

CEFLI VIRTUAL SUMMIT MEETING:

Revisions to the NAIC Suitability in Annuity Transactions Model Regulation

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Resource Materials



Suitability in Annuity Transactions Model Regulation
Compliance Implementation Considerations

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Compliance Implementation Considerations

The revised NAIC Suitability in Annuity Transactions Model Regulation was adopted by the NAIC on February 13, 2020. The revised NAIC Model implements a Best Interest standard of conduct, puts in place additional consumer data collection requirements, requires additional consumer disclosures, requires specific training of producers, requires producers take into consideration specific information and factors when recommending an annuity, and it requires insurers to establish and maintain a system of supervision. The revised Model Regulation replaces existing state law only after a state adopts the updated NAIC Model and upon the compliance date associated with the adoption.

The following pages summarize high level requirements of the revised Model Regulation. The content is organized into sections summarizing producer impacts and insurer impacts. Given the summary nature of this document, insurers should thoroughly review the full Model Regulation, along with the specific content of future state adoptions of the revised Model, to fully understand new regulatory requirements. This document does not constitute legal advice.

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Producers: Collect “Consumer Profile Information” from the consumer

The revised NAIC Model requires specific consumer information be collected by a producer, prior to making an annuity recommendation. The producer must consider the information, along with other factors, when making an annuity recommendation. The chart below summarizes the “Consumer Profile Information.”

#	Consumer Profile Information	Reference
1	Age	5.C.(1)
2	Annual income	5.C.(2)
3	Financial situation and needs, including debts and other obligations	5.C.(3)
4	Financial experience	5.C.(4)
5	Insurance needs	5.C.(5)
6	Financial objectives	5.C.(6)
7	Intended use of the annuity	5.C.(7)
8	Financial time horizon	5.C.(8)
9	Existing assets or financial products, investments, annuity & insurance holdings	5.C.(9)
10	Liquidity needs	5.C.(10)
11	Liquid net worth	5.C.(11)
12	Risk tolerance, including willingness to accept nonguaranteed annuity elements	5.C.(12)
13	Financial resources used to fund the annuity	5.C.(13)
14	Tax status	5.C.(14)

Producers: Disclosure specific information to the consumer

The revised NAIC Model requires producers disclose specific information to consumers, when making an annuity recommendation. The chart below summarizes the consumer disclosure requirements.

#	Consumer Disclosure Requirements	Appendix A Producer Disclosures	Appendix B Consumer Refusal to Provide Information	Appendix C Consumer Decision to Purchase an Annuity That Was Not Recommended	Other	Reference
1	The basis of the recommendation.				X	6.A.(1)(a)(iv), 6.A.(4)(a)
2	A description of the scope and terms of the relationship with the consumer and the role of the producer in the transaction. The “Agent Disclosure for Annuities” form (Appendix A) or a similar form may be used.	X				6.A.(2)(a)(i), Appendix A

