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August 30, 2010

**By Electronic Delivery**

Ms. Elizabeth M. Murphy  
Secretary  
Securities and Exchange Commission  
100 F Street N.E.  
Washington, D.C. 20549-1090

Re: Request for Comment to Inform Study Regarding Obligations of Brokers, Dealers, and Investment Advisers (Release No. 34-62577; IA - 3058; File No. 4-606)

Dear Ms. Murphy:

The American Council of Life Insurers ("ACLI") is a national trade association with 300 members that represent more than 90 percent of the assets and premiums of the life insurance and annuity industry. We appreciate the opportunity to share our views on the subjects under review and consideration as part of the Securities and Exchange Commission ("SEC") Study Regarding Obligations of Brokers, Dealers, and Investment Advisers (the "Study").

Our letter begins with a discussion of the unique nature of insurance product distribution and explains the extensive regulatory network governing the sale of insurance products. We then provide comment about key considerations as the SEC conducts the Study, and in particular the methodology which we believe the SEC should employ in analyzing the issues being examined. Our letter concludes with comments relating to harmonizing the broker, dealer ("BD") and investment adviser ("IA") regulatory framework. An executive summary appears early in our letter.

At the outset, we wish to note that we have substantial interest in the Study. Our members offer and distribute life insurance, annuities and other products such as mutual funds, individual securities and 529 plans through affiliated and independent distributors, including BDs and IAs. We believe that registered representatives ("RR" or "RRs") of BDs directly affiliated with the life insurance industry represent a majority of the associated persons associated with the BD industry. IAs also provide advice to clients with respect to the life insurance and annuity products which our members distribute.

We hope that the comments set forth in this letter will continue the constructive dialogue in which we have engaged with the SEC and other interested parties regarding the standards of care for BDs and IAs and related investor protections for retail customers.

## Executive Summary

- The insurance distribution and sales process is one of the most heavily regulated of the financial services available in the marketplace today - Part I of our letter summarizes the applicable regulatory framework related to the process and we have also attached as an appendix (please see Appendix A), ACLI's prior submission to the RAND Corporation Study (the "ACLI RAND Study Submission") to highlight the extensive network of laws and regulations governing our members' and their associated persons' activities that directly relate to the issues within the scope of the Study.
- The SEC should use the Study as an opportunity to approach the issues in a comprehensive manner, and to perform a rigorous analysis of the applicable existing regulatory regime, identify those things that are working well and those that are not, and evaluate the likely consequences to the retail and other investing public and the industry from any potential changes. We discuss the Study further in Part II of our letter.
- If after a comprehensive evaluation, the Study findings and results lead the SEC to determine that harmonization of the regulation applying to BDs and IAs when providing personalized investment advice to retail customers will provide tangible and concrete investor protection benefits to retail customers without significant adverse consequences to retail customers, any such harmonization efforts should be advanced with a view to the preservation and/or enhancement of:
  - investor protection for retail customers;
  - choice regarding securities products and services for the full spectrum of retail customers; and
  - access to those securities products and services for the full spectrum of retail customers.

This is discussed further in Part III of our letter.

### **I. The Unique Nature of Insurance Product Distribution.**

In this part of the letter we first discuss the operation and activities of insurance-affiliated BDs and then we discuss the regulatory framework applying to insurance product distribution.

#### **A. The Operation and Activities of Insurance-affiliated BDs**

BDs affiliated with life insurance companies are significantly different from full service or "wire-house" BDs in their operations, products and services.

One type of insurer-affiliated BD is strictly a "wholesaler" - distributing the insurance company's variable products through affiliated and unaffiliated selling BDs. This type of BD generally does not engage in retail activities and does not maintain possession or control of customer funds or securities. Those insurance company employees who perform wholesaling duties or certain related activity are generally registered with the insurer's wholesaling BD. Care should be taken in any rulemaking to distinguish these types of wholesaling BD activity from retail sales BD activity.

Another type of insurer-affiliated BD engages in retail securities activities primarily in the context of a larger insurance business. Many RRs associated with these BDs operate principally as life insurance and annuity salespersons. Securities sales can frequently constitute an incidental amount of business relative to insurance product sales by an office or RR. In some cases, the insurance-affiliated retail BD may sell a broader array of securities products, including mutual funds, 529 Plans and individual securities. Certain of these BDs and a segment of their RRs are dually registered as IAs and investment advisory representatives (“IAR” or “IARs”), respectively, and also offer various IA services such as financial planning for a fee and managed accounts. As a by-product of this type of insurer-affiliated BD, supervision and compliance is often conducted within the overall vehicle of an insurance distribution system. In some cases, an insurance company-affiliated BD may conduct both wholesaling and retail activity.

As a matter of perspective, it may be helpful to consider those securities activities and services generally *not* offered by most BDs affiliated with life insurers. Typically, these BDs do not, for example, maintain discretionary accounts permitting RRs to purchase and sell securities on behalf of a retail customer without specific approval of each transaction. These BDs generally do not take custody of retail customer funds, securities or assets. This type of BD does not typically “carry” customer accounts – instead they often have contractual relationships with “clearing” BDs who, among other things, execute securities transactions and take custody of applicable retail customer funds, securities or assets.

Insurance BDs usually require that payment for variable insurance or securities products be made by check payable to the processing office of the underwriting insurer, and not by check payable to the agent/RR or even to the BD. Additional purchases, transfers, withdrawal and redemption requests for these products are typically submitted to the underwriting insurer, not to the RR or the BD. Variable contracts and shares in investment companies are issued directly to purchasers and do not constitute bearer instruments. Consequently, the opportunity for misappropriation of these instruments by these RRs is greatly mitigated and in certain instances virtually nonexistent.

We respectfully offer this background to highlight the diversity within the BD universe, and the need for careful rulemaking that appropriately accommodates different business models, organizational structures, product lines, and compliance and oversight operations.

## **B. The Regulatory Framework Applying to Insurance Product Distribution**

Life insurance companies and their associated persons currently comply with a comprehensive array of regulation administered by state insurance departments, the SEC, the Department of Labor, Financial Industry Regulatory Authority (“FINRA”) and various state securities divisions and departments. Quite simply, and as similarly noted above, the insurance industry distribution and sales process is one of the most heavily regulated of the financial services available in the marketplace today.

For your reference and convenience, we have included the ACLI RAND Study Submission, which is attached to this letter as Appendix A to outline the important and significant role life insurers and their distributors play in the IA and BD industries, and to highlight the extensive network of laws and

regulations governing their activities that directly relate to the issues within the scope of the Study.<sup>1</sup> With this detailed information at hand, we believe the Study can be more fully balanced, effective and informed in its findings and any subsequent recommendations or actions that may result from the Study.<sup>2</sup>

## II. The Study

In this part of the letter we offer comment with respect to the legislative mandate governing the Study, the methodology we believe the SEC should employ in conducting the Study, the importance of the exception under section 202(a)(11)(C) Investment Advisers Act of 1940 (the “Advisers Act”), and the potential imposition of a fiduciary duty on BDs.

### A. The Legislative Mandate

Section 913 of the Dodd-Frank Act requires that the SEC, before engaging in any decision to advance rulemaking with respect to a new standard of care, conduct the Study to evaluate, among other things, the effectiveness of existing legal or regulatory standards of care for BDs, IAs and their associated persons providing personalized investment advice and recommendations about securities to retail customers imposed by the SEC and a national securities association, and other Federal and State legal or regulatory standards.

The Study specifies fourteen separate required considerations to be addressed. Those required Study considerations include “the effectiveness of existing legal or regulatory standards” and “whether there are legal or regulatory gaps, shortcomings, or overlaps in legal or regulatory standards,” and even “the potential impact of eliminating the broker dealer exclusion from the definition of ‘investment adviser’ under section 202(a)(11)(C) of the Advisers Act. Other required Study considerations include the SEC’s review of: (a) the specific instances related to the provision of personalized investment advice about securities in which the regulation and oversight of investment advisers provide greater protection to retail customers than the regulation and oversight of broker dealers, and *vice versa*; (b) the potential impact on retail customers, including the

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<sup>1</sup> The ACLI RAND Study Submission outlines in more detail the products, services and regulation of life insurance companies and their distributors and has been recently updated for your reference in connection with the Study. We note here certain key highlights of the ACLI RAND Study Submission, including:

- NAIC Suitability in Annuity Transactions Model Regulation;
- FINRA Rule 2330 (previously, designated as NASD Rule 2821) Suitability and Supervision in the Sale of Variable Annuities;
- NAIC Annuity Disclosure Model regulation;
- NAIC Model Replacements Regulation;
- ACLI Disclosure Initiative for Fixed, Index, and Variable Annuities;
- ACLI Summary Annuity Disclosure Templates and Instructions;
- The State Regulatory Framework Regarding Variable Product Sales

<sup>2</sup> Further, we include ACLI’s RAND Study Submission to assure that the SEC staff has access to the complete record, which does not appear to be available on the SEC’s website. We also note that the RAND report included scant, if any, reference to the role life insurance salespersons play in the distribution of IA and BD services. We have reviewed the original information submitted in the ACLI’s RAND Study Submission, and have updated it where laws or regulations have changed as part of Appendix A.

potential impact on the range of products and services offered by broker dealers if the Advisers Act standard and/or other requirements are applied to broker dealers and their associated persons; (c) the varying level of services provided by brokers, dealers and investment advisers and their associated persons and the varying scope and terms of retail customer relationships among them; (d) the potential impact on retail customers that could result from changes in regulatory requirements or legal standards of care, including protection from fraud, access to investment advice, and recommendations about securities to retail customers, or the availability of such advice and recommendations; (e) the potential additional costs and expenses to retail customers regarding their investment decisions; and (f) the potential additional costs and expenses to brokers, dealers and investment advisers resulting from potential changes in the regulatory requirements or legal standards.

Thus, Section 913 requires not only an investigation of whether a new or different standard of care will enhance investor protection, but also an evaluation of the potential consequences, intended and unintended, on retail customers, as well as the BDs and IAs who provide them with personalized investment advice about securities.

That is a tall order - especially given the short time-frame allowed for the Study. Nevertheless, not only is this analysis required by the statute, we believe it is critical to making an informed decision about what, if any, regulatory changes should follow and to help avoid any unintended negative consequences to retail customers. There are no easy answers to these questions, and the SEC should be wary of the notion that has been offered by some that there is a "silver bullet" for enhancing retail customer investor protection, such as elimination of the BD exception in the Advisers Act or simply imposing a fiduciary duty on BDs.

## **B. Methodology**

The outcome of the Study cannot be regarded as a *fait accompli*. Rather, the SEC should, as Section 913 contemplates, take this opportunity to perform a rigorous analysis of the existing regulatory regime, identify those things that are working well and those that are not, and evaluate the likely consequences to the investing public and the industry from any potential enhancements that are considered. This will set the stage for, if deemed necessary, an informed and tailored rulemaking that will enhance retail customer protection without unnecessarily increasing costs or decreasing retail customer choice and access to securities products and services. We believe that it is crucial for the SEC in conducting the Study to seek input and information through various means, including through interviews with associated persons of BDs and IAs and consider focus groups with a broad range of retail investors, in addition to reviewing the information provided in comment letters and the meetings with interested persons that the SEC has conducted or will conduct over the next several months.

