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VIA EMAIL

SUBJECT: Suggested Amendments to the Suitability in Annuity Transactions Model Regulation (#275)

Dear Ms. Matthews:

The California Department of Insurance ("CDI") appreciates the opportunity to suggest amendments to the Suitability in Annuity Transactions Model Regulation. Attached please find a redline version of the Model Regulation.

The Working Group should extend this Model Regulation to the sales of life insurance. If the Working Group declines to do so, CDI recommends that permission be requested of "A" Committee to draft a model regulation that covers suitability in the sales of these products. The comments below do not include proposed language that would be necessary if life insurance was to be covered by this Model Regulation.

The Working Group should draft amendments to the Model that provide stronger consumer protections than those afforded by the SEC's draft "Regulation Best Interest", which is in the ninety (90) day comment period. Given the questions that the SEC requested comment on, it is probable that the final version of the SEC's regulation will provide more robust consumer protections than those set forth in the initial draft.

CDI notes that merely requiring disclosure of conflicts of interest is not the same as requiring a true best interest standard. It would be harmful to consumers to permit producers and insurers to tout that they are following a best interest standard when they are merely disclosing conflicts of interest.

Section 1 Purpose
This section should be amended to make clear that recommendations made to consumers must be in the consumers' best interest.

Section 2 Scope
Subsection A. should be amended to state it applies to insurers that make recommendations. Per California Insurance Code § 10509.911, a new subsection B. should be added to make clear that the Model regulation does not interfere with existing laws.

Section 4 Exemptions
The exemptions should be amended so that the Model Regulation applies in instances where producers solicit individual employees to purchase annuities which are offered as part of one or more of the enumerated retirement saving plans. Excluding these plans would only make sense when there is an employer with a fiduciary obligation actually looking out for employees. Articles published in the New York Times raise concerns about sales by individual agents of 403(b) annuities to teachers. Although it is not clear whether any of those plans are covered by ERISA, similar issues may arise regarding the enumerated plans in situations where individual producers meet with employees to recommend purchasing annuities as a means to save for retirement. Here are links to two of the articles for your review.

https://www.nytimes.com/2016/10/23/your-money/403-b-retirement-plans-fees-teachers.html

https://www.nytimes.com/2016/10/27/your-money/403-b-retirement-plans-teachers-brokers-fees.html

Section 5 Definitions
1. CDI proposes definitions of the following terms: "Best interest"; "Compensation"; "Intermediary"; "Material conflict of interest"; and "Non-cash compensation".

2. The term "Recommendation" should be broadened to also include guidance and information. Additionally, this definition should apply to insurers, regardless of whether a producer is involved.

3. The term "Replacement" should be amended to apply to insurers, regardless of whether a producer is involved per California Insurance Code §10509.913(h).

4. The term "Suitability information" should be amended and broadened to include a best interest requirement and other amendments. Two additional suitability factors should be added to the list per California Insurance Code §10509.913 (i)(13) and (14):

    (14) Whether or not the consumer has a reverse mortgage;

    (15) Whether or not the consumer intends to apply for means tested government benefits, including, but not limited to, Medicaid or the veterans' aid and attendance benefit.

   Proposed subsections (14) and (15) are important because people who obtain a reverse mortgage on a home and those who need to apply for Medicaid or the Veterans' Aid and

Attendance program generally need access to their funds; they should not "lock up" their money in long term annuities. Further, some unscrupulous agents tie up veterans' assets in annuities in order to qualify them for the Veteran's Aid and Attendance Program. This is inappropriate both because the Veteran's Aid and Attendance Program is intended for low income veterans and because this practice artificially impoverishes veterans who would be better off having access to their funds.

Section 6 Duties of Insurers and of Insurance Producers

1. Subsection A. should be amended: (a) for clarity; (b) to be applicable to insurers regardless of whether a producer is involved; (c) to include a best interest standard; and (d) to require that the producer and insurer, in recommending an annuity, take into account other pertinent information regarding the consumer about which the producer and/or insurer becomes aware, for example, health concerns.

