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Submitted by e-mail: ESBA.FiduciaryRuleExamination@dol.gov

April 17, 2017

Office of Regulations and Interpretations
Employee Benefits Security Administration
U.S. Department of Labor
200 Constitution Avenue NW, Room N-5655
Washington, DC 20210
Attention: Fiduciary Rule Examination

RE: **RIN 1210-AB79**

Definition of the Term "Fiduciary"; Conflict of Interest Rule – Retirement Investment Advice; Best Interest Contract Exemption (Prohibited Transaction Exemption 2016-01); Class Exemption for Principal Transactions in Certain Assets Between Investment Advice Fiduciaries and Employee Benefit Plans and IRAs (Prohibited Transaction Exemption 2016-02); Prohibited Transaction Exemptions 75-1, 77-4, 80-83, 83-1, 84-24, and 86-128

Dear Acting Secretary Hugler:

I am the General Counsel of Creative One Marketing Corporation ("CreativeOne"), a national life insurance and annuity brokerage organization, which is commonly known as an independent marketing organization ("IMO"). CreativeOne supports the idea of a best interest standard in the annuity and life insurance marketplace. However, the Fiduciary Rule (the "Rule") promulgated by the previous administration will result in catastrophic consequences to the middle-class retirement investors and the tens of thousands of independent insurance agents who sell annuity and life insurance products.

Without further analysis and meaningful changes to the Rule, a large share of the 80,000 independent agents selling fixed annuities may be forced to irreversibly exit this consumer-critical market. This will cause massive upheaval for the agent, distributor, insurance carrier, and most importantly, consumers of these valuable, guaranteed retirement income insurance products.

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We maintain that the Administration should undertake a more thorough analysis in crafting a fair and reasonable rule that recognizes the uniqueness and nuances of the fixed annuity marketplace. However, the Rule and the 60-day delay released by the Department only serve to add to the uncertainty in the industry. A further day is necessary to complete a substantiated economic impact and to verify if the Department is the best body to act.

The Rule and the 60-day delay is dramatically inconsistent with the new presidential administration's stated policies of: (i) increasing, not reducing, Retirement Investors' access to certain retirement savings offerings, retirement product structures, retirement savings information, and related financial advice; (ii) minimizing, not causing, dislocations or disruptions within the retirement services industry that may adversely affect Retirement Investors; and (iii) lowering, not raising, the prices that Retirement Investors must pay to gain access to retirement services. Several FAQs, proposed delays, delays, and proposed exemptions have

With these priorities in mind, this comment will focus on three key areas. First, we believe the Department failed to adequately consider the existing state-based insurance regulatory system in its analysis of harm to consumers. While also a more prudent practical actor in this space, state insurance commissions have regulated this arena adequately and have dramatically reduced customer complaints since 2010 with the enactment of new regulations. Second, the Rule, as currently written will significantly harm small businesses and consumers as many independent distributors exist the marketplace and access to insurance products to consumers dwindle. Third, the 60-day delay promulgated by the Department of April 7, 2017 has only served to further muddy the waters regarding what is expected of insurance agents after June 9.

Ultimately, our recommendation is for the Department to delay the applicability of the Rule beyond June 9 to review the true economic impact of the Rule and to craft requirements that account for the uniqueness of the industry, rather than rely on arbitrary, unsupported, and unreasonable conclusions. We believe the fixed annuity industry and consumers would substantially benefit from a more comprehensive study of the Rule and a full and complete delay of the Rule beyond June 9.

I. <u>The State Based Suitability Regulations Are the Best Avenue for Consumer Protection</u>

The Rule's economic impact analysis failed to conduct an adequate study into the impact of the 2010 National Association of Insurance Commissioner's (NAIC) model regulation regarding the sale of annuity products of consumers, commonly known as the Suitability Model ("Suitability Model"). Instead, the prior administration relied on outdated evidence that did not consider the landscape of the industry under the Suitability Model.

In 2010 the NAIC passed the Suitability Model. This new model regulation was written to establish a system to supervise the recommendations to clients to purchase or exchange an annuity and to set forth standards and procedures for recommendation so that the insurance needs and financial objectives of the client at the time of sale were appropriately addressed.

The model regulation placed the obligation for suitability annuity transactions on both the insurer issuing the contract as well as the insurance licensed agent making the recommendation. The model regulation mandated that the agent should not make a recommendation and the insurer shall not issue the contract unless each have a reasonable basis to believe the transaction is suitable to the client's needs based on the client's suitability information. The model regulation has been adopted by 39 states and the District of Columbia and has been applied by most insurance carriers on a nationwide basis since 2010.

