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October 1, 2019

The Honorable Jillian Froment
Director, Ohio Department of Insurance
Chair, NAIC Annuity Suitability Working Group

Re: 9/17/19 Draft of Proposed Revisions to the Suitability in Annuity Transactions Model Regulation

Dear Director Froment:

These comments are submitted on behalf of the undersigned trade groups (Joint Trades) in response to the National Association of Insurance Commissioners (NAIC) Annuity Suitability Working Group (Working Group) September 17, 2019 draft of proposed revisions to the Suitability in Annuity Transactions Model Regulation (Model Regulation) (9/17/19 Draft). We remain committed to a harmonized best interest standard of care for annuities across all regulatory platforms that enhances protections for consumers seeking guaranteed lifetime income in retirement. We appreciate the efforts of the Working Group to achieve such harmonization reflected in the 9/17/19 Draft.

Our members support a transactional best interest standard of conduct for recommendations of annuities that will provide a clear objective standard for compliance and regulatory oversight of best interest obligations under the Model Regulation. Accordingly, we support the 9/17/19 Draft's proposed new framework for the Model Regulation that would require financial professionals to "act in the best interest of the consumer" by complying with four "buckets" of obligations (care, disclosure, conflict of interest, and documentation obligations). This framework is in broad alignment with the Securities and Exchange Commission (SEC) Regulation Best Interest (Reg BI), which we believe will go a long way toward ensuring a harmonized standard of care across all regulatory platforms.

While the 9/17/19 Draft provides a strong framework and aligns well with SEC Reg BI in many key respects, we do have some concerns with the 9/17/19 Draft that are explained below and

addressed in the attached "redline" of the 9/17/19 Draft.[1] Our comments cover several key points, which we will explain below. In addition, we have suggested several technical changes in the redline and we can provide more detail and explanation as needed.

Section 1. Purpose

We have proposed modifications this Section to clarify that the required standard of conduct does not guarantee an outcome. This language is included in New York's Regulation 187, and we believe it would be appropriate to include this important clarification in the Model Regulation as well.

> We have added a sentence to Section 1(A) that reads: *The best interest standard set forth in this regulation requires a producer to adhere to a standard of conduct but does not guarantee an outcome.*

Section 4. Exemptions

We have suggested deleting language regarding a specific exemption for certain direct response solicitations. We believe that this amended Model Regulation is intended to apply only to solicitations where there is a recommendation.

> Section 4(A) reads: ~~*Direct response s*~~ *Solicitations, sales or purchases of an annuity where there is no recommendation* ~~*based on information collected from the consumer pursuant to this regulation based on information collected from the consumer pursuant to this regulation.*~~

Section 5. Definitions

<u>"Consumer Profile Information"</u>

We are suggesting three modifications to this definition. We have deleted paragraphs (3) and (5) as the language used was duplicative of the language used earlier in the definition. We have also deleted the final phrase in paragraph (11) (~~*including variability in premium, death benefit or fees*~~) because we have added a definition of "Non-guaranteed elements" (see below).

<u>"Material conflict of interest" and "Non-cash compensation"</u>

We agree with the construct that the Working Group has suggested with these definitions. We have suggested modifications to Section 5(I)(2) and Section 5(J) for clarity.

> Section 5(I)(2) reads: *"Material conflict of interest" does not include cash compensation or non-cash compensation. <u>"Material conflict of interest" also does not include health insurance, office rent, office support, retirement benefits, or employee benefits provided to employees (including, but not limited to, statutory employees)</u>."*
>
> And Section 5(J) reads: *"Non-cash compensation" means any form of compensation that is not cash compensation, including, but not limited to, <u>merchandise, gifts, prizes, travel</u>*

[1] Please note that for ease of review, we started with the 9/17/19 Draft, "accepted" all changes marked in that draft and then added our comments against that "clean" document.

expenses, meals, and lodging. "Non-cash compensation" does not include health insurance, office rent, office support, retirement benefits, or employee benefits provided to employees (including, but not limited to statutory employees)."

"Non-guaranteed elements"

As mentioned, above, we have suggested adding a new definition, "Non-guaranteed elements." In the interest of ensuring consistency across NAIC model regulations, this definition is taken directly from the NAIC Annuity Disclosure Model Regulation.

> *"Non-guaranteed elements" means the premiums, credited interest rates (including any bonus), benefits, values, dividends, non-interest based credits, charges or elements of formulas used to determine any of these, that are subject to company discretion and are not guaranteed at issue. An element is considered non-guaranteed if any of the underlying non-guaranteed elements are used in its calculation*.