2. Subsection A. (2) is problematic and should be amended. There will almost always be certain features of an annuity, like tax-deferred growth, that would benefit a consumer. Just because an annuity has a few features that a consumer would benefit from doesn't mean purchasing that annuity would be suitable or in the consumer's best interest. The standard set forth in this subsection is simply too low. California Insurance Code § 10509.914(a) (2), which became effective in 2012, requires that the consumer receive a tangible net benefit from the transaction. California's standard is more appropriate to a best interest standard. Accordingly, CDI recommends adopting this requirement.

3. Regarding subsection A. (4) (c), a higher standard of care requires a longer "look back" period than 36 months because it affords greater consumer protection. Both a previous version of the Model Regulation and the November 2017 draft contained a 60 month "look back" period. There should be a "look back" period of at least 60 months.

4. A new section "C" should be added. It will prohibit producers and insurers from recommending the purchase of a replacement annuity where purchase of the replacing annuity, when compared to the existing annuity, does not confer a substantial financial benefit over the life of the policy to the consumer so that a reasonable person would believe the purchase is unnecessary. In California, this requirement has applied to annuity replacement sales to senior citizens since 2004. (California Insurance Code §§ 10509.8 and 10509.914(c) As part of requiring a higher standard of care, this requirement should be made part of the Model Regulation and expanded to be applicable to all replacement sales, regardless of the consumer's age.

5. The current subsection C. should be amended and re-lettered as "D.". Suggested amendments include a requirement that the producer explain to the consumer that the suitability information is required because it is important to determine whether the purchase of an annuity would be suitable and in the consumer's best interest. If the consumer revealed his or her suitability information to the producer, the producer and/or consumer must complete the suitability form to allow the insurer to confirm the producer's determination.

6. As currently written, the requirements of subsection D. (CDI's proposed subsection "E") are too weak. CDI often brings enforcement cases in which the agent falsely claims to have made no recommendation and/or the consumer refused to provide his/her suitability information. Subsection D. provides unscrupulous agents with an easy way to avoid providing the insurer with suitability requirements without the insurer realizing that it was the agent and not the consumer who did not want to reveal the consumer's suitability information. A "best interest" standard requires closing this loophole. California Insurance Code § 10509.914 provides stronger consumer protections than does the Model Regulation by requiring that the insurer's issuance of an annuity subject to paragraph (1) "be reasonable under all circumstances actually known, or which, after reasonable inquiry, should be known to the insurer or the insurance producer at the time the annuity is issued". This requirement should be included in subsection (2). Additionally, given the circumstances presented in subdivision D. (1)(a), (c), and (d), a provision should be added requiring that prior to issuing the annuity in those situations, the insurer must follow up with the consumer by sending the consumer a suitability questionnaire. The consumer must either complete the suitability questionnaire or write on the questionnaire a short sentence confirming that this purchase fits within the applicable scenario listed in D. (1) (a), (c), or (d). Alternatively, the insurer could call the consumer and discuss this matter with him or her.

7. Per Iowa's proposed revisions to the November 2017 draft, Subsection E. (CDI's subsection "F") should be amended to require that the producer disclose limitations on his or her ability to sell a variety of annuities. Also included is a requirement for written verbal and disclosure of material conflicts of interest as well as a requirement that a writing be provided explaining why the annuity is suitable and in the consumer's best interest.

8. Section F. should be amended as follows.

(a) Section F. (1)(d) should be amended to include a best interest standard and require that the insurer's selection criteria for heightened review include whether the applicant is a senior citizen. Most of the complaints we receive regarding unsuitable sales and replacements of annuities come from senior citizens. This group of consumers often need ready access to their money, and they lack time to make up for poor investment decisions.

(b) Section F. (2)(a) should be amended per California Insurance Code § 10509.914 (f)(2)(A) to make clear that the insurer is responsible for the compliance of its insurance producer with the provisions of this regulation regardless of whether the insurer contracts for performance of a function required under this subdivision and regardless of the insurer's compliance with subparagraph (b).

