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February 14, 2024

The Honorable Mike McGuire
California Senate President Pro Tempore
1020 O Street, Suite 8610
Sacramento, CA 95814

RE: SB 263 (Dodd) - As Amended February 8, 2024 - OPPOSE UNLESS AMENDED

Dear President Pro Tempore McGuire:

Our coalition of consumer groups continues to oppose SB 263 (Dodd) unless it is amended to protect consumers instead of misleading them into thinking they are protected when they are not. The coalition that opposed SB 263 in 2023 (the first five groups listed below) has now been joined by additional groups – California Alliance for Retired Americans and California Advocates for Nursing Home Reform -- that have seen that SB 263 hurts consumers instead of helping them. We understand that AARP California has submitted its own opposition letter.

Although SB 263 started out last year as a strong consumer protection bill – the March 7, 2023 version paralleled New York’s Regulation 187 as a model for how best to protect consumers of life insurance products from abusive sales practices – amendments pushed by the insurance industry weakened the bill so much that our coalition has been forced to oppose the bill unless it is amended materially to place consumers’ interests ahead of the interests of agents (“producers”) and insurers. Amendments made to SB 263 after it passed the Senate in May 2023 weakened an already weak bill even further.

SB 263 in its current form closely tracks the *Suitability in Annuity Transactions* Model Regulation adopted by the National Association of Insurance Commissioners (NAIC) in 2020. The standard of care set forth in the NAIC Model (and thus SB 263) is a “best interest” standard in name only. Among other problems, it allows producers to consider their own financial interests in making recommendations, in contrast to the March 7, 2023, version, which permitted agents to consider only the interests of the consumer in making recommendations. And SB 263

does nothing to protect consumers from conflicts of interest with their agents; to the contrary, it authorizes agents to mislead consumers by telling them that they have no conflicts of interest even when they have substantial conflicts.

We write to update you on some recent developments and on how California can accommodate the insurance industry while still providing meaningful protections for consumers and not undermining the Biden Administration's efforts to provide true best interest protection for the approximately half of fixed annuity purchases that are made in retirement plans or IRA's. We have requested a meeting with you through your scheduler, Barbara Mohondro. We would greatly appreciate the opportunity to discuss these issues with you before any further action is taken on SB 263.

After SB 263 was held by the Assembly Appropriations Committee in September 2023, members of our coalition met with the author and the sponsor and proposed a compromise approach based on the SEC's Regulation BI ("Reg BI"). Reg BI is not as protective of consumers as New York's Regulation 187 and the original March 7, 2023, version of SB 263, but it is much stronger than the NAIC Model. The author and sponsor would not engage us on incorporating the Reg BI standards into SB 263 -- even though sales of *variable* annuities are already governed by Reg BI and industry has already adapted to those standards. Adopting Reg BI standards in SB 263 would apply the same standards to fixed annuities as already apply to variable annuities.

Reg BI Protects Consumers Far Better Than SB 263

Like SB 263, Reg BI opens with a requirement that the producer must act in the best interest of the customer and then articulates four component obligations (Care, Disclosure, Conflict of Interest, and Compliance) that, if satisfied, deem the producer's recommendation to be made in the customer's best interest. But the scope of the component obligations differs significantly between SB 263 and Reg BI.

Care Obligation

The Care Obligation of SB 263 does not reincorporate the producer's obligation to act in the best interest of the customer, which means that the best interest requirement *drops out of the statute* if the component obligations are met. In contrast, the Care Obligation of Reg BI *reincorporates the best interest requirement* by requiring producers to "have a reasonable basis to believe that the recommendation is in the best interest of a particular retail customer based on that retail customer's investment profile and the potential risks, rewards, and costs associated with the recommendation and does not place the financial or other interest of the broker, dealer, or such natural person ahead of the interest of the retail customer." Reg BI Section 240.15I-1(a)(2)(ii)(B). SB 263 must be amended to reincorporate the best interest requirement into the Care Obligation.

Conflict of Interest Disclosure and Avoidance/Management

Both SB 263 and Reg BI require that the producer disclose material conflicts of interest, but that requirement is gutted in SB 263 by definitional sleight of hand. Under SB 263's definition of "material conflict of interest," the term "does not include cash or non-cash

compensation.” This definition exempts from the disclosure requirement nearly all conflicts of interest because nearly all conflicts of interest between agents and their customers arise from cash or non-cash compensation. SB 263 thus requires an agent to disclose stock ownership in a life insurance company whose annuity is being recommended (likely a very small conflict of interest) but does not require disclosure of the commissions the producer would earn if the consumer accepts the producer’s recommendation (often a very significant conflict of interest).

