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Honorable James V. Regalbuto, Deputy Superintendent for Life Insurance
New York Department of Financial Services
One State Street
New York, New York 10004-1511

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Re: Comments of the National Association of Insurance and Financial Advisors-New York State, Inc. (NAIFA-NYS) on the second draft of the Proposed First Amendment to Regulation 11 NYCRR Part 224 (Regulation 187) – *Suitability in Life Insurance and Annuity Transactions*

Dear Deputy Superintendent Regalbuto:

Thank you for the opportunity to comment on the second draft of the proposed First Amendment to Regulation 187, 11 NYCRR Part 224.

NAIFA-NYS represents thousands of life insurance agents and brokers, financial advisors and their associates, and others in the financial services community throughout New York State. The members of NAIFA-NYS, in turn, represent through trust-based relationships tens of thousands of New Yorkers who have wisely and appropriately entrusted their financial security needs to these licensed and regulated professionals. NAIFA-NYS members have dedicated themselves to the Association's 98-year tradition of upholding the highest ethics of their profession. They have taken pride in assisting New York's life insurance and financial product clients in making important decisions to protect their family's financial future. Our members, with and through the licensed insurance and financial products companies operating in New York, provide needed advice on asset management, growth of personal net worth, employee benefits, retirement planning, college funding, business succession, and legacy planning, among other services.

In today's world, where under-saving for retirement and deficiencies in personal financial security are two sad realities, the work of these advisors and agents is more vital than ever. NAIFA-NYS has proudly worked with regulators and legislators to further the public discussion on how to improve access to sound retirement and financial products. We consider the exchange on Regulation 187 to be as much about these concerns as they are about any other public policy objective.

The second draft of the proposed regulatory amendments contains numerous changes from the first draft. NAIFA-NYS appreciates the DFS efforts to attempt to accommodate some of our comments, as well as various comments of other interested parties in the new draft. However, in most cases the changes do not solve the inherent problems with the regulatory amendments. We believe that despite the regulatory goals of the Department as reflected in this draft, the implementation of this regulation will lead to significantly less consumer access to life insurance financial products. It is likely that fewer products from an ever decreasing number of life insurance companies and producers willing to do business in this state will be its unfortunate progeny. Given our members' strong beliefs that such a counterproductive result will ensue from the current DFS efforts, we encourage the Department to slow down the administrative process of this regulation's adoption and undertake a more fundamental examination of the supporting justification and legal grounds for these regulatory amendments.

More to the point, NAIFA-NYS strongly believes and requests that the DFS suspend its efforts on the current draft of Regulation 187 in favor of the public discussion going on at the National Association of Insurance Commissioners in conjunction with other financial regulators, including the federal Securities and Exchange Commission. Further, NAIFA-NYS requests that DFS conduct public discussions in-state on the ramifications of any Regulation 187-like initiative on consumers, producers, insurers and product-issuing financial institutions. The Department's recent public roundtable on bail bondsmen is a perfect example of the kind of forum that should be conducted before this Regulation moves forward in any form. No such public forum on the state of the life insurance market has taken place.

<u>PROPOSED SUITABILITY AND BEST INTEREST STANDARDS FOR LIFE INSURANCE ARE INAPPROPRIATE AS DRAFTED</u>

We reiterate, from our initial comment letter, that providing sound recommendations and performing capable advisory services that are in the client's best interest come second nature to NAIFA-NYS members. Our members know that adherence to these principles builds trust and is essential to succeeding in this business. However, this unprecedented effort at codification of a best interest standard for *all* life insurance products and not just qualified money products, including in-force transactions, presents guaranteed negative consequences for consumers in New York's life insurance marketplace. We are troubled that the Department has not heeded our warnings, and the warnings of New York's life insurers in this area when developing the second draft of the proposed regulation.

We have urged that the proposed regulation again be limited to annuity products. We would be happy to work with the Department over a longer period of time to develop a modified version of suitability and best interest standard for life insurance products that would minimize the negative impacts of the proposed standard.

The current proposal is far too cumbersome and complicated for most life insurance products and transactions. Regulation 187 as drafted will deter producers from marketing lower-priced products, denying access to valuable producer advice for those very consumers who need it most, those in the middle and lower-middle classes. The production burden would far outweigh any transactional benefit to the client or financial benefit to the producer.