(c) Section F. (2)(b) should be amended to make clear that "reasonable" "supervision" and "monitoring" are required as per California Insurance Code § 10509.914 (f)(2)(B).

9. Per Iowa's suggestion regarding the November 2017 draft, Section F. should be augmented by adding a new subsection that requires "insurers to maintain reasonable procedures to ensure producers adequately disclose information as required by this regulation."

10. Subsection G. should be moved to a new "Prohibited Practices" section and amended to be applicable to both producers and insurers, in keeping with California Insurance Code § 10509.914 (g).

11. Subsection H. (FINRA carve-out) should be further discussed by the Working Group since the SEC has recently proposed a best interest regulation that will likely be amended. FINRA standards should, at a minimum, provide at least the same level of consumer protections set forth in the NAIC Model Regulation. Further, per California Insurance Code § 10509.914 (h)(2), an additional sentence should be added that states: "Except as provided in paragraphs (1) and (2), all other provisions of this Model Regulation remain applicable to these broker-dealer sales."

Proposed New Section 7 Prohibited Practices
A "Prohibited Practices" section should be added that includes the prohibition in Section G. This new section should also prohibit recommending replacements of variable annuities and other investments if the producer is unauthorized to sell them. Making material misrepresentations and omissions should also be prohibited. Further, receiving compensation based on target sales levels and basing recommendations on incentives rather than acting in the consumer's best interest should not be permitted.

Section 7 (Proposed as Section 8) Insurance Producer Training
1. California requires that all producers who want to sell annuities take a one-time eight credit-hour training course and satisfactorily complete four continuing education credits prior to license renewal every two years. (California Insurance Code § 1749.8) A drafting note should be added that permits States to require additional course hours as their laws require.

2. The Working Group should consider the following amendments to the training topics.

    a. Subsection B. (2), should include an additional sentence permitting States to require insurance producers to comply with additional continuing education requirements regarding annuities prior to license renewal. California requires four hours of additional continuing education on annuities prior to license renewal. (California Insurance Code § 1749.8(b))

    b. At subsection B. (3)(c), the Model Regulation requires training on "How product specific annuity contract features affect consumers". (California Insurance Code § 10509.915(b)(3)(C)) requires that producers receive training on: "How fixed, variable, and indexed annuity contract provisions affect consumers". I propose that this subparagraph of the Model Regulation be amended to use the more specific language set forth in California law.

c. The topics should be augmented to include that set forth in California Insurance Code § 10509.915(b)(3)(F), which requires that producers receive training on:

> Prohibited sales practices, the recognition of indicators that a proposed insured may lack the short-term memory or judgment to knowingly purchase an insurance product, and fraudulent and unfair practices…for sales of annuities…

This topic should be set forth in a new subsection (3)(g).

3. California law does not include a "deemer" provision applicable to training taken in another state. California requests that subparagraph B. (8) be deleted or a drafting note be added stating that individual States should determine whether to allow another State's training requirements to satisfy the State's training requirements.

Section 8. (Proposed as Section 9) Compliance Mitigation; Penalties

1. Section A. should be amended per California law to permit the commissioner to take the actions listed in this portion of the Model Regulation, "in addition to any other available penalties, remedies, or administrative actions". The Commissioner should retain authority to obtain any penalties and remedies available, including those additional to the ones stated in the Model Regulation.

2. Subparagraph A. (2) uses the terms "general agency" and "independent agency". These terms are not defined in the Model Regulation. California law uses the term "managing general agent". The terms "general agency" and "independent agency" are neither defined in the Model Regulation, nor used in the California Insurance Code. The Working Group should consider amending this subparagraph to delete the term "independent agency" and instead use the term "production agency through which the producer transacts…"

4. For States that must adopt this Model Regulation via legislation rather than regulation, A drafting note should be added for States that enact this Model Regulation via legislation to authorize the Commissioner to adopt reasonable rules and regulations, and amendments and additions, as are necessary to administer this Regulation.