Moreover, we believe that it is critical for the SEC to thoroughly analyze the detailed rules and multiple layers of supervisory oversight to which sales of insurance products are currently subject. As noted above, we have attached the ACLI RAND Study Submission to this letter (see Appendix A) to, among other things, outline extensive laws and regulations governing insurance product distribution and sales.

## **C. Study Topic: the BD Exception to the Advisers Act**

We note that one mandated area of the Study relates to the potential impact of eliminating the BD exclusion from the definition of "investment adviser" under section 202(a)(11)(C) of the Advisers

Act. We have significant concerns that elimination or limitation of the long standing exclusion would, among other material negative consequences to retail customers, impose substantial costs (as described below) on retail customers without any clear benefit to those retail customers.

For example, the repeal of the exception would, among other things, require all BDs and RRs who provide personalized investment advice about securities to retail customers to register as IAs or become IARs - also without any correlating benefit to retail customers. Requiring BDs and RRs who provide incidental advice about securities to register as IAs or IARs would significantly increase the cost of providing services to retail customers without any real benefit. This could result in, for example, certain portions of retail customers actually having less access to much needed personalized investment advice about securities. BDs may find the costs prohibitive to continue to provide such personalized investment advice about securities to those retail customers in less densely populated geographic areas.

#### **D. The Imposition of a Fiduciary Duty**

Some have suggested that the SEC undertake its Study with a predisposition toward imposing a fiduciary duty “label” upon BDs and their RRs. We believe that the imposition of a broad and vague label or standard will not benefit retail customers and could have the unintended negative consequence of limiting investor choice and access to securities products and services. We discuss this point in greater detail in Part III of our letter immediately below.

### **III. Harmonization**

In this part of our letter, we first offer our views with respect to harmonization generally. We then examine certain considerations which we think are critical to keep in mind regarding the phrase “personalized investment advice about securities to retail customers”—a phrase which is at the foundation of the Study. Then we set forth principles which we believe should guide the SEC’s efforts with respect to any BD and IA disclosures to retail customers. We conclude with a discussion of why we believe that any rulemaking to address gaps that are identified through the Study must focus upon concrete business conduct rules, instead of a vague, nebulous and undefined standard or label.

#### **A. Harmonization Generally**

Currently, BDs and IAs are subject to different regulations when they provide personalized investment advice about securities. IAs are subject to a fiduciary standard, while BDs are subject to standards of fair dealing and suitability rules, including the various FINRA regulatory notices and interpretative materials containing additional considerations for specific products and related matters (and, specifically, in the case of variable annuity sales, the rigorous analysis and other requirements mandated by FINRA Rule 2330).

Additionally, BDs and IAs are required to provide different types of disclosures to their retail customers at different times in the investment or engagement process. Furthermore, the advertising rules applying to each are different, as are the applicable record-keeping requirements and numerous other regulatory requirements. In the area of regulatory oversight, IAs are currently directly regulated by the SEC, while BDs are directly regulated by FINRA and also by the SEC. BDs and IAs are also subject to varying types of oversight by state securities regulators.

If after a comprehensive Study, the SEC determines that harmonization of the regulation applicable to BDs and IAs when providing personalized investment advice to retail customers will enhance the protection of those retail customers without causing significant unintended negative consequences

relating to the provision of personalized investment advice,<sup>3</sup> the ACLI believes that it is critical that it advance any related rulemaking with a view to preserving and/or enhancing:

- Investor protection for retail customers;
- Choice regarding securities products and services for the full spectrum of retail customers; and
- Access to those securities products and services for the full spectrum of retail customers.

With those tenets in mind, we believe that the Study, and any resulting rulemaking that may be forthcoming as a result of the Study, should focus on the following areas:

- allowing the retail customer and the BD or IA (and as applicable their associated persons) to determine the scope and cost of services to be provided, including services to provide personalized investment advice about securities;
- permitting the types and timing of disclosures provided to retail customers to be based upon, among other things, the securities products and/or services being offered and provided; and providing disclosure to retail customers that is useful - and more specifically concise and targeted information with those retail customers seeking more detailed information being able to access such information via a BD's or IA's Website (or by hard copy if so requested); and
- modernizing and reducing overlapping, duplicative and inconsistent regulation with respect to applicable advertising, recordkeeping and certain other rules.

To these ends, as similarly noted above, we believe that the following principles should guide the SEC's efforts:

- As discussed in more detail below, any new harmonized standard of care must satisfy the Dodd-Frank Act mandate that it apply only to "personalized" investment advice about securities to "retail investors" as those terms are defined.
- Provide clear guidance as to how BDs and IAs, when providing personalized investment advice about securities to retail customers, meet a new standard of care. Specifically, such guidance should be tailored to reflect and preserve the existing and varying business models through which securities products and services are currently provided to retail customers. A one-size-fits-all approach would have the unintended negative consequence of limiting retail customer choice and access to securities products and services, particularly for retail customers with limited assets and those in less populated geographic areas.
- The Dodd-Frank Act provides that offering a limited range of products, including offering only proprietary products, would be disclosed and permissible under any new standard of care. We ask that the SEC, in any rulemaking, be careful not to require or mandate that a BD expand the securities products or services it offers. Conversely, in implementing this requirement, the SEC must also be careful to avoid promulgating rules or guidance that would unnecessarily favor one type of securities product over another or lessen retail customer access to, what some may view as more complicated securities products or, proprietary products when other securities products are available. For

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<sup>3</sup> Such as, for example, as discussed in this letter, a reduction in retail customer access, and choice related, to personalized investment advice about securities.

example, if any promulgated rules lead BDs and IAs to believe that they can gain a competitive advantage through decreasing compliance costs by offering a smaller subset of securities products and services than they otherwise would, it could result in unintended negative consequences of limiting retail customer choice and access to certain securities products and services.

We believe that by satisfying the guiding principles set forth above, any resulting regulations that may follow the Study will enhance the ability of BDs and IAs to: (1) meet the increasing needs of an expanding base of diverse and geographically dispersed retail customers across the broad economic spectrum; and (2) provide enhanced protections to those retail customers.

## **B. Personalized Investment Advice about Securities to Retail Customers.**

It is important that, as noted above, any rulemaking resulting from the Study must satisfy the Dodd-Frank Act mandate that it apply only to “personalized investment advice” about securities that is provided to “retail customers.”

We believe that “personalized investment advice” about securities is investment advice about securities that is provided to a retail customer based on the personal financial information provided by such retail customer, including the retail investor’s financial needs, investment objectives, risk tolerance and financial circumstances.<sup>4</sup> It is, therefore, investment advice about securities that is intended to be specific to the retail customer and is intended to meet his or her specific financial circumstances, objectives and needs as well as the securities products or services which he or she is seeking from the BD or IA.

### **(1) Advice as Distinguished from General Communications**

Any rulemaking in this area should be crafted in a way that avoids the unintended negative consequence of “chilling” contact and interactions between and among BDs, IAs, their respected associated persons and retail customers. There are numerous interactions between such BDs, IAs, their respective associated persons and retail customers that do not constitute personalized investment advice about securities. Accordingly, any rulemaking should make clear that such types of non-personalized investment advice about securities with retail customers will not be deemed “personalized investment advice about securities.” These include, but are not limited to:

- **General Education/ Impersonal Advice.** BDs, IAs and their associated persons provide general education and impersonal advice about securities and investments to retail customers and to broader audiences. Such information may include general concepts such as modern portfolio theory, asset diversification and asset allocation. This education and impersonal advice is not, however, intended to address the financial circumstances and/or needs of any particular individual(s) within the larger group – in fact it is typically delivered absent such specific retail customer information.
- **Account and Retail Customer Relationship Maintenance.** Depending on the business model and the nature of the relationship with the retail customer, as a matter of good business and compliance practices, an associated person of a BD or IA may have

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<sup>4</sup> In this connection, we note that the term “impersonal investment advice is defined under Advisers Act Rule 203A-3(a)(3)(ii) as “investment advisory services provided by means of written or oral statements that do not purport to meet the objectives or needs of specific individuals or accounts.”

- and should be encouraged to have - regular and frequent contact with applicable retail customers that often does not include the provision of personalized investment advice about securities.

- For example, annual or quarterly contact with a retail customer to remind him or her to rebalance assets held in a variable annuity to match allocations set up at the time of contract purchase should not constitute “personalized investment advice about securities” absent, for example, efforts initiated by the associated person to recommend that the retail customer change the allocations percentages to accommodate changes in the retail customer’s individual financial facts and circumstances.
- **Needs Analysis.** Associated persons of BDs and IAs should be able to meet with retail customers as necessary to determine their current, and any new, investment objectives and financial needs without concern that doing so would impose an affirmative duty to render personalized investment advice about securities<sup>5</sup> (on an on-going or of an episodic nature) or that a harmonized standard of care would apply to such interactions, unless the retail customer wishes to seek and the associated person is qualified to provide, and does provide, such investment advice about securities.<sup>6</sup> An associated person should also not be affirmatively obligated to provide personalized investment advice about securities simply because, for example, the associated person has communicated with a retail customer about their respective account(s) or contracts.

## (2) Definition of Retail Customer.

The Dodd-Frank Act defines “retail customer” as a natural person (or the legal representative of such natural person) who receives personalized investment advice from a BD or IA and who uses such advice primarily for personal, family, or household purposes.

Consistent with this definition, we would request that the definition of “retail customer” in any subsequent rulemaking make clear that there is no BD, IA or other obligation or requirement to “look through” defined contribution pension plans to individual participants and their accounts. Such plans are already subject to Department of Labor guidance addressing investor education and regulations governing advice, which impose fiduciary duties consistent with ERISA. The overlaying of a different and potentially conflicting fiduciary duty by the SEC would not serve to protect retail customers and potentially could discourage the formation and continuation of pension plans, as well as the continued provision of beneficial educational services to plan participants. Accordingly, if any harmonized standard of care rules are promulgated, it is important that the SEC specifically establish that any such rules are not intended to confer ERISA or other fiduciary status on a BD, IA or their associated persons.

We have significant concerns with any regulatory actions or rulemaking regarding the provision of personalized investment advice about securities that would serve to extend to others beyond “retail customers.” We suggest that a focus on institutional investors would not serve to provide any

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<sup>5</sup> Please see Section 913(g)(1)(k)(1) of the Dodd-Frank Act.

<sup>6</sup> We recognize that any harmonized standard of care would apply if, and when, personalized investment advice about securities is provided to a retail customer.

meaningful benefit and would simply serve to distract from the larger issue of how best to preserve and/or enhance investor protections for retail customers.

### C. BD and IA Disclosures to Retail Customers.

BDs and IAs, when providing personalized investment advice about securities to retail customers, should be required to make balanced and fair disclosure of material facts relevant to the retail customer's investment decision, including material conflicts of interest. As similarly noted above, disclosure will be more effective, useful and helpful to retail customers, if such retail customers receive concise, plain-English summary disclosures. Such disclosures should also, as also similarly noted above, refer retail customers seeking more detailed disclosure to the BD or IA's Website where they can access such information (or allow them to receive a "hard copy" by request).<sup>7</sup>

This position would appear to be consistent with current statements of the SEC, in particular those made at the time of the recent amendments to the Form ADV Part 2.<sup>8</sup> The SEC stated in the adopting release that it "will continue to consider different approaches to delivering financial information to investors."<sup>9</sup> In this connection we encourage the SEC to take the opportunity to consider approaches that enable BDs and IAs to be able to provide concise and helpful written disclosures to retail customers, by enabling BDs and IAs to reference links to their Websites for certain types of additional, detailed information.