3	An affirmative statement regarding the specific products the producer is authorized to sell. The “Agent Disclosure for Annuities” form (<u>Appendix A</u>) or a similar form may be used.	X				6.A.(2)(a)(ii), <u>Appendix A</u>
4	An affirmative statement describing the insurers the producer is authorized, contracted (or appointed) with, or otherwise able to sell insurance products for. The “Agent Disclosure for Annuities” form (<u>Appendix A</u>) or a similar form may be used.	X				6.A.(2)(a)(iii), <u>Appendix A</u>
5	A description of the sources and types of cash compensation and non-cash compensation to be received by the producer, including whether the producer is to be compensated for the sale of a recommended annuity by commission or as part of premium or other remuneration received from the insurer, intermediary or other producer by fee or as a result of a contract for advice or consulting services. The “Agent Disclosure for Annuities” form (<u>Appendix A</u>) or a similar form may be used.	X				6.A.(2)(a)(iv), <u>Appendix A</u>
6	A notice disclosing the consumer’s right to request additional information regarding cash compensation. The “Agent Disclosure for Annuities” form (<u>Appendix A</u>) or a similar form may be used.	X				6.A.(2)(a)(v), <u>Appendix A</u>
7	Upon request by the consumer for more information regarding producer compensation, the producer shall disclose: <ol style="list-style-type: none"> 1. A reasonable estimate of the cash compensation to be received by the producer (may be stated as a range of amounts or percentages); and 2. Whether the compensation is a one-time or multiple occurrence amount, the frequency and the amount of the occurrence (may be stated as a range of amounts or percentages). 				X	6.A.(2)(b)(i)- (ii)
8	Inform the consumer of the various features of the annuity, such as: <ol style="list-style-type: none"> 1. The potential surrender period; 2. The potential surrender charge; 3. The potential tax penalty (if selling, exchanging or annuitizing); 4. Morality and expense fees; 5. Investment advisory fees; 6. Any annual fees; 7. Potential charges for features of riders or other options; 8. Limitations on interest returns; 9. Potential changes in non-guaranteed elements of the annuity; 10. Insurance components; 11. Investment components; and 12. Market risk. 				X	6.A.(2)(c)
9	Provide a copy of the “Consumer Refusal to Provide Information” form (<u>Appendix B</u> or similar form) to the consumer if the consumer refuses to provide consumer profile information or if the consumer provides		X			6.A.(4)(b)(i)- (ii), <u>Appendix B</u>

	insufficient information. The form must be signed by the consumer and a copy of the record must be maintained by the producer and/or insurer.					
10	Provide a copy of the “Consumer Decision to Purchase an Annuity NOT Based on a Recommendation” (<u>Appendix C</u> or similar form) to the consumer if the consumer elects to enter into an annuity purchase that was not recommended. The form must be signed by the consumer and the producer, and a copy of the record must be maintained by the producer and/or insurer.			X		6.A.(4)(c), <u>Appendix C</u>

Producers: Consider several factors when making an annuity recommendation

The NAIC Model requires certain considerations of producers when making annuity recommendations. Specifically, a producer must act in the best interest of the consumer, based on the circumstances known at the time the recommendation is made, without placing the producer’s or the insurer’s financial interest ahead of the consumer’s interest. The Model specifies a producer must exercise reasonable diligence, care and skill. The Model elaborates on the specific actions required to satisfy the best interest obligation (section 6.A.):

1. Care (i.e. “Care Obligation”);
2. Disclosure;
3. Conflict of interest; and
4. Documentation.

The Model clarifies that the requirements:

1. Do not create a fiduciary obligation or relationship (section 6.A.(1)(d)); and
2. Apply to every producer who exercised material control or influence in the making of a recommendation and who received direct compensation as a result of the recommendation regardless of whether the producer had any direct contact with the consumer (section 6.A.(5)).

The chart below summarizes producer requirements when making an annuity recommendation.

#	Annuity Recommendation Considerations	Reference
Best Interest Obligation		
1	Act in the best interest of the consumer based on the circumstances known at the time the recommendation is made, without placing the producer’s or the insurer’s financial interest ahead of the consumer’s interest. A producer has acted in the best interest of the consumer if the care, disclosure, conflict of interest, and documentation obligations have been satisfied.	6.A.
Care Obligation		
2	Exercise reasonable diligence, care and skill to: <ol style="list-style-type: none"> 1. Know the consumer’s financial situation, insurance needs and financial objectives; 2. Understand the available recommendation options; 	6.A.(1)(a)(i)-(iv)

