

COMPLIANCE & LEGAL SECTIONS ANNUAL MEETING 2019

JULY 15-17

FORT LAUDERDALE MARRIOTT HARBOR BEACH RESORT & SPA

FORT LAUDERDALE, FL

ACLI
Financial Security... for Life.



Mid-Year Check-In

Best Interest Standard of Care

Steve Toretto Moderator

Former Vice-President &
Associate General
Counsel
Pacific Life Insurance Co.

Jillian Froment Speaker

Director
Ohio Department of
Insurance

Stephen J. Jordan Speaker

Partner

Drinker Biddle & Reath LLP

SEC'S Regulation Best Interest

- **Highlights of Reg. B.I.**
 - New compliance obligation
 - Changes to conflicts obligations
 - Transactional compensation not prohibited
 - Duty focuses on recommendation, not ongoing relationship
 - Clarification of retail customer
 - Expansive definition of recommendation
 - Extensive and burdensome disclosure obligations
 - Voluminous guidance

Reg. B.I.

- **Obligations:**
 - **Disclosure:**
 - Full and fair disclosure of material facts of relationship and recommendations
 - Capacity, fees and costs, products and services provided (and limitations), conflicts
 - **Care:**
 - Reasonable diligence, care, and skill
 - Understand potential risks, rewards, and costs
 - Best interest recommendation based on investment profile

Reg. B.I.

- **Obligations (Policies and Procedures)**
 - **Conflict-of-Interest:**
 - Firm level -- identify and at a minimum disclose or eliminate conflicts.
 - Associated persons – mitigate financial incentives contrary to obligation.
 - Prevent material limitations on investments from causing recommendations contrary to obligation.
 - Eliminate certain sales contests, quotas, bonuses and other noncash compensation.
 - **Compliance with Reg. B.I.**

Reg. B.I.

- **FINRA Guidance**
 - Eliminate or align suitability rules
 - Non-cash compensation rules
 - Conflict management oversight
 - Identification of conflicts
 - Mitigation of certain financial incentives
 - Policies and procedures to address limited products/services

Reg. B.I.

- **Record-making/retention**
 - Requirements
 - Guidance on documenting basis/rationale for complex investments, limited product offerings, and investor sophistication.

Reg. B.I.

- **Liability/Exposure**
 - Additional basis for SEC examination and enforcement
 - Private litigation and arbitration

NAIC Status

- November 2018 – Draft revisions to Annuity Suitability Model 275
- April 2019 – presentation comparing SEC’s proposed Reg. B.I. and draft Model 275
 - Returned to the working group for additional work
- June 2019 – NAIC request for comments:
 - If the model were to require “best interest” as the appropriate standard of conduct, how should “best interest” be defined in order to provide an objective standard for compliance by industry and for regulatory oversight?

NAIC Status

- June 2019 – SEC approved a final Reg. B.I.
- June 20, 1019 – Working group met to level set and flesh out “Best Interest”

NAIC Best Interest Framework*

- Disclosure obligation
- Care obligation
- Conflict of Interest obligation
- Documentation obligation
- Supervision System

*Current draft of the NAIC working group

NAIC Current Request for Comments

- 1) What constitutes a material conflict of interest and how should an insurer and/or producer avoid or otherwise reasonably manage that conflict?
- 2) When reviewing a producer's recommendation, should the producer be compared to "an ordinary producer in a similar circumstance" or should they be compared to what "a producer familiar with such matters" would recommend?

NAIC Current Request for Comments

- 3) There is general agreement that a recommendation must be documented, including the basis or bases of the recommendation; However, there still needs to be discussion on whether, during the sales process, the recommendation can given to the consumer during the sales process can simply be done orally and include the basis for the recommendation, but not detailed analysis.

Other Issues / Developments

- **Is a “fiduciary duty” coming? Something else?**
 - Massachusetts, New Jersey, Nevada
- **Preemption Battles – Federal vs. State law**
- **DOL Rule Redux**
- **House efforts to block funding for SEC’s Reg. B.I.**

Questions?

Of course you have questions!

Stay tuned.....