We believe that the following considerations should govern the types of disclosures the BDs and IAs are required to provide retail customers in connection with the provision of personalized investment advice about securities:

- **Simple, Clear and Concise Descriptions.** Retail customers should receive clear disclosure of the range of securities products and services that are offered to them by the BD or IA and their associated persons. Such disclosures should include a narrative description of the types of fees and costs associated with the securities offerings and the manner in which the BD or IA and its associated person are compensated. Disclosure should be written in plain-English, and the SEC and other regulators should work with

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<sup>7</sup> We would urge that consideration of any additional disclosure requirements would include a thorough analysis of the disclosures that retail customers currently receive. For example, when purchasing a deferred variable annuity, a retail (and other) customer must be informed of the general terms of various features of deferred variable annuities, such as surrender period and surrender charges; potential tax penalties; mortality and expense charges; investment advisory fees; potential charges for and features of riders; the insurance and investment components; and market risk. Additionally, such retail (and other) customers must be provided with a product prospectus, which provides a comprehensive and detailed description of the variable annuity. Finally, such retail (and other) customers are provided prospectuses for the mutual funds underlying the product subaccounts in which they invest. Simply piling more disclosure on top of the above-noted disclosure information is more likely to result in "information overload" than an enhanced understanding of the product or transaction by retail customers.

<sup>8</sup> [Amendments to Form ADV](http://www.sec.gov/rules/final/2010/ia-3060.pdf), Investment Advisers Act Release No. IA-3060 (July 28, 2010), available at <http://www.sec.gov/rules/final/2010/ia-3060.pdf>.

<sup>9</sup> *Id.*

the industry and others to identify ways to simplify, and make disclosures more helpful to retail customers.

- **Disclosure of Material Conflicts of Interest.** Perceived or actual conflicts of interest between the BD or IA and their retail customers can arise regardless of the business model. BDs and IAs should take appropriate steps to identify material conflicts and disclose these conflicts to their retail customers.
- **Disclosure of Compensation.** Retail customers should receive a brief narrative description of how an associated person is compensated for the sale of securities products and services so the retail customer can evaluate the personalized investment advice about securities she receives in light of any conflict of interest that may be created and determine the value of securities products and services and related benefits. We believe that retail customers will find most useful concise information regarding how associated persons are compensated, rather than the exact amount of compensation, in order to determine whether compensation incentives may lead to a conflict of interest.

#### D. Business Conduct Rules

As we have noted in detail above and in Appendix A, insurance distribution and sales are already subject to a detailed and rigorous framework with respect to required rules of conduct. These business conduct rules currently govern all aspects of the customer relationship including gathering information about the customer, disclosure, supervision, maintenance of customer account assets, safeguarding confidential customer information, training and supervision of associated persons.

To the extent that the SEC determines that there are gaps with respect to the detailed conduct rules already in place, the SEC should look to specifically address such gaps, as opposed to simply turning, as noted above, to a broad and vague fiduciary standard as some have suggested.

In so doing, it is critical that the SEC craft any conduct rules in a way that does not inadvertently result in a decrease in retail customer choice regarding, and access to, personalized investment advice about securities to retail customers across the broad economic spectrum. Retail customers with seven figures to invest will always be able to find personalized investment advice about securities regardless of the standard of care; a retail customer with under \$100,000 to invest and resides in a less populated rural geographic area may not be able to do so unless the proper balance is struck in any rulemaking.

Accordingly, any conduct rules should be crafted with these principles in mind:

- enable BDs to continue offering their full array of securities products and services to help meet retail customers' financial needs and objectives;
- preserve retail customer access to BDs, IAs and their associated persons and the securities products and securities services they offer;
- preserve various means of structuring securities-related compensation and fees (so that retail customers can pay for services the way such retail customers choose to do so); and

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- avoid providing unintended competitive advantages to any particular business models or securities product and services lineups.

In order to achieve these principles, any new conduct rules should not require BDs, IAs and their associated persons to:

- recommend or otherwise provide investment advice about securities that simply are the “cheapest” or “less expensive” product or service;<sup>10</sup>
- limit securities products or services choices it makes available;
- stop or limit providing personalized investment advice about securities or otherwise providing services to retail customers who have smaller accounts, reside in less populous areas of the country or are not part of the “mass affluent” or “affluent” segment of retail customers; and
- require a BD to expand its available securities product or services universe.

**Implementation Dates.** Further, we would request that in advancing any rulemaking and establishing any compliance dates with respect to such rulemaking, the SEC keep in mind the potential significant implementation issues that would likely be required. We would request that, if any Section 913 related rulemaking follows the Study, the SEC establish compliance dates to provide BDs and IAs with the time they would need to meet such implementation challenges.

#### IV. Conclusion

We greatly appreciate your consideration of and attention to our views. We look forward to meeting with you to discuss the points we raise herein and continuing to participate and contribute to the Study and any potential subsequent rulemaking.

Sincerely,



Carl B. Wilkerson



David M. Leifer

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<sup>10</sup> While we recognize that a particular securities product or services cost and any related expenses are relevant factors for consideration when providing investment advice about securities to retail customers, we strongly believe that providing such investment advice solely in consideration of the lowest costs and any related expenses would often result in retail customer harm and not in fact benefit or provide enhanced investor protections.

Elizabeth M. Murphy, SEC Secretary  
August 30, 2010

CC: Holly Hunter-Ceci, Division of Investment Management  
Emily Russell, Division of Trading and Markets

**APPENDIX “A” Appears on the immediately following pages.**



**Carl B. Wilkerson**  
Vice President & Chief Counsel  
Securities & Litigation

Appendix A to 8.30.10 ACLI  
Submission on SEC Study  
Regarding Obligations of Brokers,  
Dealers, and Investment Advisers

The background materials following  
page 13 have been updated as of  
8.30.10.

December 13, 2007

Dr. Hung  
Project Manager  
RAND Study of Broker-Dealer and Investment Advisory Issues  
By email delivery

Re: Submission of Life Insurance Industry Views on RAND Study

Dear Dr. Hung:

We greatly appreciate the opportunity to share the views of the life insurance industry on the subjects under examination in the RAND Study. ACLI is a national trade association with 373 members that account for 93 percent of the industry's total assets, 91 percent of life insurance premiums, and 95 percent of annuity considerations.

Our members offer and distribute life insurance, annuities and other products through affiliated and independent distributors, including broker-dealers and investment advisers. Many insurance salespersons have attained specialized professional designations, such as the CFP Board's Certified Financial Planner (CFP) designation or the Chartered Financial Consultant (ChFC) designation administered by the American College. The life insurance industry, therefore, is within the scope of the RAND Corporation's examination of broker-dealer and investment adviser functions and regulatory standards.

Life insurers and their salespersons fulfill comprehensive networks of regulation administered by state insurance departments, the Securities and Exchange Commission, and self-regulatory organizations, such as the FINRA. Quite simply, the insurance sales process is one of the most heavily regulated financial services in the marketplace today. Much of our submission and its accompanying attachments outline the products, services and regulation of life insurers and their distributors.

## Objectives of the RAND Study

The scope and purpose of the RAND study provide a critical yardstick to measure whether the project will fulfill its charge objectively and thoroughly. According to the SEC, the core purposes<sup>1</sup> of the RAND Study are to:

- Identify the financial products, accounts, programs and services, including advisory services such as, for example, financial planning and discretionary asset management, provided to individual investors by broker-dealers and investment advisers, and the context in which they are provided;
- Learn how these products, accounts, programs and services are marketed to individual investors;
- Determine the fees and costs paid by individual investors for the products, accounts, programs and services provided;
- Determine how and from what other sources broker-dealers, investment advisers and their associated persons are compensated for the different financial products, accounts, programs and services they offer to individual investors;
- Identify the information provided to individual investors, whether orally, in sales literature, required statements, or in account agreements, regarding the products, accounts, programs and services provided, including the nature of the responsibilities that the broker-dealer or investment adviser owes to the investor and any contractual limitations on those responsibilities;
- Evaluate individual investors' understanding of the marketing and other information provided to them regarding financial products, accounts, programs and services; and
- Evaluate individual investors' expectations regarding the obligations owed to them by the investment professional providing the financial products, accounts, programs and services.

According to the SEC, RAND was hired to elicit views on these core issues from interested parties, including industry groups, regulators, self-regulatory organizations, and investor advocates.<sup>2</sup> The SEC also directed RAND to learn about current industry practices in the marketing, sale and delivery of financial products, accounts, programs and services to individual investors by broker-dealers and investment advisers, including the:

- Marketing and advertising of such products, accounts, programs and services;
- Titles used by investment professionals;
- Communications and disclosures, oral or written, used in connection with the offer of such products, accounts, programs and services;
- Fees and costs of such products, accounts, programs and services; and
- Compensation received by broker-dealers and investment advisers from other sources for the different products, accounts, programs and services they offer to individual investors.

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<sup>1</sup> Exchange Act Rel. No. 34-54077 ( ).

<sup>2</sup> Id.

The SEC visualizes the RAND report as a “first-class empirical study,” that “will collect, categorize, and analyze *empirical* data from a *wide variety* of sources.”<sup>3</sup> Ultimately, the SEC will rely on the RAND Study to devise the most effective legal and regulatory means to govern broker-dealers’ and investment advisers’ services, programs, and products to individual investors.<sup>4</sup>

### **Interests of the Life Insurance Industry**

Life insurers and their agents have a direct and significant role in almost all of the products, services and functions that RAND will examine under the “core purposes” of its study. Life insurers create and market products and services that constructively address consumers’ retirement, estate, tax, and financial planning needs. Over 50% of FINRA’s universe of 675,000 registered representative work for broker-dealers affiliated with life insurance companies. These broker-dealers, however, are quite different from wire-house broker-dealers in structure, operation, products and services.

A principal element of insurance product distribution involves eliciting customer needs and matching them with appropriate insurance and annuity products. Similarly, many life insurance agents provide essential financial planning services in the sale of life and annuity products. Some life insurance agents are also associated with registered investment advisers as a result of their functions and services. These functions may be quite different, however, from what are commonly understood as investment advisory services.

In short, life insurers’ products, functions, services and regulation fit within the scope and purpose of the RAND Study. It is critical, therefore, that the RAND Corporation properly include the unique products, services and regulation within its “first-class empirical study.” Absent inclusion, the RAND Study will be significantly incomplete and will not provide a solid foundation for the SEC to evaluate effective regulation of broker-dealers and investment advisers.

We are greatly concerned that the RAND Study will principally focus on the products, services, functions, and regulations of wire-house broker-dealers and “typical” investment advisers. RAND appropriately met with large trade associations representing these types of firms. RAND’s exposure to products, services, and regulations of life insurers and their distributors, however, appears to be comparatively limited. As soon as the SEC granted RAND the contract to conduct the Study, ACLI volunteered with the SEC staff to meet with RAND and a delegation of representative insurers and distributors. We understood ACLI would be included on the RAND list of industry representatives for interview and dialog.