	<ol style="list-style-type: none"> 3. Have a reasonable basis to believe the recommendation effectively addresses the consumer’s financial situation, insurance needs, and financial objectives over the life of the product, in consideration of the consumer’s profile information; and 4. Communicate the basis of the recommendation. 	
3	Make a reasonable effort to collect and consider the consumer’s profile information (i.e. the consumer’s financial situation, insurance needs and financial objectives) prior to making a recommendation.	6.A.(1)(b)
4	Consider the types of products the producer is licensed and authorized to recommend or sell, that would address the consumer’s financial situation, insurance needs, and financial objectives.	6.A.(1)(c)
5	Consider the importance of each factor regarding the a.) consumer’s profile information; b.) characteristics of the insurer; and c.) product information (i.e. costs, rates, benefits and features). The importance of each factor may vary depending on the facts and circumstances of the particular case. Each factor should not be considered in isolation.	6.A.(1)(e)
6	Have a reasonable basis for believing the consumer would benefit from certain features of an annuity, such as annuitization, death or living benefits or other insurance-related features.	6.A.(1)(f)
7	The requirements apply to the particular annuity, as a whole, and to the underlying subaccounts to which funds are allocated at the time of a purchase or exchange. The requirements also apply to riders and product enhancements.	6.A.(1)(g)
8	<p>Consider whether a replacement or exchange is involved and whether:</p> <ol style="list-style-type: none"> 1. The consumer will incur a surrender charge, be subject to 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; 2. The replacing product will substantially benefit the consumer, compared to the replaced product, over the life of the product; and 3. The consumer has had another annuity exchange or replacement and, in particular, an exchange or replacement within the preceding 60 months. 	6.A.(1)(j)
Disclosure Obligation		
9	<p>Prior to the recommendation or sale of an annuity, the producer shall prominently disclose to the consumer, on a form substantially similar to the “Agent (Producer) Disclosure for Annuities” (Appendix A of the Model):</p> <ol style="list-style-type: none"> 1. A description of the scope and terms of the relationship with the consumer and the role of the producer in the transaction; 2. An affirmative statement regarding the specific products the producer is authorized to sell. Refer to 6.A.(2)(a)(ii)(I)-(X); 3. An affirmative statement describing the insurers the producer is authorized, contracted or appointed to sell for. Refer to 6.A.(2)(a)(iii)(I)-(III); 4. A description of the sources and types of cash compensation and non-cash compensation to be received by the producer, including whether the producer is to be compensated for the sale of a recommended annuity by commission or as part of premium or other remuneration received from the insurer, intermediary or other producer by fee or as a result of a contract for advice or consulting services; and 5. A notice regarding the consumer’s right to request additional information regarding cash compensation. 	6.A.(2)(a)(i)-(v)
10	<p>Upon request from the consumer, the producer shall disclose:</p> <ol style="list-style-type: none"> 1. A reasonable estimate of the amount of cash compensation to be received by the producer (can be stated as a range of amounts or percentages); and 2. Whether the cash compensation is a one-time or multiple occurrence amount and, if a multiple occurrence, the frequency and amount of the occurrence (can be stated as a range of amounts or percentages). 	6.A.(2)(b)(i)-(ii)

11	Prior to, or at the time of a recommendation, have a reasonable basis to believe the consumer has been informed of the various features of the annuity, such as: <ol style="list-style-type: none"> 1. Potential surrender period; 2. Potential surrender charge; 3. Potential tax penalty if the consumer sells, exchanges, surrenders or annuitizes the annuity; 4. Mortality and expense fees; 5. investment advisory fees; 6. Any annual fees; 7. Features of any riders or other options of the annuity; 8. Potential charges for any riders or other options; 9. Any limitations on interest returns; 10. Potential changes in non-guaranteed elements of the annuity; 11. Insurance and investment components; and 12. Any market risk. 	6.A.(2)(c)
Conflict of Interest Obligation		
12	Identify and avoid, or reasonably manage and disclose, material conflicts of interest, including conflicts related to an ownership interest.	6.A.(3)
Documentation Obligation		
13	Make a written record of any recommendation and the basis for the recommendation. Disclose the basis of the recommendation to the consumer.	6.A.(4)(a) & 6.A.(1)(a)(iv)
14	When the situation warrants, obtain the consumer's signed statement on a form substantially similar to the form in <u>Appendix B</u> , documenting: <ol style="list-style-type: none"> 1. The consumer's refusal to provide the consumer profile information; and 2. The consumer's understanding of the ramifications of not providing the consumer profile information or providing insufficient profile information. 	6.A.(4)(b)(i)-(ii), <u>Appendix B</u>
15	Obtain a consumer's signed statement acknowledging the annuity transaction was not recommended by the producer, if such is the case. <u>Appendix C</u> , or a similar form may be used.	6.A.(4)(c), <u>Appendix C</u>
16	Maintain, or be able to make available to the commissioner, records of the information collected from the consumer (i.e. Consumer Profile Information), disclosures made to the consumer (this includes the <u>Appendix A</u> disclosure, product disclosures, etc.) and any other information used in making a recommendation that was the basis for the insurance transaction. Producers are required document the disclosure of information provided in writing and summaries of any oral disclosures provided. Insurers may maintain records on behalf of their producers.	9.A.
Prohibited Practices		
17	The producer shall not dissuade, or attempt to dissuade, a consumer from: 1.) truthfully responding to an insurer's request for confirmation of the consumer profile information; 2.) filing a complaint; or 3.) cooperating with the investigation of a complaint.	6.D.