"Recommendation"

We are suggesting a modification to simplify and clarify that the recommendation is the advice provided, while at the same time ensuring that the requirements of the Model Regulation apply regardless of the result of the advice being given.

> As amended in the redline, Section 5(L)[2] reads: *"Recommendation" means advice provided by a producer to an individual consumer ~~that was intended to result or does results into a~~ to purchase, ~~an~~ exchange or ~~a~~ replace~~ment of~~ an annuity in accordance with that advice.*

Working Group Request for Comments on the definition of "Recommendation"

Whether the Draft Should Address In-force Sales.

The Joint Trades strongly urge the Working Group not to modify the definition of "Recommendation" or make any other modification to the Model Regulation to extend its requirements to in-force annuity transactions or transactions beyond the purchase, exchange or replacement of an annuity. We are concerned that doing so will have a detrimental impact on consumers and could negatively impact access to affordable products and information about annuities.

First, owners of annuities can act on contractual provisions without a recommendation and it is likely to be difficult, if not impossible, for an insurer to prohibit a consumer from exercising a contractual right. Recommendations could have been made many years previously at the time of sale of the contract, such as, a recommendation to consider adding a rider at year 6 of the contract to generate income; making additional purchase payments; re-allocating investment allocations under variable annuity contracts and certain fixed index annuity contracts; withdrawing cash value from an annuity contract; adding, replacing or terminating riders under an annuity contract; and modifying beneficiaries. The client is then free to take future action on his/her own without meeting with a

[2] In the renumbered document, it is Section 5(M).

producer again. Additionally, there are instances where a customer has provided prior express authorization for certain types of transactions and many transactions are implemented directly by the consumer online or through the mail, as permitted by the consumer's contract, with no producer or insurer involvement.

Customers that we serve could very likely react disapprovingly if a producer or insurer performs a best interest review, when the customer is simply contacting the insurer or producer in an effort to exercise a contractual right. We are unaware of any reports or allegations of consumer harm arising out of recommendations of in-force transactions that could not be effectively regulated under existing rules.

Second, logistically, it is difficult to determine whether a recommendation was made to an existing client for an in-force contract at the producer level (because insurers often are not involved in those conversations with clients) or to differentiate between in-force transactions that are or are not subject to the requirements of the Model Regulation. This could delay processing a request and possibly harm the client. Such a delay could also jeopardize compliance with certain legal requirements, such as same day pricing rules under the federal securities laws. We do not believe it is reasonable to expect insurers to investigate every customer-initiated in-force transaction to determine if a recommendation was made. Additionally, most annuity contracts would not permit the insurer to reject or delay a requested transaction while it attempts to determine whether the transaction was recommended.

Third, extension to in-force transactions would necessitate fundamental structural modifications to the Model Regulation and would create significant operational challenges.

It is unlikely that the insurer could obtain all the necessary documentation, including the consumer profile information, from the producer to fulfill its supervisory duties under Section 6.(C). After its supervisory review, if the insurer determines that the transaction does not effectively address the consumer's financial situation, insurance needs, and financial objectives, it will be difficult for the insurer to determine how to properly unwind the transaction, particularly if the consumer was exercising existing contractual rights.

Last, application of the Model Regulation to in-force transactions would undercut the fundamental concept set forth in Section 6.A.(1)(i) that the Model Regulation does not create an "ongoing monitoring obligation."

For these reasons, we respectfully recommend that the Working Group refrain from expanding the scope to in-force transactions. [3]

[3] However, if the Working Group ultimately concludes to extend the Model Regulation to in-force annuity transactions, we strongly urge the Working Group to conduct a detailed review of the 9/17/2019 Draft to map out the obligations on insurers and producers if the Model Regulation were to apply to different types of post-issuance recommendations. We strongly believe a different standard of conduct should be applied to in-force transactions than the best interest standard laid out in the Model Regulation applicable to new sales transactions.

Whether to Include a Timeframe for Review of a Consumer's "Consumer profile information"

We urge against inclusion of a required timeframe for review of a consumer's "Consumer profile information." The producer already is required to request consumer profile information in connection with a recommendation and to have a reasonable basis to believe the recommended annuity would effectively address the consumer's financial situation, insurance needs, and financial objectives in light of the consumer's consumer profile information.