Sincerely,

Jodi S. Lerner

Jodi S. Lerner
Attorney

CA Department of Insurance's Proposed Edits
May 7, 2018

SUITABILITY IN ANNUITY TRANSACTIONS MODEL REGULATION

Table of Contents

Section 1. Purpose

A. The purpose of this regulation is to require insurers to establish a system to supervise recommendations and to set forth standards and procedures for recommendations to consumers *that are suitable, 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

A. This regulation shall apply to any recommendation to purchase, exchange or replace an annuity made to a consumer by an insurance producer~~,~~ or an insurer ~~where no producer is involved,~~ that results in the purchase, exchange or replacement recommended.

B. *Nothing in this act shall be interpreted to preclude, preempt, or otherwise interfere with the application of any other laws of this state that may apply in any matter involving the sale of an annuity that is subject to this article.*

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~~ *Annuities that are not individually solicited and are* 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;

C. ~~(5)~~ Settlements of or assumptions of liabilities associated with personal injury litigation or any dispute or claim resolution process; or

D. ~~(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 offered; sold; issued; and delivered, acting with the reasonable diligence, care, skill and prudence, that a reasonably prudent person acting in a like capacity and familiar with such matters would act, and in a manner that puts the interest of the consumer first and foremost and will not result in the producer or insurer receiving in excess of reasonable compensation.*

(2) *"Best interest" does not require that 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 require that the recommendation is the single "best" annuity product available in the marketplace at the time of the annuity transaction. However, as part of acting in the consumer's best interest in compliance with subparagraph B. (1) above, if the producer and/or insurer recommend the purchase of an annuity, the annuity recommended and issued must be the best annuity for the consumer's circumstances that the insurance producer is authorized to sell and the insurer offers, taking into consideration the consumers' suitability information; the price; and annuity contract terms, including but not limited to the fees, interest rate, surrender charge period, riders, and other information that is known or should be known by the producer or insurer.*

C. *"Compensation" means any discount, concession, service fee, commission, sales charge, loan, override, or cash benefit or other remuneration received in connection with the solicitation, negotiation, recommendation or sale of an annuity."*

~~C.~~*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].

~~D.~~*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].

~~E.~~*F.* "FINRA" means the Financial Industry Regulatory Authority or a succeeding agency.

~~F.~~*G.* "Insurer" means a company required to be licensed under the laws of this state to provide insurance products, including annuities.

~~G~~*H.* "Insurance producer" means a person required to be licensed under the laws of this state to sell, solicit or negotiate insurance, including annuities.

~~H.~~*__I.__* *__"Intermediary" means an entity contracted with the insurance company to facilitate a producer's and/or insurer's sale of an annuity.__*

~~I.~~*__J.__* *__"Material conflict of interest" means:__*

__(1)__ *__A financial interest of an insurance producer and/or the insurer that a reasonable person would expect could effect the ability of the producer and/or insurer to: (1) exercise his/hers/its best judgment and (2) put the consumer's interests before the producer's and/or insurer's own interest.__*

__(2)__ *__"Material conflict of interest" includes financial incentives or rewards available to; 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. It also includes non-cash compensation available to, offered to, or received by a producer or intermediary as a result of meeting target sales levels.__*

~~J.~~*__K.__* *__Non-cash compensation" means any form of compensation that is not cash compensation, including but not limited to, merchandise, gifts, tickets to paid events, prizes, travel expenses or meals and lodging.__*

~~G.~~*__L.__* "Recommendation" means advice*__, guidance, or information__* provided by an insurance producer, or an insurer ~~where no producer is involved~~, to an individual consumer that results in a purchase, exchange or replacement of an annuity in accordance with that advice*__, guidance, or information__*.

