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2026 CFTC

**Suitability/Best
Interest/Fiduciary
Obligations- Evolving
State & Federal Sales
Standards**

cefli | 





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Agenda

- ✓ How we got here
- ✓ Where are we
- ✓ Where are we headed

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How We Got Here



Suitability- The Early Years



Concerns about inappropriate annuity sales practices came to light in the early 2000s

Securities suitability standards

- *FINRA Rule 2111 (originally NASD Rule 2021)*

Early state regulatory focus

- *Initially aimed at both life and annuity products; evolved to strictly annuities*
- *2006 original NAIC model suitability regulation*
- *Aimed at individuals age 65+*

Suitability- Evolution

Concerns continue to exist

NAIC Suitability In Annuity Transaction Model Regulation

- *2010 revision -applies to all annuity transactions*
- *Insurance companies responsible for sales activity*
- *Insurance companies must supervise annuity sales*
- *Required enhanced producer education*

SEC- Regulation BI

Regulation Best Interest

Adopted June 5, 2019

- ✓ *Designed to enhance quality and transparency of retail sales of securities*

Ensure sales and actions are in the “best interest” of a consumer

- ✓ *Required disclosure of conflicts and a description of the products and services being provided (Form CRS)*

NAIC Redux- What About BI?



Shift of focus from “suitability” to “best interest”

- Threw out work being done to shift to a fiduciary standard after Fifth Circuit ruling
- Started over with an eye toward compatibility with SEC Reg BI
- Adopted revised Suitability In Annuity Transaction Model Regulation in 2020
- Incorporates “best interest” standard applicable to the sale of annuity products
- Still called “suitability” while incorporating “best interest” as the standard

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Where Are We

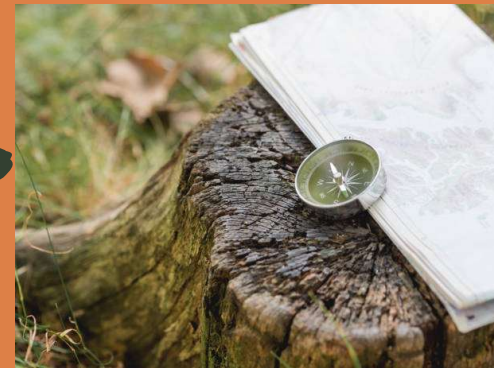


Patchwork of Requirements

Applicable standards of care depend on:

- ▶ The product sold
- ▶ The entity or individual selling it
- ▶ The state of issuance (or solicitation), and
- ▶ Funding sources

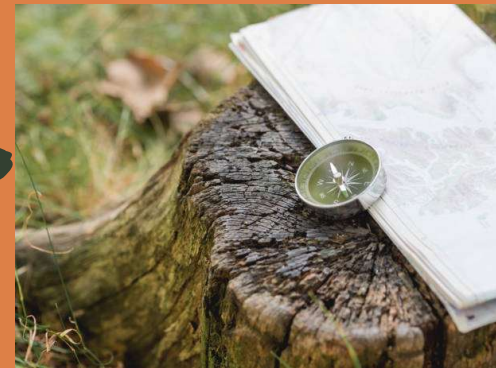
Multiple, unrelated entities may have obligations related to the same recommended transaction



FINRA Requirements

- FINRA broker-dealers and their registered representatives are subject to suitability standards for sales of variable life insurance and annuity products to retail investors
- These requirements now apply in varying degrees due to SEC Reg BI
- **FINRA Rule 2090 (Know Your Customer- KYC)**
- Requires that a broker-dealer make reasonable efforts to know essential facts about each customer

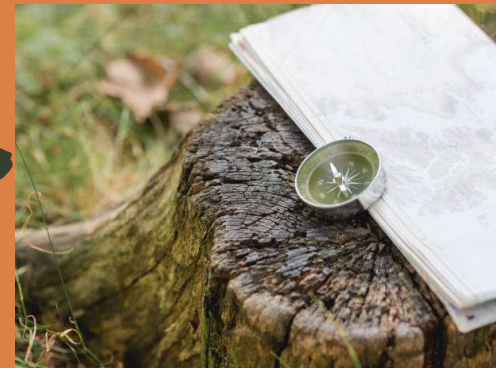
The rule applies to all customers of a broker-dealer



FINRA Requirements

FINRA Rule 2111 (Suitability). Requires that a broker-dealer or registered representative “have a reasonable basis to believe that a recommended transaction or investment strategy involving a security, or securities, is suitable for the customer [...]” *The rule applies to institutional investors only now, due to Reg BI.*