The DFS rationale, as related to us, for extending these standards to the life insurance market are limited to two basic reasons: the first is a desire for one consistent standard across all available products so as not to confuse the consumer, regardless of the negative implications of the "one-size-fits-all" approach; the second is the fact that some products have been improperly sold to consumers in the replacement context. There are currently different requirements for life insurance sales and annuity sales and none of our members has reported any client confusion by these different requirements. Importantly, the DFS has not provided one element of factual or empirical support for its notion that there is any difficulty in the marketplace with differing approaches for relatively simple and straightforward life insurance products, and more complex annuity sales.

The instances of improper replacements raised by the DFS appear to be very limited in scope compared to the size of New York's life insurance market and, again, no substantive support is provided to validate its concerns. Imposing these sweeping legal standards to the entire marketplace, based on a comparatively small number of improper replacement sales is not the best way to handle the problem. Amendments to Regulation 60 would be the best and most surgical way to correct any chronic problems in this area. Further, the imposition on all of New York's life insurance producers is far too great of a burden on their business without sufficient basis. As one of our members put it at a recent conference, "with this regulation the Department is making *all of us the bad guys".*

In the "Assessment of Public Comments" the Department did not directly address comments that it should disclose reports or studies conducted by the Department that evidence a need for this proposal. Instead, the Department cited news releases, articles, reports from the federal Department of Labor (DOL) and its Regulatory Impact Analysis as the major sources substantiating the need for this regulation. However, the DOL rule applied only to products sold in a qualified employer plan and did not apply to all life insurance products. In fact, the extension of a suitability and best-interest standard of the type in the current proposal has not been instituted anywhere in the nation. Thus, reliance on the work of the DOL rule to justify the need for a best-interest standard for life insurance sales is misplaced.

In short, the extension of a suitability and best interest standard to all life insurance product sales is not necessary, given the significant existing statutory and regulatory protections that protect New York's consumers. Further, the Department has not sufficiently investigated this unprecedented extension of regulatory authority and has, instead, relied on the findings of a Federal agency that did not examine such standards in relation to life insurance products in the first place.

<u>THE AMENDMENTS FUNDAMENTALLY CHANGE THE NATURE OF INSURANCE AGENCY</u>

Section 2101(a) of the New York Insurance Law reads, in pertinent part, as follows:

> In this article, "insurance agent" means any authorized or acknowledged **agent of an insurer**…who acts as such in the *solicitation of, negotiation for, or sale of*, an insurance, health maintenance organization or annuity contract, other than as a licensed insurance broker…(Emphasis added)

It is undisputed that an insurance agent acts on behalf of an insurer pursuant to both the laws of New York and contractual obligations existing between agents and the insurers on whose behalf they operate. This statutory mandate is juxtaposed to the statutory definition of "insurance broker", which provides for the same *soliciting, negotiating or selling*, but **on behalf of the insured, NOT the insurer**. [Sec. 2101(c)] This statutory distinction is not insignificant, and it has been a cornerstone of statutory, regulatory and enforcement treatment of brokers and agents for decades.

The proposed regulation, through the use of an amorphous "producer" term without recognition of the distinction between the differing statutory definitions, is fatally flawed on its face. Nowhere in the insurance law is the superintendent provided authority to singularly ignore the statutory definitions in favor of one that is in clear conflict with the insurance law. In fact, the insurance law acknowledges use of a "producer" term but only when such does not otherwise create a conflict with the definitions of "agent" and "broker."

We know that the Department will apply this distinction between agents and brokers in many areas. Recently, the Department visited the issue of whether life insurance policies could contain provisions for fee-based compensation for agents. The Department refused to approve such policies on the basis that agents may only be compensated by the insurer and thus, may not receive a fee from the consumer. This is an obvious recognition by the Department that the agent relationship with the insurer is inherently different than that of a broker.

NAIFA-NYS, representing both agents and brokers, finds this aspect of the regulation particularly troubling. Our members take seriously the distinction between these classes of producer, and also take on specific legal liability to their counterparties depending upon which classification they choose to embrace in their practices. This is given virtually no consideration by the Department.

We submit that if the Department wishes to alter the nature of the agency relationship it should seek such a change from the state legislature and should not attempt to do it through a regulation.