Late in the RAND Study period, however, we learned that RAND had chosen not to meet with ACLI, although it never communicated its decision. We continue to offer our willingness to actively participate in the RAND analysis notwithstanding reports that the study will be completed by year-end. It is more important to have a balanced, fully inclusive process than it is

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<sup>3</sup> SEC Press Release 2006-162 (Sept. 26, 2006) at <http://www.sec.gov/news/press/2006/2006-162.htm> .

<sup>4</sup> Id.

to meet arbitrary report deadlines with an incomplete understanding of the landscape under study.

We have provided this written submission for review by RAND in its study to outline the important and significant role life insurers and their distributors play in the investment advisory and broker-dealer world, but strongly encourage active supplemental dialog between ACLI, its members and RAND to fully execute the worthwhile purposes of the SEC's award of the RAND contract. In this way, the RAND report will genuinely function as a "first-class empirical study," that "will collect, categorize, and analyze *empirical* data from a *wide variety* of sources."<sup>5</sup> This more complete process will better serve the SEC, investors and financial service institutions as a foundation to evaluate effective regulation of broker-dealers and investment advisers.

### **The Interrelationship of Life Insurers' Products and Regulations**

In order to meet the varied needs of consumers and the demands of a highly competitive marketplace, life insurers offer a wide range of financial products and services. Increasingly, these products and services implicate the federal securities laws, including broker-dealer regulation by the SEC and FINRA under the Securities Exchange Act of 1934 (the 1934 Act) and regulation by the SEC under the Investment Advisers Act of 1940 (the "Advisers Act"). Life insurers must also fulfill a comprehensive set of state insurance laws and regulations in every U.S. jurisdiction.

As a result, life insurers and their affiliates frequently find themselves subject to the overlapping requirements of the 1934 Act, the Advisers Act, and the insurance and securities regulations of the fifty states. The RAND Study will provide a meaningful opportunity to improve investor protection and while enhancing the efficiency and effectiveness of regulatory oversight.

With the decline of defined benefit pensions and the uncertain health of federal safety net programs like Social Security and Medicare, financial services consumers in the United States bear increasing personal responsibility for their own financial well being. Life insurers and their affiliates, like other financial services providers, have responded to consumers' needs with a wide range of products and services. These products and services often include:

- term life insurance
- fixed and variable cash value life insurance
- disability income insurance
- long term care insurance
- many variations of fixed and variable annuity contracts
- investment brokerage services, including: stocks, bonds, mutual funds, ETF's, and 529 savings plans
- investment advisory services, including: financial planning, fee based wrap accounts, and separately managed accounts

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<sup>5</sup> SEC Press Release 2006-162 (Sept. 26, 2006)at <http://www.sec.gov/news/press/2006/2006-162.htm> .

- individual and business retirement planning
- estate planning and trust services
- non-qualified employee benefit consulting
- 401(k) and other qualified plan design, funding and administration

In order to meet the requirements of the federal securities laws, many of these services are delivered through affiliated broker-dealers and investment advisers subject to the federal securities laws. For example, individual variable life insurance contracts and variable annuities are “securities” under the federal securities laws. Accordingly, these contracts are distributed by registered broker-dealers often referred to as “insurance affiliated” or “independent” broker-dealers.

Life insurers have expanded their products and services to meet a wider range of customer needs that also trigger additional regulatory structures, such as FINRA governance over variable product distribution. Historically, FINRA has relied on a “rules based” approach to regulation. FINRA regulations add considerable complexity to life insurers’ enterprise-wide compliance operations that must also fulfill comprehensive regulation by all state insurance departments. Recently, the SEC approved FINRA Rule 2821, a rare single-product suitability rule for the distribution of individual variable annuities. Rule 2821 is significantly more granular and demanding than FINRA Rule 2310 governing all other securities sales. We mention this to simply demonstrate that insurance products and distributors face more layers of consumer-protective regulation than any other product in today’s financial services marketplace. The new, detailed requirements of Rule 2821 are discussed in detail in the appendix.

The Investment Advisers Act also has an increasing impact on insurers and their affiliates. Some insurers have offered investment advisory services for many years and others may not yet offer any today. On an industry-wide basis, however, life insurers and their producers are increasingly present in investment advisory functions and regulations. There are many factors driving this trend. One significant factor is simply the industry’s effort to meet consumers’ increasing need and demand for investment advice. Recent regulatory developments have only hastened that trend.

Until October 1 of this year and in keeping with the recommendations of the Tully Report, insurance affiliated broker-dealers could offer “fee based” or “fee in lieu” investment accounts without registering as Investment Advisers. That is no longer the case. On March 30, 2007, the United States Court of Appeals for the D.C. Circuit issued a ruling vacating SEC Rule 202(a)(11)-1, which had permitted these fee based accounts as an exception to the Advisers Act. The court’s ruling took effect October 1, 2007. Accordingly, insurance affiliated broker-dealers who want to continue offering fee based investment accounts now must do so through advisory – not brokerage – programs.

Although that Rule 202(a)11-1 has now been vacated, its original issuance in April 2005 also stimulated insurance affiliated broker-dealers to offer services under the Advisers Act. For example, the rule clarified that certain services, including discretionary accounts and certain kinds of “wrap” fee programs, did not meet the requirements of the broker-dealer exclusion and therefore needed to be offered by an RIA. The rule also decreed that comprehensive “financial planning” could no longer be considered “solely incidental” to brokerage services. By virtue of this rule, financial planning would have been considered an advisory service regardless of

whether firms charged a separate fee for financial planning advice. Although this rule has been vacated, it did have the effect of bringing more activity by insurers under the umbrella of the Advisers Act.

Through the evolution of insurer's business into broker-dealer and investment adviser areas, insurance agents may wear several distinct, but separate, "hats" in offering these services to the public. For example, a representative may at the same time be an appointed insurance agent (generally of multiple insurance companies), a registered representative of a broker-dealer, an investment adviser representative, and possibly a solicitor who may make referrals to others, such as other investment advisers, banks, or trust companies. Different regulatory schemes apply to the representatives' activities, depending upon the products or services offered. In the case of variable insurance products, multiple regulations apply to the same transaction because these products are considered to be both insurance and securities products. Insurers and their affiliates also face the challenge of meeting demanding new sets of comprehensive laws under Sarbanes-Oxley, Graham-Leach-Bliley and the Bank Secrecy Act for practices that were originally designed to meet the requirements of state insurance regulations.

In other cases, such as financial planning combined with implementation of various product solutions, different regulations might apply to the various aspects of the same customer relationship. For example, a client might have an advisory relationship for purposes of receiving a financial plan that is subject to the Advisers Act. That same client might also elect to purchase an insurance policy or execute securities transactions, which are each subject to differing regulatory requirements. Similarly, a single client might have an advisory account in addition to a brokerage account. While a single representative can be qualified to service both accounts, and might in fact service both accounts, different rules and standards apply to each. Needless to say, the multiple regulatory schemes that apply to the actions of a single representative pose demanding challenges in terms of training and supervising the salespersons.

Insurers provide significant written disclosures at the point of sale to satisfy multiple regulators' requirements and to help customers understand the nature of various products and relationships. These disclosures include many product related materials (insurance sales illustrations, policy contracts, mutual fund prospectuses), marketing materials describing the firm's offerings, documents that provide the terms for a brokerage or advisory relationship (brokerage account agreements, advisory account agreements, Form ADV, investment policy statements), and other required disclosures (privacy policy statements, for example). There also is a considerable amount of post-sale disclosure depending on the nature of products and services provided (in-force insurance ledgers, transaction confirms, period performance reporting for investment accounts, updated privacy statements and ADV brochures, as required in some cases). If it would be helpful to RAND in connection with its Study, we can provide samples of these kinds of documents.

### **The Relationship Between Investment Advice and "Incidental" Activities**

In adopting Rule 202(a)11-1, the SEC commented extensively on the nature and extent of advice that broker-dealers could provide under the "solely incidental" component of the B-D

exclusion. While the SEC received competing comments on the topic, it concluded that “broker-dealers have traditionally provided investment advice that is substantial in amount, variety, and importance to the consumer.” While some financial service observers have challenged the validity of this conclusion, the reality of the marketplace is that broker dealers, including insurance affiliated broker-dealers, do indeed offer valuable guidance and expertise to clients in the context of individual product sales.

Given the importance and individual nature of their own financial needs coupled with the ever-increasing array and complexity of financial services available, individual consumers benefit from analysis and advice about product and service choices. This principle is at the heart of existing broker-dealer regulation, which imposes suitability obligations on firms who make product recommendations to their clients and prospects. These suitability obligations require that firms make an effort to obtain personal and financial information from those customers and that they have “reasonable grounds for believing that the recommendation is suitable for such customer . . . ” FINRA Rule 2310. In recent years, this general suitability standard has been applied to ensure that firms act in the best interest of their customers. Based on good business practices and encouraged by the requirements of the federal securities regulators, insurance affiliated broker-dealers are expected to and do provide meaningful analysis and advice as part and parcel of their sale of products to consumers.<sup>6</sup>

Given the range of insurance products available and the tax benefits that apply to those products, it is worth pointing out that the analysis and advice that accompanies insurance product sales might differ in kind from the incidental advice offered by other broker-dealers. For example, beneficiaries of life insurance proceeds do not pay income tax on the death benefit. Moreover, because life insurance proceeds provide liquidity at an insured’s death, it can be an effective vehicle for funding estate plans. Life insurance also might be used to help fund non-qualified employee benefits for employers of all sizes. Life insurance, long term care insurance, and annuities – which provide a lifetime stream of income – also are likely to play important parts in meeting the retirement needs of the baby boom generations and others to come. Depending on the nature of products and services offered, these products and ancillary services currently might or might not fall under the federal securities laws. As the scope and requirements of those laws are reevaluated, it will be important to consider how any changes

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<sup>6</sup> In another example of rapidly evolving conduct standards, on May 31, 2007, the Certified Financial Planner Board of Standards, Inc. (CFP Board) announced the adoption of updated *Standards of Professional Conduct* that establish ethical standards for CFP professionals. Many life insurance agents hold the CFP designation. CFP professionals found in violation of CFP Board’s ethical standards may be subject to public discipline. In 2005, the CFP Board proposed revisions to its ethical standards in light of the evolving role and functions of investment advisers and financial planners. Among other things, the initiative would clarify the scope of fiduciary duty standards for individuals holding the CFP designation. The revisions also establish and refine a number of threshold definitions involving financial planning. A second set of revisions was circulated in March 2007. ACLI filed letters of comment on the two stages of the proposals, noting the unique role and different functions performed by life agents in the distribution of insurance products. The submission recommended that traditional insurance distribution activities should not be pulled into the CFP standards and fiduciary duty requirements when agents are not engaged in financial planning. ACLI’s recommendations for change were reflected in the final amendments to the CFP Board’s Ethical Code and Standards. The updated Standards will become effective July 1, 2008.

will impact the ability of consumers to access the wide range of products, services, and advice that they need to meet their financial security needs.