Prior to soliciting an annuity, the insurance agent must complete a 4-hour annuity suitability training course on appropriate sales practices when recommending an annuity as well as product specific training provided the issuing insurer. When making a recommendation to a client the agent is required to gather information regarding the client's financial objectives and needs including the client's financial information. The model provides 12 factors that should be collected and considered which includes the client's:

a. Age
b. Annual Income
c. Financial Situation and needs including the financial resources used for the funding of the annuity
d. Financial experience
e. Financial objectives
f. Intended use of the annuity
g. Financial time horizon
h. Existing assets, including investment and life insurance holdings
i. Liquidity needs
j. Risk tolerance
k. Tax Status

These factors are gathered on the company's suitability or client profile form. This form is designed by the issuing insurance carrier and is part of the client file. It is the carrier's obligation to have a system in place to monitor the recommendation of the agents. The carrier is going to use the information collected on the suitability form to evaluate questions similar to the following:

a. What is the client's financial situation?
b. What is the main objective or concern?
c. How does the recommendation fit the client's current and anticipated future situation and their risk tolerance?
d. What are the strengths and shortcomings of the product being recommended?

e. How will the recommended product better assist the client in meeting the needs than the current asset allocation?

Each insurance carrier establishes and maintain a set policy and procedure to review and approve each case submitted prior to issue. The carrier can do this through an individual review of each case or automated, systematic process based on a set of established criteria. It is the carrier's obligation to maintain procedures that are reasonably designed to detect recommendation that are not suitable. This can be done through the pre-issue review process as well as post issue client surveys, telephone interviews with clients or confirmation letters to clients. Insurers' processes vary in how they review and ultimately approve or decline the annuity business and the ongoing monitoring of agent recommendations.

Insurers' are subject to routine reviews for compliance with the requirements of the model by the states in which they transact business. The state insurance authority revaluates and tests the effectiveness of the insurer's procedures and system to detect unsuitable sales. Findings of inadequate system may lead to fines by the state insurance departments. The insurers are also subject to client complaints which can include allegations of unsuitable sales.

Since the adoption of the model regulation by most states the number of consumer complaints alleging unsuitable sales has dropped significantly. According to the carriers we have relationships with, Annuity sales complaints are significantly lower now than from 2010 and have declined each year since 2010. Premium has increased and the number of complaints has decreased lowering the complaint ratio significantly year over year.

The NAIC is currently working on revisions to the Suitability Model to reflect the need to "fill any gaps in financial services sales standards."[1] The Suitability Model has been successful in reducing investor injury since its enactment in 2010. The Department should conduct further research into the existing state of affairs to determine the necessity of the Rule. If gaps exist in the current regulatory regime, the Department should consider whether the Department is the best actor to fill those gaps through the Rule or whether the states via the NAIC are more suitable to alleviate any consumer injury. The NAIC will not hesitate to act. As noted above, the NAIC has already begun discussions concerning this issue.

II. The Rule Will Devastate Small Businesses and Consumers

The Department must balance whether the harm to consumers in the status quo, even with current actions by the NAIC, outweigh the harm, that the Rule as currently written, to small businesses and consumers. It is with great earnestness and concern that we wish to advise the Department that the Rule would devastate the independent distribution of annuities channel. The

[1] http://www.thinkadvisor.com/2017/04/10/insurance-regulators-may-update-annuity-sales-mode?eNL=58ebf7ab150ba0d17a405ad2&utm_source=TA_LifeHealthNewsFlash&utm_medium=EMC-Email_editorial&utm_campaign=04102017

impacts would be felt at all levels: from the carrier to the IMO to the independent agent to the consumer. This Rule puts the accessibility of guaranteed retirement products to middle-income Americans at severe risk.

These costs will be felt far and wide. At the carrier level, we have already seen commission rates drop among some carriers 1-2% in preparation of the annuity market taking a downturn in response to the fiduciary rule. This small number has a large impact across the industry. A cut in commission rates at this level could impact an independent agent's income by as much as 25% per year, putting independent agents on the ropes and trying to decide whether to shut down their business, undergo layoffs, or keep going in this arduous regulatory landscape.

We have also begun to see carriers discontinuing significant annuity products in anticipation of the applicability of the Rule, further limiting consumer choice of different annuities. Carriers will reduce the number of products in order to avoid what could appear to be conflicts within their own portfolios and conflicts on an IMO shelf versus other companies' products. There will be an irresistible urge to standardize and incentive to collude among carriers. Even these results will not resolve an intractable problem of significant commission differences leading to class action lawyer led allegations of conflicted advice. To give just one example, most producers pay lower commissions at upper ages due to actuarial mortality effects and the annuity guarantees. However, the ages at which these breaks occur vary widely due to carrier risk acceptance and actuarial approaches yielding multiple percentage points of commission difference. Even if that could be surmounted by every company miraculously pricing the same, the result would not be positive for a competitive market for consumers. Other examples are by state approval differences, rider differences, and renewal differences.