Producers: Satisfy training requirements

A producer may not solicit the sale of an annuity product unless the producer has complied with the training requirements of the Model (section 7.A.-B.).

#	Annuity Training Requirements	Reference
1	Prior to recommending an annuity, a producer must have adequate knowledge of the product and the producer must be in compliance with the insurer's standards for product training.	7.A.
2	Prior to recommending an annuity, a producer must be in compliance with the insurer's standards for product training.	7.A.
3	Prior to recommending an annuity, a producer must complete EITHER a <u>new</u> , one-time four (4) hour training course approved by the department of insurance and provided by a department of insurance-approved education provider, OR have completed a prior four (4) hour insurance department-approved annuity training course PLUS an additional, <u>new</u> one (1) hour training approved by the department of insurance, provided by a department of insurance-approved provider.	7.B.(6)(a)-(b)

Insurers: Support compliance with the regulation

In addition to establishing and maintaining a system of supervision, insurers are required to take certain actions prescribed by the Model. A summary of the obligations is included below. The summary chart also includes several insurer actions that may be implied by the Model, rather than expressly stated.

#	Support Compliance with the Regulation—Insurers Shall:	Reference
1	Not dissuade, or attempt to dissuade, a consumer from: 1.) truthfully responding to an insurer's request for confirmation of the consumer profile information; 2.) filing a complaint; or 3.) cooperating with the investigation of a complaint.	6.D.
2	Verify a producer has completed the annuity training required by the Model Regulation before allowing the producer to sell an annuity for the insurer.	7.B.(11)
3	Take appropriate corrective action for any consumer harmed by a failure to comply with the regulation.	8.A.(1)
4	Maintain or be able to make available to the commissioner records of the information collected from the consumer, disclosures made to the consumer (including summaries of any oral disclosures) and other information used in making a recommendation that were the basis for insurance transactions. Insurers may maintain records on behalf of their producers.	9.A.
5	<u>May be Implied:</u> Develop and provide producers with appropriate product disclosure materials aligned with the consumer disclosure requirements of the regulation, or otherwise advise producers of expectations in this area.	n/a
6	<u>May be Implied:</u> Develop and provide producers with a suitability form for capturing information necessary to make a suitability recommendation, or otherwise advise producers of the insurer's expectations in this area.	n/a
7	<u>May be Implied:</u> Develop and provide producers with a form equivalent to the "Agent (Producer) Disclosure for Annuities" form in Appendix A of the Model Regulation, or otherwise advise producers of the insurer's expectations in this area.	n/a
8	<u>May be Implied:</u> Develop and provide producers with a form equivalent to the "Consumer Refusal to Provide Information" in Appendix B of the Model Regulation, or otherwise advise producers of the insurer's expectations in this area.	n/a

9	<u>May be Implied:</u> Develop and provide producers with a form equivalent to the “Consumer Decision to Purchase and Annuity NOT Based on a Recommendation” form in <u>Appendix C</u> of the Model Regulation, or otherwise advise producers of the insurer’s expectations in this area.	n/a
10	<u>May be Implied:</u> Train and/or inform producers regarding the use of the insurer’s forms and required point-of-sale disclosures.	n/a

Insurers: Establish and maintain a system of supervision

Insurers must establish and maintain a system of supervision reasonably designed to achieve the insurer’s and its producer’s compliance with the regulation (section 6.C. and 6.E.). The system of supervision does not need to address producer recommendations of other insurers’ annuities or products (section 6.C.(4)).