### **The Unique Nature of Broker-Dealers Affiliated with Life Insurers**

Broker-dealers affiliated with life insurance companies are significantly different from “wire-house” broker-dealers in their operations, products and services. The securities activities of broker-dealers affiliated with life insurers are a component of a larger insurance business. Many registered representatives operate principally as life insurance and annuity salespersons. Securities sales frequently constitute an incidental amount of business relative to insurance product sales by an office or registered representative.

The range of products offered by these limited purpose broker-dealers is typically constrained and focuses upon the distribution of variable insurance contracts and mutual funds. It may be helpful to consider those securities activities and services *not* offered by most broker-dealers affiliated with life insurers. Typically, these firms do not maintain discretionary accounts permitting registered representatives to purchase and sell securities on behalf of a client without specific approval of each transaction. On an industry-wide basis, these broker-dealers generally do not take custody of client funds, securities or assets. This type of firm does not typically “carry” customer accounts.

Insurance broker-dealers usually require that payment for variable insurance or securities products be made by check payable to the processing office, and not by check payable to the agent/registered representative. Variable contracts and shares in investment companies are issued directly to purchasers and do not constitute bearer instruments. Consequently, the opportunity for misappropriation of these instruments by registered representatives is virtually nonexistent.

Broker-dealers affiliated with life insurers generally do not maintain “open accounts” or facilitate the implementation of stop orders and limit orders, which obviates many potential brokerage problems. These broker-dealers do not generally engage in “principal trades,” so one of the central issues identified in the broker-dealer/investment adviser conflicts discussion does not typically apply to broker-dealers affiliated with life insurers. Similarly, because these broker-dealers do not typically make available cash management accounts or manage free cash balances, many associated operational and logistical difficulties are absent. Broker-dealers affiliated with life insurers do not make markets in securities or underwrite new issues of securities. This obviates common pressures for unsuitable sales practices.

In several instances, the federal securities laws and FINRA regulations provide appropriate regulatory exceptions because these limited purpose broker-dealers are different from full service broker-dealers. For example, SIPC membership is not required (or allowed) because these entities do not make margin loans or take custody of customer assets or securities. Similarly, net capital requirements do not apply since these limited purpose broker-dealers. In the same way, the RAND Study should carefully parse the unique structure, activities, and regulation of these limited purpose broker-dealers from the much broader functions and regulatory issues associated with wire-house broker-dealers.

## Avoidance of One-size-fits-all Analysis

Even though over 50% of FINRA's population of 675,000 registered representatives work for broker-dealers affiliated with life insurers, FINRA regulations and proposals often overlook the unique structure, operation and products of life insurers. A recent example may help illustrate this phenomenon and provide constructive guidance for objective balance in the RAND Study as it will be used to design significant regulatory modifications.

In Notice to Members 07-12, FINRA invited comment on proposed amendments to NASD Rule 3010 (g), which defines the terms "Office of Supervisory Jurisdiction" and "Branch Office" in the NASD supervision rule. The notice explained that FINRA and the New York Stock Exchange (NYSE) "announced a plan to work jointly to harmonize their rulebooks in an effort to eliminate duplicative rules and streamline regulation." The proposed Rule 3010 amendments were the SROs' first endeavor in the harmonization project.

Because the NYSE rules did not contain a definition of OSJ, FINRA proposed to eliminate this definition from NASD Rule 3010. FINRA noted that the amendment would "prevent locations from being classified as branch offices under Rule 3010(g) where the only activity being conducted is principal review and approval of research reports." As part of this endeavor, FINRA had also proposed the creation of several new definitions, including "supervisory branch office," a "limited supervisory branch office," "non-supervisory branch office" and "non-branch office."

The notice indicated that joint NYSE-NASD committees reviewed all the collective NASD and NYSE rules involving sales practices, supervision, financial and operational obligations, registration, qualifications and continuing education requirements to bring the two organizations' rulebooks "into line." The notice explained that the proposal is a "critical step toward ending duplication and reducing regulatory inefficiency." The notice also explains that the NASD and the NYSE announced a plan on November 28, 2006, to consolidate operations into a new organization that will be the single SRO for all broker-dealers. The harmonization project, therefore, will remain a continuing priority for the SROs.

Unfortunately, the initiative failed in several fundamental respects, and presented a worrisome harbinger of merged NYSE-NASD rules. The life insurance industry emphasized that it will be critical for FINRA to conduct the formidable process of rule harmonization in an even-handed, well-executed manner.

Broker-dealers have established compliance procedures, training materials and supervisory responsibilities based on FINRA's definitions of OSJ, and branch office, and non-branch location. While the creation of new definitions of "limited supervisory branch office," and "non-supervisory branch office" may have appeared simply cosmetic in nature, they would have disrupted substantial enterprise-wide compliance procedures, training practices and supervisory responsibilities for broker-dealers affiliated with life insurers. Compliance manuals, office designations and management procedures would have faced substantial change.

Likewise, the elimination of the OSJ definition would have imposed significant transitional and logistical burdens. Transformational systems costs would have been large under the proposal, especially for firms operating out of numerous, small and geographically dispersed locations. One of our members, for example, distributes its products through 9,000 registered

representatives that primarily operate out of one and two person offices. The impact on companies facing these logistics would have been immense. Similarly, the definition of branch office was substantially revised in 2005, transforming to a numerical definitional threshold from a longstanding functional threshold. This revised branch office definition consumed extensive resources in adjustment, supervision, training, compliance procedures, and management. The proposed modifications to the branch office definition so rapidly after its substantial overhaul would have inflicted substantial unnecessary burdens and expenses. The definitional changes would have created an uncharted impact on complying with broker-dealer books and records requirements under the Securities Exchange Act of 1934. None of these issues appeared to have been considered in FINRA's proposed amendment.

The "harmonization" in Rule 3010(g) would have principally benefited 200 wire-house broker-dealers within the total FINRA population of 5,200 broker-dealers. The 5,000 FINRA broker-dealers who are not NYSE members do not face duplicate rule books or disparate SRO rule definitions. Likewise, broker-dealers that are not NYSE members do not typically have locations exclusively limited to supervision and review of research reports. Consequently, the proposed amendment would have principally benefited a select minority of FINRA broker-dealers, and would have imposed collateral burdens on a vast majority of FINRA broker-dealers.

FINRA did not appear to have considered or coordinated the impact of the proposed definitional changes on parallel state securities laws and regulations, which could cause multiple, disparate state and federal categories for broker-dealer offices and locations.

The proposed amendments would have imposed significant operational and compliance costs on broker-dealers. Even worse, the proposal provided no benefit to broker-dealers that are not NYSE members. These factors were properly addressed in the FINRA Notice to Members.

The burdens of the rule were not balanced against its benefits. Notwithstanding FINRA's earnest statements<sup>7</sup> that the interests of *all* broker-dealers would be fairly represented in the merged SRO, the first "critical step" in "ending duplication and reducing regulatory inefficiency" stumbled in favor of a select group to the detriment of a much larger group of broker-dealers.

Fortunately, on June 6, 2007, FINRA withdrew the proposed changes from consideration in response to industry objections. We highlight this incident to demonstrate that surveys of regulations governing broker-dealers and investment advisers need to be inclusive of the wide variety of business models in those fields.

### **Balance and Objectivity in the Use of Interviews and Focus Groups**

In 2004, the SEC released confirmation and point-of-sale disclosure proposals for mutual funds and variable insurance products, supported in part by a consultant's focus group testing. The use of the focus group study and results were fundamentally troubling, especially regarding conclusions about insurance products and distribution. We highlight this development to

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<sup>7</sup> See comments of NASD CEO Mary Shapiro before SEC on a consolidated NYSE and NASD (Nov. 28, 2006) at [http://www.nasd.com/PressRoom/SpeechesTestimony/MaryL.Schapiro/NASDW\\_017978](http://www.nasd.com/PressRoom/SpeechesTestimony/MaryL.Schapiro/NASDW_017978) [Consolidation of the SROs "will mean adopting a uniform set of rules *flexible enough to accommodate the different business models and sizes of firms that exist within the industry*" [emphasis added].

amplify our concern that the RAND Study should be properly objective and thoroughly inclusive of data concerning the structure, operation, products, services and regulation of life insurers and their distributors.

The SEC's 2004 point-of-sale proposal simply indicated that:

[t]he proposed new rules *respond to concerns*<sup>8</sup> that investors in mutual fund shares, UIT interests (including certain insurance company separate accounts that issue variable insurance products) and municipal fund securities used for education savings lack adequate information about certain distribution-related costs, as well as certain distribution arrangements, that create conflicts of interest for brokers, dealers, municipal securities dealers, and their associated persons.<sup>9</sup>

The proposal failed to demonstrate that the regulatory revisions would have resolved the thinly explained regulatory “concerns.” These uncertainties precluded meaningful scrutiny and analysis. The proposal also contained a largely unstated premise that consumers do not read prospectuses. This observation was unsubstantiated in the release.

The initiative's reproposal was quite different from the initial proposal, in purpose and scope. The release stated that:

[m]any investors wanted point of sale disclosure to provide comprehensive information about all the costs of owning covered securities, not just distribution-related costs. They sought comprehensive information about ownership costs, in percentage terms and in dollar terms, to better inform them about the total costs associated with purchasing and owning these securities.<sup>10</sup>

The background and volume of the “many investors” was important to properly and fairly evaluate the initiative. The 2004 release did not specifically identify any commentators or investors making this point, however. Nothing in the release quantified the “many” investors requesting cost disclosure at the point of sale.

In the development of the proposal, the SEC retained consultants to elicit feedback from investors on “comprehensive” cost information in model point-of-sale documents.<sup>11</sup> The direction of the revised proposal relied heavily on the consultant's limited investor interviews. While we respected the SEC's determination to utilize consultants, we questioned the validity of the survey methods used, especially regarding variable contracts.

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<sup>8</sup> Whose concerns? The 2004 release did not quantify or articulate the “concerns” forming the basis for this proposal. Were they the SEC's concerns? Investors? How many? What scope? To what extent did these concerns encompass variable contracts? The answers to these questions were not apparent from the release.

<sup>9</sup> See Investment Company Act Rel. No. 26341 (Feb. 10, 2004) at 3.

<sup>10</sup> See Investment Company Act Rel. No. 26778 (March 4, 2004) at text accompanying footnote 7 (emphasis added).

<sup>11</sup> The release cites the consultant's reports in footnote 12. See Investment Company Act Rel. No. 26778 (March 4, 2004).

The consultants' conclusions were based on individual one-hour interviews with 33 participants.

The report characterizes these surveys as "in-depth" interviews. All participants in the study were required to have purchased a mutual fund within the past two years.<sup>12</sup> The survey screening did not require participants to have experience with variable life insurance or variable annuities. The survey methodology was underwhelming. The report stated that:

*[g]enerally, respondents had little experience with variable annuities. While some had actually invested in them, even they could not clearly describe the features of the product.*

The consultants' report apparently provided a primary foundation for the point-of-sale documents that were expanded to include "comprehensive" cost information. That the proposal was premised on responses from focus group participants without any experience with variable contracts is shocking. The survey appeared unacceptably small to provide "tested" justification for the proposed point-of-sale documents. Moreover, the consultants had not offered survey participants the prospectus Fee Table or Example to address their quest for cost information. We believe the responses would have been far different had participants reviewed this existing cost information.

