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Submitted Electronically to jmatthews@naic.org

The Honorable Doug Ommen
Commissioner, Iowa Insurance Division
Chairman, NAIC Life Insurance and
Annuities (A) Committee
Two Ruan Center
601 Locus, 4th Floor
Des Moines, IA 50309

The Honorable Stephen C. Taylor
Commissioner, D.C. Department of Insurance,
Securities and Banking
Vice Chairman, NAIC Life Insurance and
Annuities (A) Committee
1050 First Street, NE, Suite 801
Washington D.C., 20002

Re: Suitability in Annuity Transactions Model Regulation
Exposure Draft dated November 19, 2018

Dear Commissioner Ommen and Commissioner Taylor:

On behalf of our members, the Insured Retirement Institute ("IRI")[1] appreciates the opportunity to provide comments regarding the November 19, 2018 draft revisions (the "Exposure Draft") to the National Association of Insurance Commissioners (the "NAIC") on the Suitability in Annuity Transactions Model Regulation (#275) (the "Suitability Model"). This letter is intended to supplement the separate comment letter being concurrently submitted to the NAIC by a group of industry associations including IRI (the "Industry Groups Letter"). The comments and recommendations set forth in the Industry Groups Letter are incorporated by reference into this letter. The remainder of this letter will discuss and describe a number of additional comments and recommendations we have regarding the Exposure Draft.

[1] IRI is the only national trade association that represents the entire supply chain of the retirement income industry. IRI has more than 500 member companies, including major life insurance companies, broker-dealers, banks, and asset management companies. IRI member companies account for more than 95 percent of annuity assets in the United States, include the top 10 distributors of annuities ranked by assets under management, and are represented by more than 150,000 financial professionals serving over 22.5 million households in communities across the country.

As we have stated in previous submissions, IRI and our members have long supported the principle that financial professionals[2] should be required to act in their clients' best interest when providing personalized recommendations. Although the vast majority of financial professionals already act in their clients' best interest and improve retirement readiness, some investors remain hesitant to seek out professional financial advice. According to a new report from RAND Corporation and the SEC Office of Investor Advocate, trust is a major determinant in whether an investor will accept investment advice.[3] As part of the report, 45 percent of investors who do not currently receive financial advice indicated that it is difficult to find a trustworthy financial professional.[4] In addition, nearly a quarter of investors who do not currently receive financial advice do not believe that financial professionals are honest in their dealings with clients.[5]

Despite the reality that 97 percent of investors using a financial professional believe that their financial professional has their best interest in mind already[6], investors without a financial professional remain skeptical. Requiring financial professionals to act in their clients' best interest may encourage more investors to seek out the financial advice they need to better prepare for retirement. As Americans continue to live longer than ever before and access to defined benefit plans continue to diminish, it is critical that they receive the financial advice necessary to protect against longevity risk. Studies show that consumers who receive assistance from financial professionals save more throughout their working years, make better use of available retirement planning products and strategies, and experience better returns on their investments. Financial professionals have been shown to help consumers earn 1.59 percent in additional annual returns, which over time leads to 22.8 percent more income in retirement.[7]

We view the work being done to enhance the Suitability Model as more than just raising the bar for insurance producer conduct. It is an opportunity to build and grow trust between producers and consumers. Of course, as we have indicated in the past, we urge you to take care to avoid creating unnecessary compliance burdens that could undermine the effectiveness of the

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[2] The term "financial professional" is used throughout this letter to refer to any individual who provides advice or recommendations about annuities or other insurance or investment products, including state-regulated insurance producers as well as securities-licensed representatives of broker-dealer or investment adviser firms.
[3] Rick Fleming, Investor Advocate, Office of the Investor Advocate, Investor Testing Regarding Standards of Conduct for Investment Professionals (Oct. 12, 2018), https://www.sec.gov/comments/s7-07-18/s70718-4513005-176009.pdf.
[4] *Id*.
[5] *Id*.
[6] U.S. Chamber of Commerce, Supplemental Comment Letter on Proposed Regulation Best Interest, Form CRS, and the Proposed Commission Interpretation Regarding Standard of Conduct of Investment Advisors (Sept. 5, 2018), https://www.sec.gov/comments/s7-07-18/s70718-4305949-173212.pdf.
[7] Insured Retirement Institute, Comment Letter on Proposed Regulation Best Interest, Form CRS, and the Proposed Commission Interpretation Regarding Standard of Conduct of Investment Advisors (Aug. 7, 2018), https://www.sec.gov/comments/s7-07-18/s70718-4185630-172656.pdf.