FINRA Rule 2330 (Variable Annuities). Defines additional, product-specific requirements for broker-dealers and registered representatives to consider when recommending a variable annuity. *This is in addition to Reg BI requirements.*

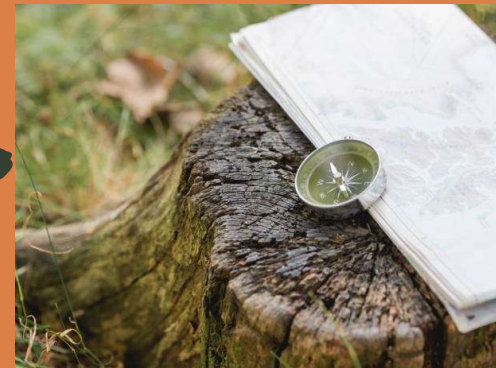


SEC Regulation BI

FINRA-registered broker-dealers were subject to suitability standards

SEC-registered investment advisers were subject to fiduciary standards

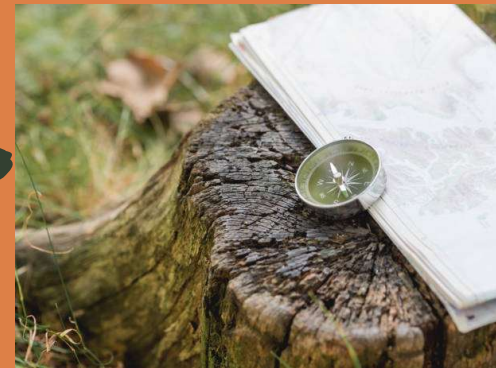
The SEC issued Reg BI to establish a uniform sales standard applicable to registered representatives of broker-dealers as well as investment adviser representatives



SEC Regulation BI

“Regulation Best Interest codifies the fundamental principle that investment professionals should not put their interests ahead of the interests of their clients and customers.”

-Former SEC Chairman Jay Clayton



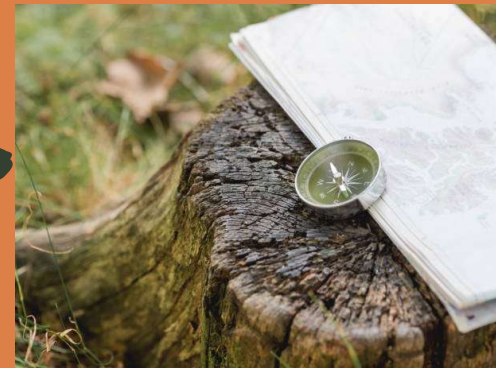
SEC Regulation BI

Four primary obligations

- 1) Disclosure obligation
- 2) Care obligation
- 3) Conflict of Interest obligation
- 4) Compliance obligation

Effective June 30, 2020

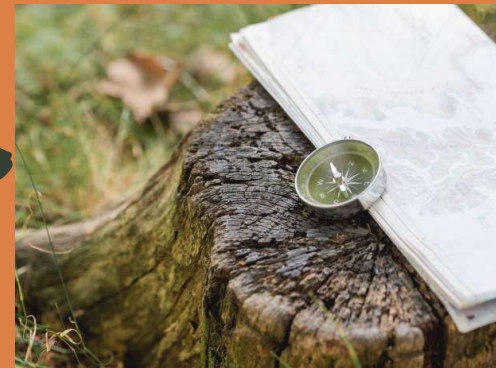
Compliance is a top SEC exam priority



SEC Regulation BI

CEFLI maintains information and resources on the *Additional Resources* page of its website, including:

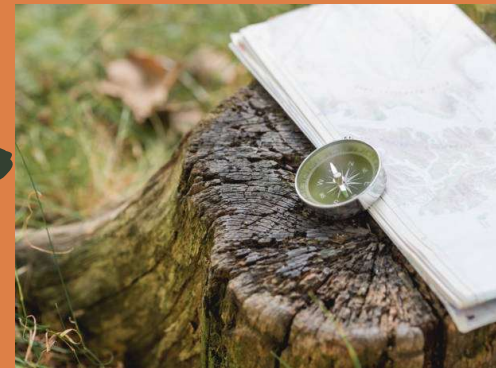
- Links to SEC content regarding Reg BI
- Links to SEC content regarding SEC Form CRS
- Executive summary of SEC Reg BI & Form CRS roundtable



SEC Regulation BI

How does this impact insurers?