<u>THE PROPOSED AMENDMENTS IMPOSE A FIDUCIARY STANDARD WITHOUT SUFFICIENT STATUTORY AUTHORITY</u>

The express authority for the proposed amendments is Insurance Law sections 2103, 2104, 2110, 2123 and 2208, 3209, 4224, 4226, 4525 and Article 24. These statutory provisions are insufficient to support the promulgation of such a broad-based regulation that imposes a fiduciary duty on the life insurance producers of New York. While several of these statutes prohibit producers from being untruthful with a consumer or misrepresenting the terms of a policy, not one of these statutory provisions provides the authority for the Department to impose a "best interest" standard. The provisions of this proposed standard require the producer to go well beyond the statutory standard of being truthful and accurately representing the terms and provisions of the policy. The proposed standard essentially places the producer in the position of a fiduciary to the consumer, which is authorized nowhere in the cited statutes.

The DFS has stated that the "best interest" standard is not a fiduciary standard. However, in the Assessment of Public Comments to the proposed regulation, the Department indicates that its "best interest" standard is not inconsistent with the "Code of Ethics and Standards of Conduct" adopted by the Certified Financial Planner Board (CFP). A review of that Code indicates that it requires its advisors to be a fiduciary to the client. It is apparent that the DFS, either intentionally or not, has created a fiduciary standard for New York's producers. This proposed regulation has no authority in the statutes cited by the Department. The authority for any such requirement, whether advisable or not, must be enacted by the legislature and is currently beyond the authority of the Department to promulgate.

"BEST INTEREST STANDARD AND PRODUCER COMPENSATION"

Our initial comment letter expressed concern with the producer compensation language in the "best interest" standard. While we appreciate that the Department heard our concerns about the "without regard" language, the new language in the second draft fails to alleviate our concerns. The proposed regulation now requires that producer compensation "shall not be considered in any respect". [Sec. 224.4(b)(1)] This new language creates a fiduciary standard that is not realistic in the current producer marketplace. In a business dependent on commission sales, it is simply not realistic to demand that compensation "shall not be considered in any respect". We can envision situations where more than one product may be "suitable" and in the "best interest" of the consumer. Our members fear that if they recommend one of those products that pays a bit more compensation than the others, that they would be violation of this regulation. Further, many producers participate in complicated insurer incentive compensation. It is unclear what the result of the application of the proposed regulation's language to such arrangements would be. Retaining this language would be paramount to setting many well-intentioned producers to fail.

We continue to urge that the Department adopt a standard that prohibits compensation from being the "primary" reason for a producer to recommend a policy.

THE DIRECT SALES EXEMPTION MUST BE REMOVED

The proposed regulation exempts "purchase of a policy where the application is solicited and received in response to a generalized offer by the insurer by mail or under other methods without producer involvement and where there is no recommendation made;" [Sec. 224.2(a)]. In the interest of uniform consumer protection and fundamental fairness to all engaged in the production of insurance and financial products, this exemption must be removed, and the proposed regulation be clarified to apply to all policy sales whether or not a producer is involved.

This exemption is problematic for several reasons. First, since the regulation defines "policy" as a "life insurance policy, annuity contract or a certificate issued by a fraternal benefit society…" the exemption could apply to annuity sales. At least one life insurer has announced—ironically, after the issuance of the first draft of the proposed changes to this Regulation—that it will soon add an annuity to its direct sales platform. This means that consumers could be purchasing annuities without any recommendation and outside the protections of this Regulation. This cannot possibly be the result intended by the Department.

Further, the exemption creates an unfair playing field for producers. Insurers and the third parties with whom they work could be increasing sales on a direct basis, asking the consumer to simply check a box next to the amount of coverage desired. The consumer will be purchasing this policy without ever hearing about other available products or options. The same product being sold by a producer would be subject to the full protection of the proposed regulation. Since life insurance products are not easily sold, many consumers may simply opt for the easier method of obtaining a policy through a direct sale, without ever knowing what product available was suitable for them or was offered in their "best interest".

Since the stated goal of the regulation is to "help ensure that a transaction is in the best interest of the consumer and appropriately addresses the insurance needs and financial objectives of the consumer…" [Section 224.0(c)], the direct sales exemption will thwart this goal for large sections of the insurance-consuming community. If the Department truly believes that the provisions of this regulation will help insurance consumers, then it must make the regulation applicable to ALL policy sales.