proposal. With this in mind, we respectfully offer the following comments and recommendations for your consideration:

1. <u>The NAIC Should Strive for Consistency with the SEC as to the Substantive Formulation of the Standard of Conduct and the Terminology Used to Identify the Standard.</u>

As noted above and in numerous comment letters to the NAIC and other regulators over the past several years, IRI and our members support the adoption of a "best interest" standard. However, we also believe that the standard must be carefully crafted to protect the market for financial advice. We have several recommendations on how the Exposure Draft could be improved to achieve a clear and consistent standard.

First, the NAIC should clarify the enhanced standard included in the Exposure Draft and work with the SEC to establish a consistent best interest framework. We understand the concerns some regulators and interested parties have about the use of this phrase, including the views outlined in the Drafting Note following Section 1 of the Exposure Draft. We continue to believe, though, that this phrase is the most appropriate label for the standard of conduct for producers and other financial professionals.

In the same vein, we are concerned about the terminology used in the Exposure Draft. Instead of using the phrase "best interest," the NAIC refers to "the interest of the consumer" in Section 6 of the Exposure Draft. It remains unclear how this term is different from the SEC's "best interest" language and creates a fog of uncertainty around the duties of insurers and producers. We urge the NAIC to strive for consistency with the SEC, both in substance and terminology.

If the SEC's final rule continues to use the phrase "best interest" to describe the standard it adopts and the NAIC opts to use a different label for its enhanced standard, the result will be significant confusion and uncertainty among consumers, producers, carriers and regulators. We think you will agree that this would not be a positive outcome.

Introducing new terminology into the Suitability Model also raises the risk of inconsistent interpretations across the states. One of the important benefits of the Suitability Model over the years has been its readily understandable formulation, which has allowed states to implement largely uniform regulatory structures to protect consumers fairly and equitably regardless of their locality. If the NAIC introduces new terminology into the Suitability Model that is left unrecognized by other regulators, state regulators will likely formulate divergent views on how to apply the new Suitability Model. In contrast, incorporating a uniform "best interest" requirement into the Suitability Model would increase the likelihood that it will be applied consistently across state lines.

Although the term "best interest" is left undefined in the SEC's proposal, IRI believes the SEC's principles-based regime provides a clear and straight-forward compliance roadmap for firms and financial professionals. While some commenters were disappointed in the SEC's decision to forego an explicit definition of "best interest" in the proposal, IRI believes the obligations detailed in the proposal provide ample guidance on how to meet the best interest standard. Put simply, the SEC's proposed best interest standard is merely a sum of its parts. In lieu of a formal definition, the SEC has simply stated that the standard can be satisfied through a process under which financial professionals satisfy the proposal's three obligations: disclosure, care, and conflicts of interest.[8] A formal definition of best interest beyond the reference to these three obligations could potentially leave financial professionals exposed to the risk that they will fall short of meeting their best interest obligation even if they satisfy the specific requirements set forth in the proposal.

The Exposure Draft already reflects some congruity with the SEC's approach, and we commend the Working Group for its efforts to align with the SEC proposal. Section 6.A(1) sets forth the applicable standard of conduct, while Sections 6.A(2), B, C and D walk through the steps producers must follow in order to satisfy the standard, including the multitude of factors a producer must consider when determining which product will best suit a client's needs.

<u>IRI's Recommendation</u>: The NAIC should continue to work with the SEC to achieve a consensus as to both the label and the substance of the applicable standard.

2. <u>The Proposed Changes to the Rules for Recommendations of Annuity Exchanges or Replacements are Unnecessary and Confusing and Could Deprive Consumers of Information About Potentially Beneficial Transactions.</u>

The Exposure Draft would modify the rules applicable in the context of exchange and replacement recommendations in three significant and, in our view, unnecessary ways. First, producers would be required to determine whether "the replacing product will provide a substantial benefit to the consumer in comparison to the replaced product over the life of the product." This is substantially different from the Suitability Model's current requirement to consider whether "the consumer would benefit from product enhancements and improvements."