Reg BI requires producers to “identify and mitigate” material conflicts of interest. SB 263 has a similar provision requiring producers to “identify and avoid or reasonably manage and disclose material conflicts of interest.” But SB 263’s definitional sleight of hand eliminates the producer’ obligation to identify and reasonably manage conflicts of interest that arise from cash or non-cash compensation. Under SB 263, producers *are not required even to try to reasonably manage conflicts of interest arising from cash or non-cash compensation*. SB 263 must be amended to include material conflicts of interest that arise from cash or non-cash compensation in its definition of “material conflict of interest.”

Timing of Disclosure

Disclosures required by Reg BI must be made “prior to or at the time the recommendation is made.” In contrast, SB 263 does not require disclosures about the terms of the annuity being recommended (including its features and charges) to be made until *the time of sale*, which may be long after the recommendation is made. This is far too late for the disclosures to be useful because the consumer’s purchase decision has already been made by time of sale. This is true regardless of whether sale is deemed to happen at application, issuance or delivery of the annuity. SB 263 must be amended to require disclosures about the recommended annuity to be given *at the time a recommendation is made*.

Adoption of SB 263 Would Undermine the Biden Administration’s Retirement Security Proposal

On October 30, 2023, the federal Department of Labor announced a proposed regulation (called the Retirement Security Proposal) that would impose a true fiduciary standard on producers selling annuities within a retirement plan or IRA. The President personally condemned the higher costs consumers incur because of conflicted advice when buying annuities. <https://www.whitehouse.gov/briefing-room/speeches-remarks/2023/10/31/remarks-by-president-biden-on-protecting-americans-retirement-security/#:~:text=So%2C%20here's%20what%20my%20administration,gets%20them%20the%20best%20payday>. In addition, the White House issued a statement that pointedly criticized the NAIC Model for its “inadequate protections and misaligned incentives.” See Fact Sheet at <https://www.whitehouse.gov/briefing-room/statements-releases/2023/10/31/fact-sheet-president-biden-to-announce-new-actions-to-protect-retirement-security-by-cracking-down-on-junk-fees-in-retirement-investment-advice/>.

The insurance industry is vigorously opposing the Retirement Security Proposal. Adoption of the NAIC Model/SB 263 in California could readily be weaponized by an argument that if even a traditionally consumer-protective state like California does not think a genuine best interest standard is necessary to protect annuity consumers, that proves the Retirement Security

Proposal is unnecessary and excessive government regulation. This dynamic may explain why the industry is trying to rush SB 263 to approval even though many months remain in the current session.

Our coalition believes that no bill at all would be better than SB 263 in its current form. It is true that would open the door to potential federal regulation of the approximately half of all fixed annuity sales that are made outside retirement plans and IRA's (and thus outside the Labor Department's jurisdiction). But passage of SB 263 in its current form would demonstrate that California is not interested in protecting annuity consumers and that consumers would be better off the federal government regulated not just variable annuities and fixed annuities purchased in retirement plans or IRA's but *all* annuities.

Members of our groups have worked on the issues at play in SB 263 for many years and are some of the foremost experts in this area. We remain fully available to assist in fixing the bill so that it meets California's long-held consumer protection standards, ideally by implementing the standards applicable to variable annuities under the SEC's Reg BI.

Sincerely,

/s/ Brian P. Brosnahan

Executive Director
Life Insurance Consumer Advocacy Center

/s/ Amy Bach

Executive Director
United Policyholders

/s/ Robert Herrell

Executive Director
Consumer Federation of California

/s/ Michael DeLong

Research and Advocacy Associate
Consumer Federation of America

/s/ Birny Birnbaum

Executive Director
Center for Economic Justice

/s/ Arabelle Malinis, Esq.

Staff Attorney
California Advocates for Nursing Home Reform (CANHR)

/s/ Dwane Camp, Jr.

Executive Director
California Alliance for Retired Americans

CC: The Honorable Bill Dodd
Michael Martinez, Chief Deputy Commissioner, CDI
Josephine Figueroa, Deputy Commissioner for Legislative Affairs, CDI