Consumers and small businesses will also be squeezed out of the market. Assuming some workable IMO Exemption were granted, as the cost of compliance increases, it will cost the IMO, as the supervising "financial institution", a fixed cost to maintain and support each and every independent agent. For each independent agent, the IMO will have to maintain the requisite amount of insurance and create compliance and supervisory capability to cover each agent and their sales. It has become clear that IMOs will not be able to support all of their agents with such increased and new role of supervisor. Many lower producing independent agents will be squeezed out of the market as their IMO will not be able to support their administrative costs. An agent with small production at one IMO, but more significant production at another IMO may be rejected by the former. This will result in single IMO agents, making independent distribution, less independent—a negative impact on consumers.

The consumer will also face significant harm due to lowered access. As noted above, a consumer's local "mom-and-pop" insurance agent could possibly go out of business. The consumer could try to find another authorized insurance producer licensed and appointed to support their annuity, but this is highly unlikely. Many registered reps of broker-dealers do not have contracts to sell fixed indexed annuities, preferring to sell variable annuities. End even if a registered rep could obtain a license and appointment with the insurance carrier to service an indexed annuity customer, most customers would likely face the firm's minimum investable assets threshold that many broker-dealers impose to work with them—a level that many middle-income Americans won't reach. Registered investment advisors will similarly decline to support these annuity customers because most do not maintain high minimum investable asset thresholds and won't be able to charge a fee on the annuity purchased. Most RIA firms charge 1-1.5% for the average annuity customer ($250,000-$750,000 net worth), and simply do not want to serve Main Street customers because they make more money working with millionaires. Some RIA and BD firms have stated in their own industry conferences that the fee model does not work for a significant portion of the consumer base who are not millionaires. And a last theoretical BICE-approved "financial institution" are banks, yet to our knowledge no bank has agreed to serve as a "financial institution" for independent agents. Customers might also theoretically seek out a different independent agent properly appointed with their insurance carrier, but finding an authorized agent would prove impossibly cumbersome and expensive for the customer. Further, even if they located an authorized independent agent to service their annuity account, most agents would impose their own minimum investable asset thresholds and decline to serve those customers. The BICE rule and the Proposed Exemption will price out a great majority of middle-income Americans. Good retirement strategies and products will be reserved only for the rich.

III. <u>The 60-Day Delay Only Muddied the Waters</u>

While the Department will conduct its review as mandated by the February 3rd Memorandum, the Rule will become applicable on June 9. After June 9, individuals within the industry who were previously considered salesmen will now be considered fiduciaries and be forced to follow the impartial conduct standards. While the Department argues that the impartial conduct standards are the least controversial aspects of the Rule, they may also be the least explained. Overnight, many in the industry will be looking towards the Department for guidance on the meaning of a fiduciary and the requirements of the Impartial Conduct Standards. There are several important questions that remain that without additional guidance from the Department will leave newly anointed fiduciaries to litigate interpretations with zealous trail lawyers. Those issues include, how the old version of 84-24 fits into IRA annuity sales when the 84-24 was never designed to apply to annuity sales to IRAs. What are the disclosure requirements of old 84-24 plus Impartial Conduct Standards? How does the best interest exemption apply with only impartial conduct standards? Is anything required under the BICE exemption between June 9 and January 1, 2018? Does the BICE exemption between June 9 and January 1, 2018 require any disclosure to the investor? Does the BICE exemption between June 9 and January 1, 2018 require a financial institution? These questions will be answered. They will be answered either by the Department in the next 53 days or after an additional delay. Or they will be answered after millions of dollars are spent in legal fees.

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We understand that the requirements enumerated within the Rule are not without purpose. We believe in the general concept of a "best interest" standard, but unfortunately, the Rule is written in such an unworkable and burdensome manner as to put the entire fixed annuity industry at risk. We believe there are alternative methods to accomplish the goals of a "best interest" standard without devastating small businesses and consumers. The Department should fully delay the applicability date, review the current regulatory regime, and devise the most practical solution that protects consumers and preserves the viability of this desperately needed guaranteed retirement income industry—whether through the Department or another actor. Such a delay is fully warranted based on the demonstrated dislocation for the industry and harm that will occur to the consumer. Robust regulatory consumer protections will continue to be applied and enforced during the Administration's review, justifying a thoughtful reconsideration of the Rule in its entirety. The fixed annuity industry and the fixed annuity customers deserve more time to engage in meaningful dialogue with policyholders and other stakeholders to avoid a cataclysmic impact.

Thank you in advance for considering these comments. If you have any questions or if we can be of assistance, please feel free to contact me.

Sincerely,

Andrew Payne

Andrew Payne
General Counsel
CreativeOne Marketing Corporation