- ★ Applies to securities recommendations to retail investors
- ★ This could include variable annuity, registered annuity, and variable life recommendations
- ★ Focus is on the broker-dealer or registered investment advisor making the recommendation



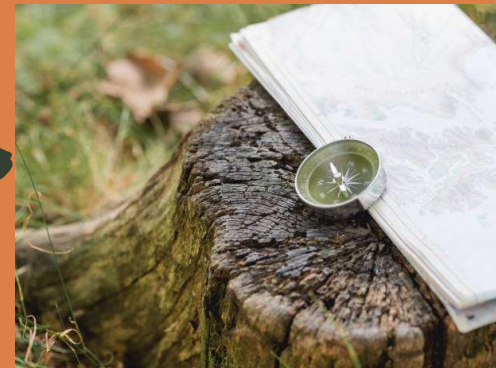
NAIC Suitability Model

The 2020 version of NAIC Suitability In Annuity Transactions Model Regulation (Model) establishes a “best interest” standard for any sale or recommendation of an annuity (with certain exceptions noted in the Model)

Revisions made in 2020 represent an effort by the NAIC to follow the core elements of the SEC’s Regulation Best Interest

49 states as well as DC* have adopted the Model

*DC awaiting final adoption



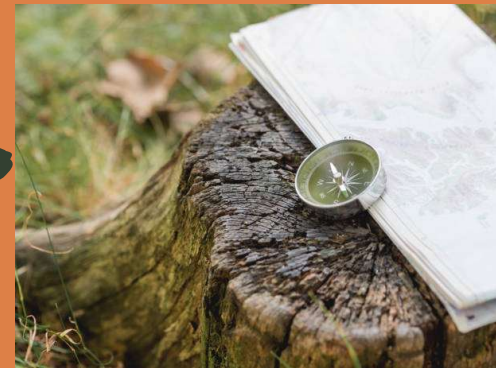
NAIC Suitability Model

The 2020 version sets requirements for producers (*who may also be registered representatives or advisors*) and insurers

Producers are subject to obligations similar to Reg BI:

- 1) Disclosure obligation
- 2) Care obligation
- 3) Conflict of Interest obligation
- 4) Documentation obligation

Insurers must implement a supervisory system
to ensure compliance



New York Reg 187

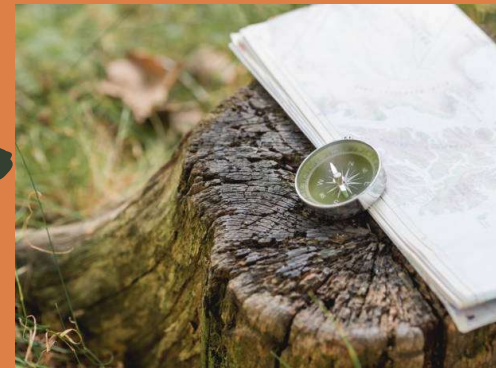
New York maintains a different legal and regulatory structure when compared to other states

The New York Department of Financial Services (NYDFS) did not adopt the Model

NYDFS Regulation 187 applies a “best interest” standard to annuities **and** life insurance products

The regulation was the first...

- state insurance department “best interest” standard
- “best interest” standard to apply to life insurance product sales



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Where Are We Headed

Structure of an Effective Compliance Program

Considerations

- ❑ Carefully review current insurance Model Regulation
- ❑ If you sell in NY- review Reg 187 and Reg 60
- ❑ Consider your distribution partners' regulatory responsibilities
 - Broker-Dealers, other insurers, IMO's, Investment Advisors
- ❑ Are you going to delegate any obligations to a third party or operate under the Safe Harbor provision?
- ❑ Contemplate your company's organizational size/structure to assess the who/what/where for addressing regulatory obligations with an eye toward perceived conflicts

Key Elements of the Program

- ✓ Informing producers of regulatory obligations
- ✓ Producer training
- ✓ Informing consumers
- ✓ Reviewing recommendations prior to issuance
- ✓ Detecting unsuitable sales
- ✓ Reporting to senior management

Information & Training Producers

Consider the following:

- ✦ *Do you publish your annuity sales guidelines on a producer-accessible site?*
- ✦ *Can producers access training or FAQs on-demand?*
- ✦ *How often do you review/update? What are triggers to do so?*
- ✦ *Do you have producer training controls in place?*

Safe Harbor Considerations

- ✓ Authority to utilize a “like” regulatory entity to determine suitability and best interest
- ✓ SEC Regulation BI and use of Form CSR
- ✓ Different from delegating – yet related
- ✓ Company still responsible for determining that the other regulatory entity is used properly
- ✓ Requiring oversight in the selling agreement
- ✓ Has been a point of consternation between regulators and industry
- ✓ Recent NAIC Guidance on the issue

