

BEST INTEREST BACKGROUND

In February 2020, the National Association of Insurance Commissioners (NAIC) adopted revisions to the Suitability in Annuity Transactions Model Regulation to incorporate a best interest standard of care. With this action by the NAIC, insurance regulators in all 50 states and the U.S. territories are urged to seek adoption of these enhanced consumer protections in their respective jurisdictions as expeditiously as possible.

Overview of Key Revisions to the Model Regulation

Best Interest Standard of Care

The revised Model Regulation expressly requires a producer, including an insurer where no producer is involved, to act in the best interest of the consumer, without placing the producer's or the insurer's financial interest ahead of the consumer's interest.

To act in the best interest of the consumer, the producer is required to satisfy four obligations – the care, disclosure, conflict of interest and documentation obligations. To fulfill the care obligation, a producer is required to exercise reasonable diligence, care and skill to have a reasonable basis to believe a recommended annuity effectively addresses the consumer's financial situation, insurance needs and financial objectives as evaluated in light of the consumer's profile information.

To fulfill the disclosure obligation, a producer is required to prominently disclose to the consumer: (i) a description of the scope and terms of the producer's relationship with consumer; (ii) whether the producer is licensed and authorized to sell specified products; (iii) a description of the insurers the producer is authorized to sell insurance products for; (iv) a description of the sources and types of cash and non-cash compensation to be received by the producer; and (v) notice of the consumer's right to request additional information regarding cash compensation

To fulfill the conflict of interest obligation, a producer is required to identify and avoid or reasonably manage and disclose "material conflicts of interest," defined as a financial interest a reasonable person would expect to influence the impartiality of a recommendation. "Material conflict of interest" does not include cash or non-cash compensation.

To fulfill the documentation obligation, a producer is required to: (i) make a written record of any recommendation and the basis for the recommendation; and (ii) obtain signed statements from a consumer relating to the consumer's refusal to provide consumer profile information or to an annuity transaction that is not recommended by the producer.

New Supervision Requirements

The revised Model Regulation subjects insurers to several new supervisory requirements. Among other things, the Model now requires insurers to establish and maintain reasonable procedures to identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation that are based on sales of specific annuities within a limited period of time.

Safe Harbor

The revised Model Regulation reflects an expansion of its previous safe harbor, that was applicable to sales made by broker dealers in compliance with FINRA requirements, to now include recommendations and sales of annuities made in compliance with “comparable standards” by registered investment advisors and investment advisory representatives, not regulated by FINRA, but subject to fiduciary duties.

Alignment with SEC’s Regulation Best Interest and ACLI Policy

The revised Model Regulation incorporates a best interest standard of care for annuities similar to the best interest standard of care for securities established under the SEC’s Regulation Best Interest.

The revised Model Regulation aligns well with ACLI policy in support of a best interest standard of care for individualized recommendations to retail customers regarding the purchase, exchange or replacement of an annuity.

Adoption of the revised Model Regulation by the states will further ACLI’s goal of a harmonized standard of care for annuities and securities across regulatory platforms to significantly enhance consumer protection across the country.