediary in connection with the recommendation of an annuity that is worth more than a de minimis amount, including but not limited to, entertainment, merchandise, gifts and prizes, trips, travel expenses, ~~or~~ meals and lodging, and marketing or advertising expenses.
- ~~M~~L. "Reasonable cash compensation" means cash compensation that is not excessive, based on the facts and circumstances at the time of the recommendation. Relevant factors would include known compensation market ranges, and the complexity, features and benefits of the product. No single factor is dispositive in determining whether cash compensation is reasonable. that reflects the time and complexity of the product and the transaction involved and is not connected to volume of production.
- ~~N~~M. "Recommendation" means advice provided by an insurance producer, or an insurer where no producer is involved, to an individual consumer that results in a purchase, sale, exchange or replacement of an annuity in accordance with that advice.
- Recommendation does not include general communications to the public, marketing and other product or sales materials, prospectuses, general education information and tools, and general customer service assistance or administrative support.
- ~~O~~N. "Replacement" means a transaction in which a new policy or contract is to be purchased, and it is known or should be known to the proposing producer, or to the proposing insurer if there is no producer, that by reason of the transaction, an existing policy or contract has been or is to be:

- (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.

PO. ~~“Suitability information~~Consumer Profile Information” means information that is reasonably appropriate to determine the recommendation is ~~suitable and~~ in the best interest of the consumer, including the following:

- (1) Age;
- (2) Annual income;
- (3) Financial situation and needs;
- (4) Financial experience;
- (5) Financial objectives;
- (6) Intended use of the annuity;
- (7) Financial time horizon;
- (8) Existing assets or financial products, including investment and life insurance holdings;
- (9) Liquidity needs;
- (10) Liquid net worth;
- (11) Risk tolerance, ~~including changes in nonguaranteed elements in an annuity contract;~~
- (12) Financial resources used to fund the annuity; and
- (13) Tax status.

## **Section 6. Duties of Insurers and of Insurance Producers**

- A. In recommending to a consumer the purchase of an annuity or the exchange of an annuity that results in another insurance transaction or series of insurance transactions, the insurance producer, or the insurer where no producer is involved, shall only make a recommendation that the insurance producer, or the insurer where no producer is involved, has reasonable grounds to believe is ~~suitable and~~ in the best interest of the consumer at the time ~~it~~the recommendation is made based on the ~~facts disclosed by the consumer as to his or her investments and other insurance products and as to his or her financial situation and needs, including the consumer’s suitability information~~Consumer Profile Information.

- B. Prior to the recommendation of an annuity, an insurance producer, or an insurer where no producer is involved, shall do all of the following:
- (1) Make reasonable efforts to obtain the ~~consumer's suitability information~~Consumer Profile Information;
  - (2) ~~Evaluate~~Consider the types of insurance and financial products that the insurance producer, or an insurer where no producer is involved, is authorized to recommend or sell when reviewing the consumer's insurance needs and financial objectives which correspond to the consumer's disclosed by the consumer in the suitability informationConsumer Profile Information ~~and address the consumer's financial objectives~~; and
  - (3) Disclose to the consumer ~~any limitations the producer or the insurer has in regard to~~ the following:
    - (a) The types of insurance and ~~of~~ financial products that can be provided;
    - (b) Whether only specific insurer ~~company proprietary products~~ or a limited range of annuity products can be offered;
    - (c) The scope of services provided; and
    - (d) The scope of the producer's licenses.
- C. In making a recommendation, the insurance producer, or insurer where no producer is involved, shall disclose to the consumer:
- (1) ~~Any and all m~~Material conflicts of interest;
  - (2) ~~The percentage or amount of cash compensation above three (3) percent, whether by commission or fee, the insurance producer would receive as a result of a contract for services for advice or for the sale of a recommended annuity; and~~
    - (a) A description of the cash compensation the producer will receive from the insurer, intermediary or directly from the consumer, as a result of the annuity recommendation;
    - (b) That the cash compensation received by the producer may vary depending on a number of factors;
    - (c) That the consumer can obtain additional information about the cash compensation expected to be received by the producer as a result of the recommendation by requesting such information from the producer;
    - (d) If the consumer requests such additional information about the producer's cash compensation prior to the issuance of the annuity, the producer shall disclose the requested information at or prior to the issuance of the annuity which may, if requested, include the use of percentages, dollar amounts, ranges, or estimates;
  - (3) A description of the types of non-cash compensation the insurance producer would receive or be eligible for from the insurer whose product is recommended or an intermediary as a result of the annuity recommendation.
  - (34) ~~The basis or bases of the recommendation~~How the recommendation will further the consumer's insurance needs and financial objectives.
- D. In making a recommendation, the insurance producer, or insurer where no producer is involved, shall have a reasonable basis to believe all of the following:

- (1) The consumer has been reasonably 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, potential charges for and features of riders, limitations on interest returns, insurance and investment components and market risk; and the potential for changes in nonguaranteed elements;

**Drafting Note:** If a State has adopted the NAIC Annuity Disclosure Model Regulation, the State should insert an additional phrase in paragraph (1) 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.