The term "substantial benefit" has not previously been used in the Suitability Model and is left undefined. Without further guidance as to what constitutes "substantial benefit," we are concerned that the ambiguity surrounding this term is likely to chill exchange or replacement recommendations.

Moreover, the size of the benefit should not matter in assessing the validity of an exchange or replacement recommendation. Those recommendations should be judged by the same

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[8] Doug Ommen, Iowa Insurance Commissioner, Comment Letter on Proposed Regulation Best Interest, Form CRS, and the Proposed Commission Interpretation Regarding Standard of Conduct of Investment Advisors (Aug. 6, 2018) (recognizing that compliance with Regulation BI is a process that is satisfied by meeting the three requirements), https://www.sec.gov/comments/s7-07-18/s70718-4171183-172120.pdf.

standard as any other type of recommendation. The only relevant inquiry is whether the customer would benefit from the transaction. If that answer is yes, regardless of the size of the benefit, then the transaction should be treated as suitable. Using the “substantial benefit” language will only cause financial professionals to stay silent when opportunities are available to clients.

To address this concern, we believe the NAIC should strike the “substantial benefit” requirement entirely. Alternatively, if the NAIC believes this language is necessary, it should provide clear guidance for producers to help them determine exactly what constitutes a “substantial benefit.” For example, is the underlying purpose to ensure that there are commensurate benefits at least offsetting any costs or other detrimental impacts experienced in the transaction?

The second significant change to the rules for replacements relates to the duration of the look back period for past exchanges or replacements. The Exposure Draft would increase this period from 36 months to 60 months. We respectfully request more information as to the reason for this change. If there is substantial evidence to suggest that unsuitable exchanges or replacements are occurring four and five years after a previous exchange or replacement, IRI would certainly be open to supporting this change. In the absence of any such evidence, this change would simply serve to increase the compliance burden on producers and insurers by requiring them to subject a greater number of proposed sales to heightened review without any meaningful consumer benefit, in which case, we would oppose this modification.

Finally, the Exposure Draft includes a change to the definition of “replacement” in Section 5.N, striking the phrase “if there is no producer involved” and inserting the phrase “whether or not a producer is involved.” This change cold be interpreted as significantly expanding the circumstances under which a transaction would constitute a replacement. Under the language in the current Suitability Model, if a producer recommends an annuity purchase and has neither actual nor constructive knowledge that the consumer is taking action with respect to an existing policy or contract, the transaction would not be treated as a replacement. We are concerned that the Exposure Draft’s revisions to this definition would require that producer to satisfy the rules applicable to exchanges and replacements based on information in the possession of the insurer. We are unclear as to the reason for this change, but we certainly do not see how a producer could reasonably be expected to tailor his or her conduct based on information they do not have. This proposed revision could also expand the obligation of the insurer since it would be applicable “whether or not a producer is involved”. However, the language is ambiguous, and the duties of an insurer are undefined. Further, to the extent that the insurer would have additional responsibilities, the rationale for such a change is also unclear.

<u>IRI's Recommendation</u>: The NAIC should reject the proposed changes to Sections 5.N and 6.D(1)(d) and revert back to the language in the corresponding sections of the current Suitability Model regarding annuity exchanges or replacements.

3. <u>Other Suggested Revisions.</u>

   A. *Definition of Consumer Profile Information*

   The Exposure Draft includes several modifications to the term "suitability information," including a change in the defined term itself to "consumer profile information." While we are generally comfortable with the revisions to this definition, we are concerned that two of the changes could give rise to uncertainty or confusion for producers and insurers. First, we are unclear as to the intent of the phrase "including debt and other obligations" in clause (3). As drafted, this could be interpreted as requiring producers, and insurers where no producer is involved, to seek information from their clients about every single debt they owe, regardless of the amount, nature and repayment status of the debt. Our sense is that the intent is to ensure that producers and insurers are aware of the client's most significant financial obligations before recommending that they purchase an annuity. Mortgage debt, auto loans, student loans, and the like would typically be relevant; the $10 borrowed from a co-worker to pay for lunch would not. To avoid any confusion, we suggest the addition of a materiality qualifier or other clarification.