We note that the impetus for the Working Group to explore the possibility of a requirement for the periodic review of the profile information appeared to be federal securities law requirements applicable to broker-dealers. Under SEC Rule 17a-3(a)(17) of the Securities Exchange Act of 1934, there is a requirement to "furnish" the broker-dealer customer, no less than every 36 months, the customer's account record information that is on file. The furnishing requirement does not, however, apply if there have been no recommendations related to the account during the preceding 36 months.

For these reasons, we recommend that the Model Regulation not include an additional provision specifying a time frame for a producer's review of the consumer profile information.

Section 6. Duties of Insurers and Producers

Our members broadly support the intent and construction in Section 6. We appreciate the effort that the Working Group made in crafting this section. We offer a few suggestions.

> We have recommended the addition of a phrase to the last sentence of Section 6(A) so the sentence reads: *A producer is deemed to comply with this subsection by satisfying the following obligations regarding care, disclosure, conflict of interest and documentation, independent of the performance of the recommended annuity:*

Section 6.A. (1) Care Obligation

We have made four suggestions for modifications to Section 6(A)(1).

- The suggested change to Section 6(A)(1)(a)(ii) is a technical correction to clarify the language.
- The suggested changes to Section 6(A)(1)(a)(iii) have two purposes. We have suggested deleting, "over the life of the contract" as we are concerned that that could be interpreted as requiring an on-going duty. We have added "provided to the producer" to make clear that producers can only evaluate the information they actually receive from consumers.
- The suggested change in Section 6(A)(1)(j)(ii) is to delete the word, "substantially." Use of that word is inconsistent with the standard in Sections 6(A)(1)(iii) ("recommended option effectively addresses") and Section 6(A)(f) ("the consumer would benefit"). We also believe

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Further, we recommend that the extension be limited to situations where: (i) the consumer exercises a contractual right under an existing annuity contract at the recommendation of the producer; and (ii) the producer receives new sales compensation, that is separate and distinct from compensation provided to a producer when, after, the initial premium or deposit under an annuity, the consumer pays further premiums or deposits pursuant to the annuity.

that word to be too subjective. We further note that replacement transactions would also continue to be subject to the existing requirements under the NAIC Life Insurance and Annuities Replacement Model Regulation.

- The suggested change in Section 6.A.(1)(j)(iii) is to bring the time frame closer in line to the current replacement requirements in most states.

In addition to these suggested changes, our members have asked what information the regulatory community is expecting the producer to share or gather with the use of the phrase, "characteristics of the insurer" in Section 6(A)(1)(e). We believe that producers can consider, for example, factors such as reputation, service record and financial strength.

Section 6.A.(2) Disclosure Obligation

We have suggested adding a new paragraph (v) to Section 6.A.(2)(a) that requires the disclosure of any material conflict of interest, in alignment with Reg BI. We have suggested a conforming change be made to Appendix A.

We have also suggested several additional technical, clarifying changes to Section 6.A.(2) and (3).

Working Group Request for Comments – "Materially Participated"

The Joint Trades are concerned that the proposed language rendering the Model Regulation applicable to any producer who "materially participated" in the transaction is too vague, and will create too much uncertainty in the marketplace as to when a producer is considered to have "materially participated" in a transaction and thus is subject to the Model Regulation. The articulated purpose for the provision was to ensure that more senior producers were not shielding themselves from responsibility by using junior producers to technically make a recommendation. The Joint Trades believe that a state insurance regulatory authority will always have jurisdiction over, and ample tools to sanction, a senior producer in those circumstances without needing to rely on this provision. The Joint Trades urge that this language not be included in the Model Regulation.

Section 6.B. – Transactions not based on a recommendation

We have suggested reverting to the language in Section 6.B.(1) to the language in the current version of the Model Regulation. We are concerned that the proposed changes to this subsection would inadvertently deprive insurers of the relief intended to be granted by this provision under the specified circumstances even if a producer is involved.[4]

Section 6.C. Supervision system

We have proposed modifying deleting Section 6.C.(1) entirely as the substance of that paragraph is covered in following paragraph and subparagraphs.

[4] The definition of "producer" includes an insurer only "where no producer is involved."

We have modified Section 6. C.(2). Many producers are appointed with multiple insurers. An insurer does not have the requisite knowledge or control over a producer to gauge the producer's compliance with the requirements of subsection A and the other specified subsections in connection with other insurers' products.

In addition, consistent with our modification to Section 1.A., we added a sentence to the end of Section 6.C.(2)(e) to make it clear the insurer is not required to warrant the producer is acting in the consumer's best interest.