- (2) The consumer would benefit from certain features of the annuity, such as tax-deferred growth, annuitization or death or living benefit;
  - (3) The particular annuity as a whole, the underlying subaccounts to which funds are allocated at the time of purchase or exchange of the annuity, and riders and similar product enhancements, if any, are ~~suitable and~~ in the best interest of the consumer (and in the case of an exchange or replacement, the transaction as a whole is ~~suitable and~~ in the best interest of the consumer) for the particular consumer based on his or her ~~suitability information~~ Consumer Profile Information; and
  - (4) In the case of an exchange or replacement of an annuity, the exchange or replacement is ~~suitable and~~ in the best interest of the consumer including taking into consideration whether:
    - (a) 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;
    - (b) The consumer would benefit more over the life of the replacing annuity than the annuity being replaced based on factors such as product enhancements and improvements, the level of benefits or payment terms, or product fees and charges from product enhancements and improvements and the replacing product would provide a substantial financial benefit to the consumer over the life of the product; and
    - (c) The consumer has had another annuity exchange or replacement and, in particular, an exchange or replacement within the preceding 60 months.
- E. Except as permitted under subsection F, an insurer shall not issue an annuity recommended to a consumer unless there is a reasonable basis to believe the annuity ~~is suitable~~ furthers the consumer's insurance needs and financial objectives based on the ~~consumer's suitability information~~ Consumer Profile Information.
- F. (1) Except as provided under paragraph (2) of this subsection, neither an insurance producer nor an insurer shall have any obligation to a consumer under subsection A or E of this Section related to any annuity transaction. An insurer is not obligated to determine an annuity is suitable, but instead, shall determine the annuity is reasonable prior to issuance based on the circumstances actually known to the insurer at the time the annuity is issued if any of the following situations occur:
- ~~(1a)~~ (1a) ~~Neither the~~ The producer ~~nor the insurer~~ makes ~~any~~ recommendation;
  - ~~(2b)~~ (2b) A recommendation was made and was later found to have been prepared based on materially inaccurate information provided by the consumer;
  - ~~(3c)~~ (3c) A consumer refuses to provide relevant ~~suitability information~~ Consumer Profile Information and the annuity transaction is not recommended; or
  - ~~(4d)~~ (4d) A consumer decides to enter into an annuity transaction that is not based on a recommendation of the insurer or the insurance 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.

- G. An insurance producer or, where no insurance producer is involved, the responsible insurer representative, shall at the time of ~~sale~~ recommendation:
- (1) Make a record of any recommendation and the basis or bases of how the recommendation will further the consumer's insurance needs and financial objectives ~~the recommendation~~ subject to this regulation;
  - (2) Obtain a customer signed statement documenting a customer's refusal to provide ~~suitability information~~ Consumer Profile Information, if any; and
  - (3) Obtain a customer signed statement acknowledging that an annuity transaction is not recommended if a customer decides to enter into an annuity transaction that is not based on the recommendation of the insurance producer<sup>s</sup>, or insurer, where no insurance producer is involved ~~or insurer's recommendation~~.
- H. (1) An insurer shall establish a supervision system that is reasonably designed to achieve the insurer's and ~~its~~ insurance producers' producers authorized to recommend the insurer's annuity products' compliance with this regulation, including, but not limited to, the following:
- (a) The insurer shall maintain reasonable procedures to inform ~~its~~ insurance producers authorized to recommend the insurer's annuity products of the requirements of this regulation and shall incorporate the requirements of this regulation into relevant insurance producer training manuals;
  - (b) The insurer shall establish standards for insurance producer product training and shall maintain reasonable procedures to require ~~its~~ insurance producers authorized to recommend the insurer's annuity products to comply with the requirements of section ~~9-8~~ 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~~ insurance producers authorized to recommend the insurer's annuity products;
  - (d) The insurer shall maintain procedures for review of each recommendation of its annuity products prior to issuance of an annuity that are designed to ensure that there is a reasonable basis to determine that a recommendation further the consumer's insurance needs and financial objectives ~~is suitable and in the best interest of a consumer~~. 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 maintain reasonable procedures to detect recommendations of its annuity products that do not further the consumer's insurance needs and financial objectives ~~are not suitable and are not in the best interest of the consumer~~. This may include, but is not limited to, confirmation of ~~consumer suitability information~~ 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 ~~suitability information~~ Consumer Profile Information after issuance or delivery of the annuity; ~~and~~