<u>NECESSARY CHANGES TO THE PROPOSED REGULATION</u>

1. <u>Regulation's application to in-force transactions</u>. In our original comment letter, we urged the Department to omit language making the regulation applicable to in-force transactions. While we continue to support that idea, we are appreciative that the Department did remove some of the regulation's requirements for in-force transactions that do not generate new sales compensation. However, the application of the bulk of the "best interest" standard to these transactions will cause the same result that we warned about in our first comment letter, namely, that the adherence to the cumbersome "best interest" standard, *in situations where no additional compensation will be earned,* will cause many producers to abandon this service to the consumer, referring them to the insurer's help line. Unfortunately, the change made by the Department will not solve this problem. Further, the Department has not identified any current market problems with such in-force transactions of sufficient seriousness to justify such sweeping regulatory action. The solution is to omit in-force transactions entirely from this regulation.

2. <u>The consumer signed statement requirement should be eliminated.</u> The second draft of the proposed regulations contains a new requirement that the producer obtain a signed statement from the consumer in the event that the consumer either refuses to provide suitability information or decides to enter into a transaction that is not based on the producer's recommendation. [Sec. 224.4(e)(3&4)] This provision further

complicates the transaction that already is made more complicated by the rest of this regulation. In life insurance transactions, especially, it is quite common for consumers to refuse the recommended amount of insurance in order to find a face amount that is more affordable. This signature requirement needlessly makes the producer interaction with the consumer more cumbersome.

3. <u>Consumer financial ability to afford the policy.</u> The proposed regulation requires the producer to form a reasonable basis to believe that the consumer has the financial ability to meet the financial commitments under the policy. [224.4(f)] This provision is not sufficiently clear and places an unreasonable burden on the producer. A consumer's ability to meet the financial burden of a policy is a determination that requires far more financial information than is usually asked of the consumer. The ability to afford all of the financial commitments would require a complete financial statement. We are concerned that this significant intrusion by the producer into the financial affairs of the consumer will not be received well and will negatively affect the producer/consumer relationship. Further, affordability of all of a policy's commitments may be very difficult to determine. We urge to Department to eliminate this requirement.

4. <u>Prohibition on the implication that a recommendation is part of "financial planning, comprehensive financial advice, or investment management".</u> We took issue with this provision in the first draft on the basis that the language was not specific enough as to which designations would suffice for compliance with this section. We also continue to urge that the Department add language that would open up multiple sources of organizations that could issue such designations, such as NAIFA-NYS itself. While the Department did not accept our suggestions for clarification language, it added the following sentence to the second draft,

   > "A producer shall not use a title or designation of financial planner, financial advisor or similar title unless the producer is properly licensed or certified and actually provides securities or other non-financial services."

   There is a great deal of confusion amongst our members as to what this additional sentence means. Some have asserted that this means that you must have a proper federal securities license and provide securities in order to refer to yourself by the listed titles. Is this the Department's intent here? We strongly urge the Department to provide language to clarify exactly what it intends in this area. Another problem with this provision is that it creates a hardship for those members who have been defining themselves as such for many years, without a certification, providing sound and valuable advice to their clients, who would unfairly be forced to stop or seek such a certification at a very senior age. We believe the Department should include a standard that accounts for significant experience over many years of providing such products, absent a specific certification.

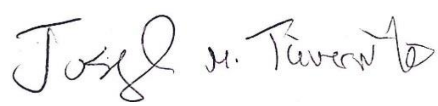
5. <u>Provision applicable to captive or affiliated producers.</u> The Department created a cumbersome provision in the second draft of the proposed amendments concerning

the consumer disclosures that are required when a captive producer limits the range of policies offered to the consumer. We are opposed to yet another Department-approved disclosure form that must be shown to the consumer. We believe that the consumer would be confused when the producer discloses the details of the arrangement made with the insurer concerning how the producer's product offerings are limited by the insurer, and when the producer may officer products from other insurers. Further, this level of disclosure will not benefit the consumer. The Department should simply require the producer to inform the consumer that his range of offerings is limited by his arrangement with the insurer, if that is the case.

CONCLUSION

We appreciate the Department's willingness to discuss this proposed regulation and we respectfully urge that the Department issue another draft for comment, taking into account our concerns as expressed in this letter. We look forward to continuing this dialog on this very important topic.

Very truly yours,



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