Safe Harbor Supervision

Effective monitoring by the Company can include the following:

- ✓ The Contract –A written contract reduces misunderstanding as to who is doing the supervising; conveys expectations; requires performance of contracted responsibilities
- ✓ Onboarding –Ensure policies and procedures will satisfy the safe harbor
 - Review for regulatory actions
 - Do the policies apply to the sale of unregistered annuities?
- ✓ Ongoing monitoring
- ✓ Due diligence/compliance questionnaires: may be stand-alone or wrapped into a larger process to review other non-suitability requirements

Safe Harbor Supervision

- ▶ Demonstrate periodic engagement with the entity's compliance and/or legal team
- ▶ Use data analytics to categorize sales data from a risk perspective
- ▶ Sort data by number of contracts and by premiums for a risk-informed review of producers for key elements such as sales to older consumers, free-look cancellations, early surrenders, replacements, etc.

Safe Harbor Supervision

- ◀ An effective audit program including selecting adequate sample size on a frequent basis
- ◀ An escalation procedure for failure to respond - selection of frequency should be risk-based
- ◀ A regulatory exam that focuses on the supervising entity's annuity sales is strong evidence that can be relied upon as part of a monitoring program
- ◀ Certifications of compliance from the supervising entity are required annually

Information & Training Producers

Consider the following:

- ❖ Track producer activity- are there trends for certain producers or partners?
- ❖ Information for producers where you commence relationship- should they attest?
- ❖ Regular program communications to producers- maybe use an existing newsletter?
- ❖ If you have wholesalers- do you have an oversight program for their activity related to annuity sales?
- ❖ Understand which standard of care a third party utilizes

Information & Training Producers

Consider the following:

- ▣ Review wholesaler presentations
- ▣ Audit or attend certain wholesaler presentations
- ▣ Formal Producer Training Document (internal facing)
- ▣ Include suitability/best interest requirements in annuity product training courses
- ▣ Review production trends (and complaints) to determine if producers may need further training

Consumer Disclosure & Feedback

Consider the following:

- Promote use of consumer-facing education materials
- Include a short high-level summary of the product with the contract delivery
- Use call out programs or consumer surveys (via email or mail, possibly leveraging LIMRA)
- Use internal resources or external

Reviewing Recommendations

Prior to issuance, consider the following if delegating to a Third Party:

- *Get copies of guidelines/procedures for review as part of due diligence process (before signing agreement)*
- *Annuity certification process using CEFLI–Standardized forms*
- *Regularly sample third party files to verify compliance (risk-based and random)*

Reviewing Recommendations

Prior to issuance, consider the following if performing the review internally:

- ▶ Where review team sits within the organization and team lead
 - CCO, chief supervision officer? Band level?
- ▶ Review forms– maybe allow for more information to help assess and defend?
- ▶ Hard and soft flags based in part of Model language and 2330
 - Concentration, liquidity limits, age limits, etc.
 - Formal approval if flags tripped?
- ▶ Supervision help desk?

Reporting to Senior Management

Annual Suitability Report

The Annual Suitability Compliance Report should provide leadership with a snapshot of the program and summarization as to why the program remains well-designed

Length. 3-5 pages likely light; 30+ pages likely excessive; but will vary by company and program (e.g., if supervision is delegated it may be a shorter report)

Reporting to Senior Management

Annual Suitability Report

- ❑ Status update and details on the reviews conducted and recommended changes to program
- ❑ Results from complaint tracking reports (and corrective actions taken)
- ❑ Results from testing
- ❑ Report on FINRA firm annual certification process
- ❑ Reports on state or federal exams or audits applicable to the suitability program

Detecting Unsuitable Sales

You should be tracking complaints, customer questions, early surrender rates, etc.

- Think about MCAS data points regulators will review
- Recognize that MAWG continues to monitor the marketplace and will contact companies as they deem appropriate
- Anticipate future market conduct exams focused on validating the industry's compliance with the revised Model Regulation

Future Trends & Considerations

Where will we be in 3-5 years?

Regulatory requirements/expectations will only grow!

The questions are:

- ✧ How much?
- ✧ Timeline (e.g., economy changes, political changes, news articles, new industry entrants, Insurtech)?

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Questions



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Thanks Calvin and Dave!

PLEASE PROVIDE US WITH SESSION FEEDBACK USING THE QR
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Up Next

BREAK UNTIL 10:45 AM