The participants' background and meager number comprised too small of a sample for reliable research conclusions supporting significant disclosure modifications. While the study reports contained numerous observations, the scope and reliability of the sampling techniques raised significant questions about the validity of the conclusions and the point-of-sale documents they addressed.

We were troubled with a survey using a narrow sample of participants having little experience with variable annuities. The report did not reveal whether the participants understood variable life insurance or had ever purchased a policy. The participants' input on variable contract cost disclosure had limited value, therefore, if any. The sample size for variable contracts was effectively zero because none of the participants had purchased a variable life contract or could clearly describe the features of variable annuities. In our view, the SEC should always base significant new regulatory or disclosure practices on a more substantial and authoritative

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<sup>12</sup> To qualify for the study, each participant: (i) either solely or jointly made investment decisions; (ii) graduated high school, attended some college or graduated college (those with graduate degrees were excluded); (iii) made a mutual fund purchase through a broker in person, over the phone or online in the past (those who had only purchased online were excluded); (iv) made a mutual fund purchase from a financial representative or broker within the past two years; (v) passed an articulateness test. See consultant's survey report at 10 [<http://www.sec.gov/rules/proposed/s70604/rep110404.pdf> and <http://www.sec.gov/rules/proposed/s70604/sup-rep010705.pdf>].

The survey's participant thresholds are so unfocused that they failed to generate meaningful information. Why were participants with graduate degrees excluded? Why weren't the participants grouped or measured on the basis of economic background to better translate the responses? The survey's approach was principally geared to mutual funds and failed to generate a study population germane to variable contracts. The survey's least common denominator approach yielded unreliable information for purposes of significant SEC rulemaking. While the survey report may provide a collection of generalized feedback, it is hardly sufficient to provide the basis for a "comprehensive" revision of disclosure at the point of sale or for a significant transformation of the initial proposal. Good rulemaking demands better methodology.

foundation. The process of using survey and focus group information in the point-of sale initiative provides instructive lessons for the RAND Study.

### **Multiple Moving Parts**

An impressive number of state and federal initiatives are underway that address the supervision, suitability, and disclosure about variable annuities and insurance product distribution. The May 2006 FINRA “annuity roundtable” produced a number of task forces on these matters that will promulgate recommendations. ACLI participated in the FINRA roundtable and has a proactive CEO Task Force on Annuities that developed a comprehensive initiative on streamlined annuity disclosure and meaningful suitability procedures. State regulators are also actively developing initiatives to address similar matters. With so many moving parts, it will be critically important that the RAND Study project managers understand these issues and the unique aspects of life insurers and their distributors under regulatory and disclosure requirements.

### **Appendix Materials**

We have summarily highlighted and referenced the comprehensive regulatory structures faced by life insurers and their distributors in this letter. We have also provided more extensive discussion about the scope, nature, and evolving status of many of these laws and regulations in the attached appendix materials, especially as they affect the life insurance industry.

### **Conclusion**

We greatly appreciate your attention to our views. We remain greatly concerned that the RAND Study will be incomplete regarding the life insurance industry because only a few insurance industry representatives were asked to participate in the process. Life insurers and their distributors fulfill a more comprehensive set of state and federal regulatory structures than any other financial service institution in today’s marketplace. Without a proper understanding and inclusion of these factors, the RAND Study will not fulfill its worthwhile mission. We stand ready to discuss the important role of the life insurance industry in the subjects under study by RAND. Through this process, the RAND report can properly fulfill its core purposes and become a “first-class empirical study,” that “will collect, categorize, and analyze *empirical* data from a *wide variety* of sources.”

Sincerely,

A handwritten signature in cursive script that reads "Carl B. Wilkerson".

Carl B. Wilkerson

**Table of Contents to ACLI Submission on the RAND Study**

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<sup>1</sup> Items VIII and IX did not appear in ACLI's RAND Submission dated December 13, 2007. These outlines were added to this appendix to provide additional content and background for the SEC Study Regarding Obligations of Brokers, Dealers, and Investment Advisers.

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## **NAIC Suitability in Annuity Transactions Model Regulation: A Coordinated Approach to Suitability and Supervision in the Sale of Individual Annuity Contracts**

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### **I. Recent NAIC Modifications Enlarge Suitability and Supervision Responsibilities in NAIC Model Regulation Governing Individual Annuity Sales**

A. The National Association of Insurance Commissioners (NAIC) adopted several evolving sets of revisions to its model regulation governing suitability and supervision in the sale of individual annuity contracts.

1. The NAIC's initial regulation was entitled the Senior Protection in Annuity Transactions Regulation, and governed suitability and supervision in annuity transactions with "senior consumers" age 65 or older.
2. The NAIC's 2006 revision to this regulation applied it to all individual annuity sales. To reflect the broader application of the regulation, it was re-titled the Suitability in Annuity Transactions Model Regulation. This regulation incorporated suitability and supervision practices parallel to those under the federal securities laws and FINRA rules.
3. In 2010, the NAIC added further amendments to the Suitability in Annuity Transactions Model Regulation. Among other things, the 2010 NAIC revisions to the regulation established new restrictions on supervisory delegation to third-party and reliance on producer suitability recommendations, established a new producer training requirement (which must be completed by producers prior to their being able to solicit the sale of annuities), and expanded powers of Commissioners to levy sanctions and penalties.

B. The evolving iterations of the NAIC model regulation can be found at NAIC Model Regulation Service II-275-1 (2010). Over 40 states have implemented the 2006 version of the model regulation. Over time, states will incorporate the 2010 revisions as they update their regulations.

C. **In light of the majority of states currently following the 2006 model, its content and purpose are summarized first below. The 2010 changes to the model are summarized separately below, following the 2006 regulation's summary.**

D. ACLI supports strong suitability standards to ensure annuity sales recommendations are suitable and will promote consumer confidence in making informed annuity purchase decisions.

## II. Approach of the 2006 Revised NAIC Regulation

- A. The regulation establishes standards and procedures governing recommendations in annuity transactions, to ensure “that insurance needs and financial objectives of consumers at the time of the transaction are appropriately addressed.”
- B. The regulation imposes suitability and supervision duties for insurers and insurance producers, including requirements for maintaining written procedures and conducting periodic reviews of records to detect and prevent unsuitable sales practices.

## III. Scope and Governing Framework of the 2006 Revised NAIC Regulation

- A. The regulation applies to any recommendation to purchase or exchange an annuity made to a consumer by an insurance producer, or an insurer where no producer is involved, that results in the purchase or exchange recommended.
  - 1. “Annuity” means a *fixed annuity or variable annuity* that is *individually solicited*, whether the product is classified as an individual or group annuity [Section 5 (A)].
  - 2. “Recommendation” means advice provided by an insurance producer, or an insurer where no producer is involved, to an individual consumer that results in a purchase or exchange of an annuity in accordance with that advice [Section 5(D)].
- B. The regulation does not apply to annuity transactions involving:
  - 1. Direct response solicitations where there is no recommendation based on information collected from the consumer under the regulation;
  - 2. Contracts funding specified retirement plans:
    - a) An employee pension or welfare benefit plan that is covered by the Employee Retirement and Income Security Act (ERISA);
    - b) A plan described by Sections 401(a), 401(k), 403(b), 408(k) or 408(p) of the Internal Revenue Code (IRC), as amended, if established or maintained by an employer;
    - c) A government or church plan defined in Section 414 of the IRC, a government or church welfare benefit plan, or a deferred compensation plan of a state or local government or tax exempt organization under Section 457 of the IRC;
    - d) A nonqualified deferred compensation arrangement established or maintained by an employer or plan sponsor;
  - 3. Settlements of, or assumptions of, liabilities associated with personal injury litigation or any dispute or claim resolution process; or

4. Formal prepaid funeral contracts.

#### IV. Duties Imposed Under the Regulation [Section 6]

**A. Suitability Standard:** In recommending to a consumer the purchase of an annuity or the exchange of an annuity that results in another insurance transaction or series of insurance transactions, the insurance producer, or the insurer where no producer is involved, shall have reasonable grounds for believing that the recommendation is suitable for the consumer on the basis of the facts disclosed by the consumer as to his or her investments and other insurance products and as to his or her financial situation and needs.

1. “Insurer” means a company required to be licensed under the laws of this state to provide insurance products, including annuities.
2. “Insurance producer” means a person required to be licensed under the laws of this state to sell, solicit or negotiate insurance, including annuities.
3. Note: this suitability standard directly parallels the general standard of FINRA Suitability Rule 2310(a), set forth at [http://nasd.complinet.com/nasd/display/display.html?rbid=1189&element\\_id=1159000466](http://nasd.complinet.com/nasd/display/display.html?rbid=1189&element_id=1159000466) .

**B. Suitability Ingredients** [Section 6(A)]: Prior to the execution of a purchase or exchange of an annuity resulting from a recommendation, an insurance producer, or an insurer where no producer is involved, shall make reasonable efforts to obtain information concerning:

1. The consumer’s financial status;
2. The consumer’s tax status;
3. The consumer’s investment objectives; and
4. Such other information used or considered to be reasonable by the insurance producer, or the insurer where no producer is involved, in making recommendations to the consumer.
5. Note: the suitability ingredients above precisely track those in FINRA Suitability Rule 2310(b) set forth at [http://nasd.complinet.com/nasd/display/display.html?rbid=1189&element\\_id=1159000466](http://nasd.complinet.com/nasd/display/display.html?rbid=1189&element_id=1159000466) .
6. An insurer or insurance producer’s recommendation under the suitability standard and ingredients must be reasonable under all the circumstances actually known to the insurer or insurance producer at the time of the recommendation [Section 6(c)(2)].
  - a) Neither an insurance producer, nor an insurer where no producer is involved, has any obligation to a consumer under the

suitability standard [Section 6(a)] related to any recommendation if a consumer:

(1) Refuses to provide relevant information requested by the insurer or insurance producer;

(2) Decides to enter into an insurance transaction that is not based on a recommendation of the insurer or insurance producer; or

(3) Fails to provide complete or accurate information.

(4) Note: these narrow exclusions directly parallel FINRA approaches to suitability in Rule 2310.

### C. Supervision Standard

#### 1. For insurers:

a) An insurer either (i) shall assure that a system to supervise recommendations that is reasonably designed to achieve compliance with the suitability standards in the regulation is established and maintained, or (ii) shall establish and maintain such a system, including, but not limited to:

(1) Maintaining written procedures; and

(2) Conducting periodic reviews of its records that are reasonably designed to assist in detecting and preventing violations of this regulation.

b) To fulfill the supervision standard, an insurer may contract with a third party, including a general agent or independent agency, to establish and maintain a system of supervision as required by Section 6(D)(1) regarding insurance producers under contract with, or employed by, the third party.

(1) To utilize a third party for supervision, an insurer must make reasonable inquiry to assure that the third party is performing the functions required under the regulation, and must take reasonable action under the circumstances to enforce the contractual obligation of the third party to perform the functions.