~~H~~M. "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~~ *__whether or not a__* producer *__is involved__*, that by reason of the transaction, an existing policy or contract has been or is to be *__any of the following__*:

(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.

~~I.~~*__N.__* ~~"Suitability information" means information that is reasonably appropriate to determine the suitability of a recommendation, including the following:~~
"Suitability information" means information that is reasonably appropriate to determine *__whether__* ~~the suitability of~~ a recommendation __is suitable and in the best interest of the consumer__, including the __all of the following__…"

(1) Age;

(2) Annual income;

(3) Financial situation and needs, including the financial resources used for the funding of the annuity;

(4) Financial experience *__and knowledge__*;

(5) Financial objectives;

(6) Intended use of the annuity;

(7) Financial time horizon, *including the duration of existing liabilities and obligations*;

(8) Existing assets *and* ~~or~~ *financial products,* including investments**, annuities** and life insurance holdings;

(9) Liquidity needs;

(10) Liquid net worth;

(11) Risk tolerance; and

(12) Tax status.

(14) Whether or not the consumer has a reverse mortgage;

(15) Whether or not the consumer intends to apply for means tested government benefits, including, but not limited to, Medicaid or the veterans' aid and attendance benefit.

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 ~~have reasonable grounds for believing that the recommendation is suitable for~~ *make only suitable recommendations that are in the best interest of* the consumer *at the time the recommendations are made. These recommendations shall be based* on ~~the basis of~~ 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~~,~~ *and other relevant information about the consumer about which the insurance producer or insurer becomes aware,* and ~~*that*~~ there ~~is~~ *must be* 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;

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 consumer would receive a tangible net benefit from the transaction.

(~~3~~*4*) 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 case of an exchange or replacement, the transaction as a whole is suitable) for the particular consumer based on his or her suitability information; and

(4*5*) In the case of an exchange or replacement of an annuity, the exchange or replacement is suitable 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 from product enhancements and improvements; and

(c) The consumer has had another annuity exchange or replacement and, in particular, an exchange or replacement within the preceding ~~36~~ *60* months.

B. Prior to the execution of a purchase, exchange or replacement of an annuity resulting from a recommendation, an insurance producer, or an insurer where no producer is involved, shall make reasonable efforts to obtain the consumer's suitability information.

C. *The producer or insurer if no producer is involved shall compare the annuity that is to be replaced or exchanged with the replacing annuity to determine whether the proposed transaction would be in the consumer's best interest. Except as permitted under subdivision (D) below, an insurer shall not issue an annuity recommended to a consumer unless there is a reasonable basis to believe the annuity is suitable and in the consumer's best interest based on the consumer's suitability information and other information about which the producer and/or insurer may become aware. The preceding sentence and subdivision (D) notwithstanding, neither a producer nor an insurer shall recommend the sale of an annuity to replace an existing annuity where purchase of the replacing annuity does not confer a substantial financial benefit over the life of the policy to the consumer, so that a reasonable person would believe the purchase is unnecessary.*

~~C~~.*D.* *If it appears that the consumer does not want to provide the suitability information, the producer shall explain that the suitability information is required because it is important to the determination of whether the purchase of an annuity would be suitable and in the consumer's best interest. If the consumer revealed that information to the producer, the producer and/or consumer must complete the suitability form to allow the insurer to confirm the producer's determination.* Except as permitted under subsection ~~D~~ *E,* an insurer shall not issue an annuity recommended to a consumer unless there is a reasonable basis to believe the annuity is suitable based on the consumer's suitability information.

~~D~~.*E.* (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 C related to any annuity transaction if:

(a) No recommendation is made;

(b) A recommendation was made and was later found to have been prepared based on materially inaccurate information provided by the consumer;

(c) A consumer refuses to provide relevant suitability information and the annuity transaction is not recommended; or

(d) A consumer decides to enter into an annuity transaction that is not based on a recommendation of the consumer 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*, or which after reasonable inquiry, should be known* to the insurer *or insurance producer* at the time the annuity is issued.

