EquiTrust

NAIC Revised Suitability in Annuity Transactions Model Regulation

What Is It? What's New? How Does It Affect Me?

In February 2020, the NAIC adopted the much-anticipated Revised Suitability in Annuity Transactions Model Regulation (#275). While the NAIC's 2010 Model Regulation established a "suitability" standard, the Revised Regulation requires that the producer act in the best interest of the customer when making recommendations for the purchase of an annuity, without putting the producer's or insurer's interests above the customer's. The best interest obligation is applicable to every producer that exercises material control or influence in the making of a recommendation and receives direct compensation, regardless of whether the producer has had any direct contact with the consumer. The heightened best interest standard is met by meeting four distinct obligations: care, disclosure, conflict of interest, and documentation, as discussed in more detail below.

Reasonable Diligence, Care and Skill: The producer must "exercise reasonable diligence, care and skill" when making a recommendation by:

- Knowing the customer's financial situation, insurance needs and financial objectives;
- Understanding the recommendation options after making an inquiry into the options available to the producer;
- Having a reasonable basis to believe the recommendation addresses the customer's financial situation, objectives, and insurance needs;
- Communicating the basis of the recommendation.

As part of the Revised Regulation, the NAIC expanded the information that the producer is required to collect when determining a "consumer profile."

At a minimum, the producer is required to collect:

- age
- annual income
- financial situation and needs
- including debts and other obligations
- financial experience
- insurance needs
- financial objectives
- intended use of the annuity
- financial time horizon
- existing assets
- liquidity needs
- liquid net worth
- risk tolerance - including a willingness to accept non-guaranteed elements in the annuity
- financial resources used to fund the annuity
- tax status

EquiTrust has added additional data fields to the Financial Needs Analysis form in order to make sure that the producer collects every data element required under the Revised Regulation at the time of sale.

While the Revised Regulation enhances the producer's obligations to customers, the producer is not required to consider products outside the scope of his/her authority and license, nor does it create a fiduciary duty.

The producer must have a *reasonable basis* to believe the consumer would benefit from certain features of the annuity and the producer must be able to communicate the basis of the recommendation.

The producer is not required to choose the product that simply has the lowest compensation structure, but the producer must consider the contract as a whole, including product features, riders, and subaccounts at the time of purchase.

If the sale involves a replacement contract, the producer must consider if the replacing product would *substantially benefit* the customer and consider whether the customer has had another replacement in the last 60 months.

Disclosure: One significant change to the Suitability Regulation is related to the information the producer is required to provide to customers. Under the Revised Regulation, the producer must provide:

- a description of the scope and terms of the relationship with the customer and the producer's role in the transaction;
- an affirmative statement on whether the producer is licensed and authorized to sell fixed annuities, fixed indexed annuities, life insurance, mutual funds, stocks and bonds, and CDs;
- an affirmative statement describing the insurers that the producer is authorized and appointed to sell, using the following descriptions: one insurer, two or more insurers, two or more insurers although primarily contracted with one insurer;
- a description of the sources and types of cash and non-cash compensation to be received by the producer;
- a notice of the customer's right to request additional information regarding the cash compensation received. If the consumer requests, the producer must disclose a reasonable estimate of the cash compensation to be received and whether the compensation is a one-time or multiple occurrence amount.

Changes to EquiTrust's Financial Needs Analysis form incorporate the additional requirements under the Revised Suitability Regulation.

Conflict of Interest: Under the Revised Regulation, the producer must identify and avoid or reasonably manage and disclose material conflicts of interest. Material conflicts of interest include a financial interest that a reasonable person would expect to influence the impartiality of a recommendation but *does not* include cash or non-cash compensation.

Documentation: At the time of recommendation or sale, the producer must document any recommendation and its basis in writing. If the customer refuses to provide consumer profile information, the producer must obtain a statement signed by the customer that documents the customer's refusal. Furthermore, if the customer decides to buy an annuity that is not based on the producer's recommendation, the producer must obtain a statement signed by the consumer acknowledging this.

Changes to Training: Under the Revised Regulation, suitability training must include "standard of conduct" content. Producers who have already completed the annuity course required under the 2010 model regulation requirements need to complete either a new 4-hour training course or an additional one-time, 1-credit training course to provide education pertaining to the new standards and requirements of the amended regulation. The training requirements will be rolled out as states adopt the Revised Regulation.