(2) An insurer may comply with its obligation to make reasonable inquiry by doing all of the following:

(a) Annually *obtain a certification* from a third party senior manager who has responsibility for the delegated functions that the manager has a reasonable basis to represent, and does represent,

that the third party is performing the required functions; and

(b) Based on reasonable selection criteria, periodically select third parties for review to determine whether the third parties are performing the required functions. The insurer must perform those procedures to conduct the review that are reasonable under the circumstances.

c) Insurers that contract with a third party to perform supervision and that comply with the certification and periodic review procedures will fulfill their supervisory responsibilities under the regulation.

d) Note: the supervisory approaches implemented in the regulation parallel those in FINRA Rule 3010(a).

e) No one may provide a certification under the regulations supervisory delegation unless:

(1) The person is a senior manager with responsibility for the delegated functions; and

(2) The person has a reasonable basis for making the certification

2. For insurance producers:

a) A general agent and independent agency either must (i) adopt a system established by an insurer to supervise recommendations of its insurance producers that is reasonably designed to achieve compliance with the regulation, or (ii) establish and maintain such a system, including, but not limited to:

(1) Maintaining written procedures; and

(2) Conducting periodic reviews of records that are reasonably designed to assist in detecting and preventing violations of this regulation.

3. Scope of required system of supervision for insurers and producers:

a) An insurer, general agent or independent agency is not required to review, or provide for review of, all insurance producer solicited transactions; or

b) An insurer, general agent or independent agency is not required to include in its system of supervision an insurance producer's recommendations to consumers of products other than

the annuities offered by the insurer, general agent or independent agency.

c) Note: these clarifications to the scope of the supervisory requirements parallel those applied under FINRA Rule 3010.

4. Deference to FINRA Suitability rule for variable annuity sales:

a) Compliance with FINRA's suitability rule will satisfy the regulation's suitability requirements for variable annuity recommendations.

b) Deference to FINRA suitability standards and practices in variable annuity sales does not, however, limit the insurance commissioner's ability to enforce the regulation.

#### **D. Recordkeeping**

1. Insurers, general agents, independent agencies and insurance producers must maintain or be able to make available to the commissioner records of the information collected from the consumer and other information used in making the recommendations that were the basis for insurance transactions for [a specified number of] years after the insurance transaction is completed by the insurer.

2. An insurer is permitted, but shall not be required, to maintain documentation on behalf of an insurance producer.

3. Records required to be maintained by this regulation may be maintained in paper, photographic, microprocess, magnetic, mechanical or electronic media or by any process that accurately reproduces the actual document.

#### **E. Enforcement Powers and Mitigation Provisions**

1. To implement the regulation, the state insurance commissioner may order:

a) An insurer to take reasonably appropriate corrective action for any consumer harmed by the insurer's, or by its insurance producer's, violation of this regulation;

b) An insurance producer to take reasonably appropriate corrective action for any consumer harmed by the insurance producer's violation of this regulation; and

2. Any applicable penalty under the state code may be reduced or eliminated if corrective action for the consumer was taken promptly after a violation was discovered.

## V. Observations on the NAIC Suitability in Annuity Transactions Model Regulation (2006 Revisions)

A. The NAIC's 2006 modifications to, and substance of, the regulation directly address a number of public concerns about annuity regulation.

1. Applying the regulation to all ages provides coordinated suitability and supervision standards covering all individual annuity sales promotes state regulatory uniformity modeled on FINRA approaches to supervision and suitability.

2. FINRA advocated similar patterns of regulation for fixed and variable annuities under state and federal regulation in a number of public forums, including:

a) The May 5, 2006 Annuity Roundtable which is available by archived webcast at [http://www.nasd.com/RulesRegulation/IssueCenter/VariableAnnuities/NASDW\\_016465](http://www.nasd.com/RulesRegulation/IssueCenter/VariableAnnuities/NASDW_016465).

b) Statements of FINRA representatives:

(1) FINRA believes that "rules governing the marketing and sale of annuity products - regardless of whether the particular annuity is regulated as an insurance product or a security - should be comparable.... In partnership with the Minnesota Department of Commerce, FINRA is working with the Securities and Exchange Commission and state insurance and securities regulators to *bring the rules governing annuity sales, in both the insurance and securities regulatory regimes, into conformity.*" (emphasis added); Maxey, *American Equity CEO: Slower Indexed Sales Won't Hit Net*, Dow Jones Newswires October 13, 2006;

(2) *Mary Shapiro, Former FINRA Chairman & CEO stated:*

(a) "Last, let me bring to your attention our efforts to *harmonize requirements across other financial products that compete with securities.* Variable annuity sales compete with equity-indexed and plain vanilla annuities. Variable annuities are securities, equity-indexed annuities may not be securities, yes the subject of another long and tortuous story, and plain vanilla annuities are not securities. These are *complex products in pricing, operation and structure* that may be purchased for similar purposes but are subject to *disparate levels of regulation and offer dissimilar levels of protection to investors.*" SIA Compliance & Legal Division Annual Conference (March 20, 2006)(emphasis

added). [Available at http://www.nasd.com/PressRoom/SpeechesTestimony/MaryL.Schapiro/NASDW\\_016200](http://www.nasd.com/PressRoom/SpeechesTestimony/MaryL.Schapiro/NASDW_016200) .

(b) Quasi-securities products like equity-indexed annuities also are on our radar screen, and we recently issued a Notice to Members on EIA's to our membership. Despite what you may read in the press, our goal is not to extend our jurisdiction to insurance companies. Rather, we simply believe that our *members need to be aware of the regulatory and supervisory risks that can arise when their registered representatives sell these products*, particularly when they are marketed as securities products and offer substantially greater sales compensation than traditional registered securities. SIA Mutual Fund Reform Conference (September 23, 2005) (emphasis added). [Available at http://www.nasd.com/PressRoom/SpeechesTestimony/MaryL.Schapiro/NASDW\\_015070](http://www.nasd.com/PressRoom/SpeechesTestimony/MaryL.Schapiro/NASDW_015070) .

(c) "The [post-annuity roundtable] working group will consider the issues of disclosure, suitability, supervision and marketing of fixed, variable and equity-indexed annuities. *Regardless of which regulator has jurisdiction over these products, investors deserve as level a playing field as possible.* When product lines blur and regulators' reach is limited, we have an important responsibility to ensure that we work closely together to ensure the highest quality of investor protection." NASAA Annual Conference (September 18, 2006) (emphasis added). Available at [http://www.nasd.com/PressRoom/SpeechesTestimony/MaryL.Schapiro/NASDW\\_017410](http://www.nasd.com/PressRoom/SpeechesTestimony/MaryL.Schapiro/NASDW_017410)

B. The life insurance industry has responded to the public observations and has acted to support and promote enactment of the revised NAIC Suitability in Annuity Transactions Model Regulation.

1. The American Council of Life Insurers (ACLI) endorsed the 2006 removal of the age 65 limitation in the scope of the NAIC Senior Protection in Annuity Transactions Model Regulation, and supports adoption of the NAIC Suitability in Annuity Transactions Model Regulation, and the NAIC Annuity Disclosure Model Regulation.

a) See ACLI Press Release, NAIC Senior Protection in Annuity Transactions Model Should Cover All Consumers, ACLI SAYS ((Jan. 24, 2006) [The decision to support extending standards results from ongoing ACLI efforts to identify areas where the state

laws or regulations governing annuity sales can be enhanced, and reflects a strong desire by U.S. life insurers to enhance Americans' retirement security]; available at <http://www.acli.com/ACLI/Newsroom/News%20Releases/Text%20Releases/NR06-004>

2. ACLI also established a CEO Task Force to develop constructive solutions to promote meaningful disclosure about annuities and suitable sales practices in September 2005 that has coordinated with FINRA and the SEC about a number of responsive industry developments in these areas. A summary about ACLI's disclosure initiatives appears in a separate outline in this appendix.

## **VI. Overview of the Modifications in the 2010 Revised NAIC Suitability in Annuity Transactions Model Regulation**

- A. Insurance producers are required to obtain information about the customer's needs and financial objectives when formulating a recommendation for an annuity purchase and must have reasonable belief that the recommendation is suitable. (NAIC Model Sec. 6(A)&(B)).
- B. Insurers must assure that a system is in place to supervise compliance with the Model, including review of producers' recommendations. (NAIC Model Sec. 6(F)(1)(d)).
- C. An insurer must conduct reviews of its records to assist in detecting and preventing violations of the regulation. (NAIC Model Sec. 6(F)(1)(e)).
- D. )When an insurer contracts with a third party to establish a system of supervision, the insurer must monitor and audit, as appropriate, to assure that the third party is performing the required functions. (NAIC Model Sec. 6(F)(2)(b)(i)).
- E. When an insurer relies on a third party to perform required suitability functions, the third party, when requested by the insurer, must give a certification that it is performing the functions in compliance with the regulation. (NAIC Model Sec. 6(F)(2)(b)(ii)).
- F. Sales of annuities made in compliance with stringent federal securities rules pertaining to suitability and supervision (FINRA Rule 2330) satisfy the requirements under the Model. (NAIC Model Sec. 6(H)).
- G. An insurance producer shall not solicit the sale of an annuity unless the producer has adequate knowledge of the product and shall be in compliance with the insurer's product training standards. (NAIC Model Sec. 7(A)).
- H. Insurance producers who engage in the sale of annuities must complete an annuity training course approved by the appropriate State. (NAIC Model Sec. 7(B)).

I. The Commissioner may order that an insurer or producer take appropriate corrective action for any consumer harmed by the insurer's, or producer's, violation of the regulation. (NAIC Model Sec. 8(A)(1)&(2)).

## **VII. Broad Impact Through IMSA Standards Implementation**

A. On October 19, 2006 the Insurance Marketplace Standards Association ([IMSA](#)) announced its adoption of new suitability standards for annuities and long-term care insurance, which implement the NAIC Suitability in Annuity Transactions Model Regulation. The IMSA standards became effective immediately with a compliance date of January 2, 2008.

**VIII. ACLI Issues Status Chart follows this page, and provides an index and citations to every jurisdiction regarding the NAIC Suitability in Annuity Transactions Model Regulation, together with the NAIC Annuity Disclosure Model Regulation and the NAIC Senior-Specific Certifications Model Regulation.**

## Issue Status Chart: NAIC Annuity Disclosure, Suitability in Annuity Transactions, & Senior-Specific Certifications Model Regulations

(As of **August 16, 2010**)

The chart tracks state adoption of the NAIC Suitability (formerly Senior Protection) in Annuity Transactions Model Regulation, the NAIC Annuity Disclosure Model Regulation, Use of Senior-Specific Certifications and variations of the models. ACLI actively supports state adoption on a uniform basis of the NAIC Suitability in Annuity Transactions Model Regulation, the NAIC Annuity Disclosure Model Regulation, and Use of NAIC Senior-Specific Certifications. Bill text, digest and legislative history are available in ACLI's Legislative Tracker. Also, proposed and adopted regulations are available through ACLI's [Advance Services](#) and the [Market Conduct Compliance Service](#).  
Contacts: [Kelly Ireland](#), 202.624.2387 or [Michael Rowden](#), 202.624.2371.

**OVERVIEW OF STATE ACTIVITY TO DATE:**

19 states have adopted NAIC Senior-Specific Certifications.

Alaska	Iowa	North Carolina	Oregon	Texas	West Virginia
Arkansas	Minnesota	Ohio	Rhode Island	Utah	Wisconsin
Colorado	New Hampshire	Oklahoma	South Carolina	Virginia	Wyoming
Dist. Of Columbia					

38 states have adopted the NAIC Suitability in Annuity Transactions Model (2006 version).