(3) *If any of the situations set forth in subparagraphs (1)(a); (c); or (d) occur, prior to issuing the annuity, the insurer shall send by email or United States mail the consumer a product suitability form with a cover letter that states that in order to ensure that the consumer is purchasing an annuity which is in the consumer's best interest, the insurer is requesting the consumer's suitability information. If the consumer refuses to complete the suitability form, the consumer must write on the form:*
"I refuse to complete this questionnaire and want to purchase the annuity which was not recommended by the insurance agent."

The insurer is prohibited from issuing the annuity until it receives a response to its mailing from the consumer or speaks with the consumer to verify that the consumer refuses to provide the suitability information. If the insurer speaks with the consumer to verify that the consumer refuses to provide the suitability information, the insurer must make a written record of the discussion with the consumer.

~~E.~~*F.* An insurance producer or, *insurer* where no insurance producer is involved, ~~the responsible insurer representative,~~ shall:

(1) *At the time of making the recommendation, disclose to the consumer any and all limitations the producer or the insurer has regarding:*

(a) *The type of financial products, including annuities, that can be provided;*
(b) *Whether only the products of specified insurers can be offered;*
(c) *The scope of the services provided; and*
(d) *The scope of the producer's licenses.*

(2) *At the time of making the recommendation and completing the application, disclose to the consumer verbally and in writing, any and all material conflicts of interest, including:*

(a) *That the producer will receive a commission or fee for the sale of the annuity; the amount of the commission or fee and if applicable, the amount of all other cash compensation that may and/or will be received as a result of entering into a contract for services for advice and/or for the sale of the recommended annuity; and all non-cash compensation that is available and/or may and/or will be received. The required written disclosure shall be set forth in a separate standalone document that is no more than two pages in length and is written in plain language in 14 point font and is left with the consumer when the application is signed.*

(~~1~~3) Make a record of any recommendation subject to section 6A of this regulation~~;~~*. This writing shall contain an explanation of the reasons the recommendation is suitable and in the consumer's best interest, including the assumptions and analysis that led to the determination. The required written disclosure shall be set forth in a separate standalone document that is no more than two pages in length and is written in plain language in 14 point font A copy of this writing must be left with the consumer at the time the application is signed and a copy must be provided to the insurer;*

(~~2~~4) *If applicable*, ~~Obtain~~ *obtain* a customer signed statement documenting a customer's refusal to provide suitability information, if any; and

(~~3~~5) *If applicable*,~~Obtain~~ *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 insurance producer's or insurer's recommendation.

~~F.~~*G.* (1) An insurer shall establish a supervision system that is reasonably designed to achieve the insurer's and its insurance producers' compliance with this regulation, including, but not limited to, the following:

(a) The insurer shall maintain reasonable procedures to inform its insurance producers 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 to comply with the requirements of section 7 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;

(d) The insurer shall maintain procedures for review of each recommendation prior to issuance of an annuity that are designed to ensure that there is a reasonable basis to determine that a recommendation is suitable ***and in the consumer's best interest***. 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. ***The selection criteria shall include, among other things, whether the applicant is a senior citizen***;

(e) The insurer shall maintain reasonable procedures to detect recommendations that are not suitable ***or in the consumer's best interest***. This may include, but is not limited to, confirmation of consumer suitability 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 after issuance or delivery of the annuity; and

(f) 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 8 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. ***An insurer is responsible for the compliance of its insurance producer with the provisions of this article regardless of whether the insurer contracts for performance of a function required under this subdivision and regardless of the insurer's compliance with subdivision (b) of this paragraph.***

(b) An insurer's supervision system under paragraph (1) shall include ***reasonable*** supervision of contractual performance under this subsection. This includes, but is not limited to, the following:

(i) ***Reasonable monitoring*** ~~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 include in its system of supervision an insurance producer's recommendations to consumers of products other than the annuities offered by the insurer.

(4.) The insurer shall maintain reasonable procedures to ensure producers adequately disclose information as required by this regulation.