Safe Harbor: Recommendations made in compliance with “comparable standards” covering best interest (i.e. SEC, FINRA, Investment Advisor Act of 1940, etc.), shall satisfy the requirements of the Model (section 6.E.). The insurer may base its analysis on information received from either the financial professional or from the entity supervising the financial professional. In order to rely on the safe harbor, the insurer must monitor the relevant conduct of the financial professional relying on the safe harbor or the entity supervising the financial professional (i.e. broker-dealer, investment advisor, etc.), using the information collected in the normal course of business.

Specific supervisory elements are summarized in the following table.

#	Establish and Maintain a System of Supervision—Insurers Shall:	Reference
1	Not issue a recommended annuity unless there is a reasonable basis to believe the annuity would effectively address the consumer’s financial situation, insurance needs and financial objectives, based on the consumer’s profile information.	6.C.(1)
2	Establish and maintain reasonable procedures to inform producers of the requirements the regulation and incorporate the requirements into relevant producer training manuals.	6.C.(2)(a)
3	Establish and maintain reasonable procedures to require producers comply with Section 7, regarding the insurer’s product training.	6.C.(2)(b),7.A.
4	Establish and maintain reasonable procedures to require producers comply with Section 7, regarding the one-time NEW four (4) hour training module OR the prior four (4) hour training module with completion of a NEW one (1) hour annuity training. All training must be approved by the department of insurance and provided by an insurance approved education provider.	6.C.(2)(b), 7.B.
5	Develop and provide product-specific training and training materials which explain all material features of its annuity products.	6.C.(2)(c)
6	Establish and maintain procedures for the review of each recommendation prior to issuance of an annuity that are designed to ensure there is a reasonable basis to determine that the recommended annuity would effectively address the particular consumer’s financial situation, insurance needs and financial objectives. 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.	6.C.(2)(d)
7	Establish and maintain reasonable procedures to detect recommendations that 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,	6.C.(2)(e)

	systematic customer surveys, producer and consumer interviews, confirmation letters, producer statements or attestations and programs of internal monitoring. Note: Insurers may apply sampling procedures or confirm information after issuance or delivery of the annuity.	
8	Establish and maintain 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 (e.g. rationale for the sales, product disclosures, producer relationship disclosures, refusal to disclose disclosure, etc.).	6.C.(2)(f)
9	Establish and maintain reasonable procedures to identify and address suspicious consumer refusals to provide profile information.	6.C.(2)(g)
10	Establish and maintain reasonable procedures to identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific annuities within a limited period of time. Note: The regulation does not prohibit a producer's receipt of health insurance, office rent, office support, retirement benefits or other employee benefits as long as those benefits are not based upon the volume of sales of a specific annuity within a limited period of time. Additionally, the intent of this the requirement is to prohibit sales contests, sales quotas, bonuses and non-cash compensation that promote the sale of a particular product within a limited period of time, but not to prohibit general incentives regarding the sales of a company's products with no emphasis on any particular product.	6.C.(2)(h)
11	Annually provide a written 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.	6.C.(2)(i)
12	Supervise the contractual performance of any contracted functions.	6.C.(3)(b)
13	Monitor and, as appropriate, conduct audits to assure that any contracted function is properly performed.	6.C.(3)(b)(i)
14	Annually obtain 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.	6.C.(3)(b)(ii)
15	Monitor the conduct of financial professionals seeking to rely on the safe harbor provision.	6.E.(3)(a)
16	Provide the entity responsible for supervising financial professionals relying on the safe harbor provision, with information and reports that are reasonably appropriate to assist such entities in maintaining their supervision system.	6.E.(3)(b)

This document is designed to provide an outline of the key compliance implementation considerations associated with the 2020 version of the NAIC Suitability in Annuity Transactions Model Regulation for the benefit of CEFLI's members and does not constitute legal advice.