   Second, the proposed insertion of the phrase "including willingness to accept non-guaranteed elements in the annuity" in subsection (11) seems out of place. We are not opposed to requiring consideration of the extent to which the annuity includes nonguaranteed elements as part of the best interest analysis, but we think it would make more sense to move this to Section 6.D. In other words, a producer, or an insurer where no producer is involved, should be expected to make sure that their clients understand any non-guaranteed elements in the annuity being recommended (Section 6.D(1)(a)), and any such elements should be taken into account when determining whether the "particular annuity as a whole [is] suitable" (Section 6.D(1)(c)).

   <u>IRI's Recommendation</u>: The NAIC should provide greater clarity regarding "debt and other obligations" and "non-guaranteed elements," as currently referenced in the Exposure Draft's definition of "consumer profile information."

   B. *Definition of "Suitable"*

   As a matter of consistency, IRI suggests that the NAIC slightly revise the language in the definition of "suitable" to ensure that consistent terminology is used throughout the regulation. Currently, the Exposure Draft defines "suitable" as "a recommendation of an annuity that is consistent with the consumer's insurance needs and financial objectives based upon the facts disclosed by the consumer…." Given that the Exposure Draft refers to the information consumers provide to producers as "consumer profile information," we believe it would be clearer to use that term in this definition.

***IRI's Recommendation*: The NAIC should revise the definition of "suitable" to reference the "consumer profile information disclosed by the consumer" rather than the "facts disclosed by the consumer."**

C. *Disclosure of Available Products*

While IRI and our members are generally supportive of the disclosure requirements set forth in the Exposure Draft (with the exception of the compensation disclosure provisions, as discussed in the Industry Groups Letter), we are concerned about the product disclosure requirement as currently formulated in Section 6.C(2). In our view, requiring disclosure of "any limitations the producer or the insurer has in regard to" available products places the emphasis in the wrong place. We believe it would be more beneficial to consumers, and more manageable for the industry, to focus on helping consumers understand which products can be recommended rather than those that cannot be recommended (as implied by the reference to limitations).

***IRI's Recommendation*: The NAIC should revise Section 6.C(2) to read "Disclose to the consumer the following:" in lieu of the reference to "limitations."**

D. *Supervision of Producer Disclosures*

The Exposure Draft purports to require insurers to include in their system of supervision "reasonable procedures to assess, prior to or upon issuance or delivery of an annuity, whether a producer has provided to the consumer the information required to be provided under this section." We do not believe it would be appropriate to require insurers to verify delivery of required disclosures by producers. This would be extremely burdensome and would provide little to no meaningful consumer benefit. Moreover, it could be interpreted as imposing a requirement on insurers to review and verify the accuracy of such disclosures. If the NAIC disagrees and chooses to retain this requirement, we believe it would be appropriate to at least permit insurers to rely on certifications from producers as to compliance with applicable disclosure requirements.

Similarly, insurers should not be required to obtain or retain copies of producer disclosure documents, nor should producers be required to obtain or retain copies of carrier disclosures. The reference to disclosures made to the consumer in Section 9 of the Exposure Draft should be limited only to disclosures made by the regulated entity itself.

<u>IRI's Recommendation</u>: The NAIC should

(a) either strike Section 6.H(1)(f) from the Exposure Draft or modify that provision to expressly authorize insurers to comply with its requirements by obtaining certifications from producers stating that all required disclosures have been delivered to their clients; and

(b) revise the reference to disclosures in Section 9 to refer only to "disclosures made by such person to the consumer."

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Thank you again for the opportunity to provide these comments. If you have questions about anything in this letter, or if we can be of any further assistance in connection with this important regulatory effort, please feel free to contact the undersigned at jberkowitz@irionline.org or 202-469-3014.

Sincerely,

Jason Berkowitz
Vice President & Counsel, Regulatory Affairs

Cc: The Honorable Eric Cioppa, Maine Insurance Superintendent, NAIC President
The Honorable Raymond Farmer, South Carolina Insurance Director, NAIC President-Elect
The Honorable David Altmeier, Florida Insurance Commissioner, NAIC Vice President
The Honorable Dean Cameron, Idaho Insurance Director, NAIC Secretary-Treasurer
Mr. Michael Consedine, NAIC Chief Executive Officer