Finally, we also have proposed modifying Section 6.C.(2)(e) to more precisely reference the standard we believe insurers' supervision system can and should be expected to satisfy. Specifically, we have modified subparagraph (e) to read:

> *The insurer shall establish and maintain reasonable procedures to detect recommendations ~~that~~ where there is not a reasonable basis to determine the recommendation would effectively address the particular consumer's financial situation, insurance needs and financial objectives ~~are not in compliance with subsections A, B, D and E~~. This may include, but is not limited to, confirmation of the consumer's 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 the consumer profile information after issuance or delivery of the annuity. An insurer is not required to warrant the producer is acting in the consumer's best interest*;

We urge that subparagraph (f) be deleted. When a producer is engaged in activities relating to the sale of other insurers' products, an insurer does not have the requisite knowledge or control over the producer to gauge compliance with the disclosure requirements of Section 6.A.(2). Moreover, Section 8, as proposed to be modified below, provides that an insurer is responsible for compliance with the disclosure and other requirements of the Model Regulation by producers who sell the insurer's products.

We have suggested changes to subparagraph (h). Our purpose is to:

(i) Make it applicable to sales contests etc. based on the sales of specific annuities of the insurer. We eliminated the reference to "specific types of annuities" as that may be overly broad as applied in the context of annuities. We clarified the section only applies to the insurer as the insurer does not have control over the business of third party entities; and

(ii) In line with SEC Reg BI, clarify the requirements of this section (a) do not apply to compensation practices based on total annuity products sold; (b) would not prevent the offering of proprietary products, placing material limitations on the menu of products or incentivizing the sale of such products through its compensation practices, so long as the incentive is not based on the sale of a specific annuity product of the insurer within a limited period of time; and (c) are not intended to prohibit the receipt of employee benefits by employees.

As modified, subparagraph (h) reads: *The insurer shall establish and maintain reasonable procedures to identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation provided by the insurer that are based on the sales of specific annuities ~~or specific types of annuities~~ within a limited period of time; ~~and~~ the requirements of this subsection: (i) do not apply to compensation practices based on total annuity products sold; (ii) would not prevent the offering of only proprietary products, placing material limitations on the menu of products or incentivizing the sale of such products through its compensation practices, so long as the incentive is not based on the sale of a specific annuity product of the insurer within a limited period of time; and (iii) are not intended to prohibit the receipt of health insurance, office rent, office support, retirement benefits or employee benefits by employees (including, but not limited to statutory employees).*

Section 7. Producer Training

We added a new subparagraph to account for producers who have had required training before the effective date of the amended Model Regulation.

As modified, the paragraph reads: *A producer who has completed an annuity training course approved by the department of insurance prior to [insert effective date of amended regulation] shall, within six (6) months after [insert effective date of amended regulation], complete either:*

(a) a new four (4) credit training course approved by the department of insurance after [insert effective date of amended regulation], or

(b) an additional one-time one (1) credit training course approved by the department of insurance and provided by the department of insurance-approved education provider on appropriate sales practices, replacement and disclosure requirements under this amended regulation.

Section 8. – Compliance Mitigation: Penalties

We have proposed modifying Section 8.A. to clarify that insurers only are responsible for the action or inaction of our producers "in connection with the insurer's annuity products" and not for activities relating to the sale of another insurer's products over which the insurer has no control.

As modified: *An insurer is responsible for compliance with this regulation by the insurer and the producer in connection with the insurer's annuity products. If a violation occurs, either because of the action or inaction of the insurer or its producer, the commissioner may order:*

Appendix A – Producer Relationship Disclosure Form

Our members generally support the creation of this document. As requested, we have offered some initial changes in our submitted redline. We do urge: 1) the elements of this disclosure be finalized after the content of the amended Model Regulation is finalized; 2) that regulators and interested

parties work with together to make the document more readable, approachable and meaningful for our customers; and 3) the Working Group to consider combining Appendix A and Appendix B.

The Joint Trades appreciate and thank the Working Group for its continued consideration of our concerns and would be glad to answer questions relating to any of the above. We worked diligently with our members to provide meaningful input within the deadline. We may have additional thoughts that we will share, as appropriate and as time permits.

Regards,

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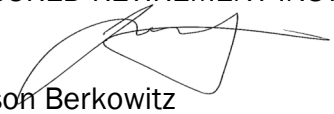

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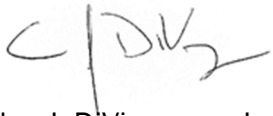

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