~~G.~~ ~~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;~~

~~(2)~~ ~~Filing a complaint; or~~

~~(3)~~ ~~Cooperating with the investigation of a complaint.~~

H. (1) Sales made in compliance with FINRA requirements pertaining to suitability*, best interest standards* and supervision of annuity transactions shall satisfy the requirements under this regulation *if at a minimum, FINRA's standards provide the consumer protections set forth in this NAIC model regulation*. ~~This subsection applies to FINRA broker-dealer sales of annuities if the suitability 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. *Except as provided in this paragraph, all other provisions of this Model Regulation remain applicable to these broker-dealer sales.*

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

Section 7. *Prohibited Practices*

~~G.~~*A.* *An insurance producer or insurer shall not dissuade, or attempt to dissuade, a consumer from:*

(1) *Truthfully responding to an insurer's request for confirmation of suitability information;*

(2) *Filing a complaint; or*

(3) *Cooperating with the investigation of a complaint.*

B. *An insurance producer or insurer shall not recommend that a consumer sell or replace variable annuities or other investments that the producer is unauthorized to sell.*

C. *Neither a producer nor an intermediary shall accept or receive cash or non-cash compensation which is based on having reached target sales levels.*

D. *Neither a producer nor an intermediary shall create or base a recommendation on incentives (such as target sales goals, quotas, sales contests, or other similar inducements) that would reasonably be expected to cause the insurance producer or intermediary to act on the producer's or intermediary's or insurer's own financial interest, rather than in the consumer's best interest. Nothing in this subsection prohibits a producers from recommending proprietary products.*

E. *Neither a producer nor an intermediary nor an insurer shall make any materially misleading statements or omissions regarding the annuity transaction.*

Section ~~7.~~ *8.* **Insurance Producer Training**

A. An insurance producer shall not solicit the sale 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.

Drafting Note: If a State requires more than four (4) hours of initial training on annuities, the State may instead require additional course hours in accordance with State law.

(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. ***States may also require insurance producers to comply with additional continuing education requirements regarding annuities prior to license renewal.***

(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~~ *fixed, variable and indexed annuities* affect consumers;

(d) The application of income taxation of qualified and non-qualified annuities;

(e) The primary uses of annuities; ~~and~~

(f) Appropriate sales practices, replacement and disclosure requirements;

(g) *Prohibited sales practices, the recognition of indicators that a proposed insured may lack the short-term memory or judgment to knowingly purchase an insurance product, and fraudulent and unfair practices for sales of annuities*

(4) 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 products. Additional topics may be offered in conjunction with and in addition to the required outline.

(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~~*8*) 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 ~~8~~ *9*. Compliance Mitigation; Penalties

A. An insurer is responsible for compliance with this regulation. If a violation occurs, either because of the action or inaction of the insurer or its insurance producer, the commissioner may*, in addition to any other available penalties, remedies, or administrative actions,* 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 this regulation;

(2) A *managing* general ~~agency~~ *agent*, ~~independent~~ *production* agency *through which the producer transacts and/*or 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.

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.

Drafting Note: States that adopt this Model Regulation as a statute may include a section authorizing the Commissioner to adopt reasonable rules and regulations, and amendments and additions, as are necessary to administer this Regulation.

Section ~~9.~~ *10*. [Optional] 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 and other information used in making the recommendations that were the basis for insurance transactions for [insert number] 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 and specify a time period that is consistent with those laws. For some States this time period may be five (5) years.

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 10. 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.

Chronological Summary of Action (All references are to the Proceedings of the NAIC).

2003 Proc. 3rd Quarter 17-18, 24-27, 32, 213 (adopted).
2006 Proc. 2nd Quarter 40, 90 (amended).
2010 Proc. 1st Quarter Vol. I 105-106, 117, 129-139, 146-159, 313 (amended).
2015 Proc. 1st Quarter, Vol. I 117-118, 131-134, 326-335, 431 (amended).