- (f) The insurer shall make reasonable efforts to address a situation for which there is a clear indication that a producer failed to act with reasonable diligence, care, skill and prudence, or failed to place the consumer's interest above the producer's financial interest.
- (fg) The insurer shall annually provide a 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.
- (2) (a) Nothing in this subsection restricts an insurer from contracting for performance of a function (including maintenance of procedures) required under paragraph (1). An insurer is responsible for taking appropriate corrective action and may be subject to sanctions and penalties pursuant to section ~~10-9~~ 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 paragraph (1) 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.
- (3) An insurer is not required to consider or have knowledge of other insurers' annuity products that an insurance producer could have recommended to a consumer nor include in its system of supervision an insurance producer's recommendations to consumers of products other than the annuities offered by the insurer that the producer is authorized to recommend.
- (4) Notwithstanding any Material Conflict of Interest that may be presented by compensation payable by an insurer to the insurance producer, or other Material Conflicts of Interest or other information that would reasonably be known to the insurer, an insurer is not required to:
- (a) confirm the adequacy, or nature, of an insurance producer's disclosure of producer's Material Conflicts of Interest required by Section 6.C (1); or
- (b) validate, or otherwise reasonably determine, the accuracy of an insurance producer's other disclosures required by Section 6.B. and Section 6.C.
- I. An insurance producer shall not dissuade, or attempt to dissuade, a consumer from:
- (1) Truthfully responding to an insurer's request for confirmation of ~~suitability information~~ Consumer Profile Information;
- (2) Filing a complaint; or
- (3) Cooperating with the investigation of a complaint.
- J. (1) ~~Sales—Recommendations~~ made in compliance with FINRA requirements pertaining to suitability/best interest standards and supervision of annuity transactions shall satisfy the requirements under this regulation. This subsection applies to FINRA broker-dealer ~~sales recommendations~~ of annuities if the suitability/best interest standard and supervision is similar to those applied to variable annuity sales. However, nothing in this subsection shall limit the insurance commissioner's ability to enforce (including investigate) the provisions of this regulation.

**Drafting Note:** Non-compliance with FINRA requirements means that the broker-dealer transaction is subject to compliance with the suitability-best interest 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.

(K) Nothing herein shall impose on an insurer or an insurance producer any continuing obligation to the consumer under this Regulation after the recommended annuity is issued.

#### ~~Section 7. Non-Cash Compensation Disclosure Requirement~~

~~In addition to the disclosures required under Section 6 of this regulation, an insurance producer or an insurer, where no producer is involved, shall disclose to the consumer information regarding the non-cash compensation that exceeds \$100 per producer per year the producer receives from an insurer or intermediary that is tied to the sale of annuities including, but not limited to, gifts, meals, trips, entertainment, prizes, marketing, and advertising.~~

#### ~~Section 87. Prohibited Practices~~

An insurance producer or an insurer where no producer is involved:

- (1) Shall receive no more than reasonable cash compensation in making a recommendation;
- (2) Shall not make any materially misleading statements regarding the annuity transaction; and
- (3) Shall not base a recommendation on the producer's or insurer's own financial interest.

#### ~~Section 98. Insurance Producer Training~~

- A. An insurance producer shall not solicit, negotiate, or recommend the sale or replacement of an annuity product unless the insurance producer has adequate knowledge of the product to recommend the annuity and the insurance producer is in compliance with the insurer's standards for product training. An insurance producer may rely on insurer-provided product-specific training standards and materials to comply with this subsection.
- B.
  - (1)
    - (a) An insurance 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) Insurance 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;
  - (f) Financial exploitation of seniors and other vulnerable adults; and
  - (g) Appropriate sales practices, replacement and disclosure requirements, including the requirements under this regulation.
- (4) (a) 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 annuity products. Additional topics may be offered in conjunction with and in addition to the required outline.
- (b) A training course that complies with the requirements of FINRA Rule 1250 meets the requirements of Paragraph (3).
- (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 insurance producer continuing education courses as set forth in [insert reference to State law or regulations governing producer continuing education course approval].
- (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].
- (7) 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].
- (8) 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.
- (9) 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.
- (910) An insurer shall verify that an insurance 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 109. Compliance Mitigation; Penalties**

- A. An insurer is responsible for compliance with its obligations under this regulation when a recommendation results in the purchase of its annuity products, or for the training required in Section 8 for producers authorized to sell the insurers annuity products. If a violation occurs, either because of the action or inaction of the insurer in meeting its obligations under Section 6.H., or ~~its~~ the action or inaction of an insurance

producer in meeting the producer's obligations under this regulation~~insurance producer~~, the commissioner may order:

- (1) An insurer to take reasonably appropriate corrective action for any consumer harmed by the insurer's~~, or by its insurance producer's~~, violation of its obligations under this regulation;
- (2) A general agency, independent agency or the insurance producer to take reasonably appropriate corrective action for any consumer harmed by the insurance 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 commissioner,] 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.

C. [Placeholder for any additional considerations needed for harmonization efforts with other regulators]

**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 11. Recordkeeping**

A. Insurers, general agents, independent agencies and insurance producers shall maintain or be able to make available to the commissioner records of the information collected from the consumer, written disclosures made to the consumer and other information used in making the recommendations that were the basis for insurance transactions for six (6) 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 an insurance producer.

**Drafting Note:** States should review their current record retention laws for consistency with Subsection A above.

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 12. Effective Date**

The amendments to this regulation shall take effect six (6) months \_\_\_\_\_ after the date the regulation is adopted or on [insert date], whichever is later.