Alabama	Delaware	Iowa	Massachusetts	North Dakota	Texas
Alaska	Georgia	Kansas	Michigan	Ohio	Utah
Arkansas	Hawaii	Kentucky	Montana	Oklahoma	Virginia
Arizona	Idaho	Louisiana	Nevada	Pennsylvania	Washington
Colorado	Illinois	Maine	New Jersey	Rhode Island	West Virginia
Connecticut	Indiana	Maryland	New Hampshire	South Dakota	Wisconsin
			North Carolina	Tennessee	

1 states have proposed the NAIC Suitability in Annuity Transactions Model (2010 version).

West Virginia

2 states have adopted the NAIC Suitability in Annuity Transactions Model (2010 version).

Wisconsin  
Iowa

6 states have adopted the NAIC Senior Protection in Annuity Transactions Model Regulation.

Arizona  
Arkansas  
Delaware  
Florida  
Indiana  
Nebraska

6 states have similar or related suitability standards.

Connecticut  
 Florida  
 Iowa  
 Minnesota  
 Missouri  
 Oregon

22 states have adopted the NAIC Annuity Disclosure Model Regulation.

Alabama  
 Alaska  
 Arizona  
 Arkansas  
 Colorado  
 Hawaii  
 Idaho  
 Iowa  
 Kentucky  
 Maine  
 Montana  
 Nevada  
 New Jersey  
 New Mexico  
 North Carolina  
 Ohio  
 Oklahoma  
 Oregon  
 Rhode Island  
 Utah  
 West Virginia

9 states have adopted variations of an older NAIC Model Regulation.

Florida  
 Georgia  
 Maryland  
 New Hampshire  
 New York  
 Pennsylvania  
 South Carolina  
 Washington  
 Wisconsin

(Updates in **bold**.)

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
<b>ALABAMA</b>					
Admin. Code ch. 482-1-129		X		Adopted 2004.	
Ch. 482-1-129.05		X		Adopted 2006.	Similar to the NAIC Annuity Disclosure Model.
Ch. 482-1-137	X			Adopted 2006.	Similar to the NAIC Suitability Model.
<b>ALASKA</b>					
Overview of recent adopted regulations					The Insurance Division adopted permanent regulations relating to annuity disclosure, suitability, and replacements, as previously posted to the ACLI Web site on July 2. ACLI staff has made separate comparisons between the adopted rules and the NAIC Annuity Contract Disclosure Model Regulation, the NAIC Life Insurance Policy and Annuity Contract Replacements Model Regulation, and the NAIC Suitability in Annuity Contract Transactions Model Regulation for your review and information. Noted deviations between the adopted regulations and the NAIC Models are: Suitability: No corresponding "purpose" section or "mitigation of responsibility" section in the adopted rule; Annuity Disclosure: No corresponding sections relating

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
<a href="#">Adopted Regulation 3 AAC 26.750+</a> <a href="#">Adopted Regulation 3 AAC 26.770+</a>	X	X		Effective July 25, 2008  Effective: July 25, 2008	to "purpose", "penalties", and "severability" in the adopted rules; Replacement: No corresponding sections relating to "purpose", "violations/penalties", and "severability" in the adopted rules. The Alaska Administrative Procedures Act provides that regulations become effective 30 days after filing by the Lieutenant Governor, and the adopted regulations are published quarterly in the Alaska Administrative Register. There may still be unintended drafting errors in these adopted rules that may cause compliance concerns, and ACLI staff urges companies to advise us of any problematic language in the adopted rules that differs from the NAIC Models and that may require clarification from the Division for compliance purposes. Given past experience with Alaska rule adoption, the Division has not deviated from the effective date but has offered clarification with respect to ensuring compliance with the rules.
<a href="#">Bulletin B 09-07</a>	X	X			Director Linda Hall issued Bulletin B 09-07 on August 6 reminding licensees and admitted insurers to comply with the record requirements in relation to regulations on suitability in annuity transactions, life insurance and annuity replacements, and annuity disclosures that became effective July 25, 2008. The bulletin places specific importance on records that must be kept in documenting the analysis and grounds for believing that a recommendation is suitable; documenting the reasonable efforts to obtain the necessary information to make a suitable recommendation; and documenting that the required disclosure have been provided.
<a href="#">Bulletin B 08-04</a>	X				The Bulletin contains an overview of each regulation, stating that the regulations adopt the NAIC Suitability in Annuity Transactions Model Regulation and the NAIC Life Insurance and Annuities Replacement Model Regulation; however, it states that the disclosure regulation adopts, in substance, the NAIC Annuity Disclosure Model Regulation and highlights the differences between the Alaska disclosure document and the NAIC Model.
<a href="#">Notice Of Proposed Changes In The Regulations Of The Division Of Insurance</a>			X		The Insurance Division has published a Notice of proposed new rules relating to the use of senior-specific certifications and professional designations in connection with a solicitation, sale or purchase of, or advice made in connection with a life insurance or annuity contract by an insurance producer.

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
<a href="#">Reg. 3 AAC 26.820±</a>			X	Effective: 6/28/09	Establishes standards and requirements for the use of senior-specific certifications and professional designations in the solicitation, sale, purchase, or advice made in connection with a life insurance or an annuity contract by an insurance producer. The rules substantively follow the NAIC model regulation, except the rules use the term annuity "product" instead of "contract", includes a non-model provision in 3 AAC 26.825(a)(2) adding "oral statements or representation", and omits NAIC Model language, "There is a rebuttable presumption", at the beginning of 3 AAC 26.825(c).
<b>ARKANSAS</b>					
Rule 82	X			Adopted 2004	Applies to consumers over 65. Also see <a href="#">Directive 2-2006</a> .
<a href="#">Rule 82</a>	X			Effective: 7/15/09	The rule, which deviates substantially from the NAIC model regulation, establishes standards for insurers and insurance producers in the sale of annuities, including a required four hours of suitability training for producers.
<a href="#">Bulletin 5-2010</a>	X			Dated: 6/28/10	The Insurance Department issued Bulletin 5-2010 regarding suitability training requirements that were established by Rule 82. Until the rule is revised, the department will not enforce the four hour training requirement.
<a href="#">Rule 96</a>			X	Effective: 7/15/09	Establishes standards and requirements for the use of senior-specific certifications and professional designations by an insurance producer in the sale of life insurance and annuities.
<a href="#">Rule 98</a>		X		Effective: 7/15/09	The new annuity disclosure rule by and large adheres to the NAIC model. It deviates from the model in that it adds a provision to the disclosure document and buyer's guide standards stating that disclosure statements must be signed and dated by the insurance producer and maintained by the producer and issuing company for five years. And, as in the revised version of the rule, the scope now incorporates pre-need policies.
<b>ARIZONA</b>					
Rev. Stat. Ann. §§ 20-1243+	X			Enacted 2006. (HB 2162)	Similar to the NAIC Suitability Model.
Rev. Stat. Ann. §§ 20-1242+		X		Enacted 2003.	

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
Admin. Comp. R20-6-212.01		X		Adopted 2004.	
<b>CALIFORNIA</b>					
Proposed Suitability Regs.	X				Commissioner will not introduce suitability regulation; no pending legislation to adopt the model.
<b>COLORADO</b>					
Reg. 4-1-12		X		Re-proposed Sept. 2006. Adopted December 2006. Effective 1/1/07.	Offers criteria for the disclosure of specified data about annuity contracts to make certain that purchasers comprehend essential aspects of the contracts. Re-proposed to change sections including requiring a free look period of at least 15 days at or prior to the time of application in the absence of a Buyer's Guide and a disclosure document and having the reg. apply to contracts sold on or after 1/1/07, the same day the amended reg. becomes effective.
Reg. 4-1-11	X			Adopted 2004. Revised 2006.	Similar to the NAIC Suitability Model.
<a href="#">Reg. 1-2-18</a>			X	Effective: 6/1/09	Establishes standards and requirements for the use of senior-specific certifications and professional designations in the solicitation, recommendation, sale or acquisition of life insurance and annuity products.
<b>CONNECTICUT</b>					
<a href="#">Prop. Reg. 38a-xxx-1</a>			X	Hearing date: No date given Comments date: 2/26/10	Would establish standards and requirements for the use of senior-specific certifications and professional designations in the sale of insurance, including annuities.
<a href="#">Reg. 38a-432a-1±</a>	X			Effective: 11/10/08	The regulation amends provisions on suitability in annuity transactions to include all consumers by deleting references specific to seniors and the definition of a "senior consumer."
Act 05-57	X*			Enacted 2005. (SB 6622)	*Enabling legislation authorizing the Insurance Commissioner to adopt regulations to establish (1) standards for the sale or exchange of annuities to sr. consumers and (2) procedures for making recommendations to sr. consumers regarding the sale or exchange of an annuity.
Reg. 38a-432a-1 et seq.	X			Adopted 2005.	Similar to the NAIC Senior Protection Model.

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
<b>DELAWARE</b>					
Reg. 1214	X			Adopted 2005.	Similar to the NAIC Senior Protection Model.
<b>DISTRICT OF COLUMBIA</b>					
<a href="#">Rule 5800+</a>			X	<b>Effective: 7/30/10</b>	<b>Substantially similar to NAIC Senior Specific Certifications Model.</b>
<b>FLORIDA</b>					
<a href="#">Rule 69B-162.011</a>	X	X		Effective: November 15, 2009* *Suitability Rule and Forms adopted on October 27th and as published on Florida Administrative Weekly website and FL DFS site stipulates an effective date of November 15. This is a clerical error on the part of Secretary State's office. The statute, which controls, provides an effective date of January 1, 2009 or 60 days following the adoption of the rule, which would be December 25th. The Joint Administrative Procedure Committee has advised FL DFS that the effective date provided in the rule is a "nullity" and should be disregarded. FL DFS is considering a General Bulletin to this effect.	Establishes the duties required of insurers and insurance producers in the sale of annuity contracts to senior consumers, including the purchase, exchange, and replacement of such contracts. Also incorporates by reference an annuity suitability questionnaire and an annuity contracts disclosure form.
<a href="#">S. 2082</a>				Signed by governor on 6/30/08. Effective upon this	

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
Stat. § 626.99				act becoming a law, Department of Financial Services may adopt rules to implement this act. Sec. 9 of this act and such implementing rules shall take effect 60 days after date on which the final rule is adopted or 1/1/09, whichever is later.	
Stat. § 627.4554	X			Enacted 1982 and 1991. Enacted 2004. (SB 2994)	Requires delivery of Annuity Disclosure Model Buyer's Guide. Applies to consumers over 65.
<b>GEORGIA</b>					
<a href="#">S. 95</a>	X			Measure carried over	Failed to pass and died upon adjournment.
Admin. Comp. ch. 120-2-73				Enacted 1996.	Variation of the NAIC Annuity Disclosure Model.
Rule Ch. 120-2-94	X			Adopted 2006.	Similar to the NAIC Suitability Model.
<b>HAWAII</b>					
S. 1008	X			Signed by governor 7/5/07. Effective 1/1/08.	Enacts the NAIC's Suitability in Annuity Transaction Model Regulation. Amends "general agent" to read "managing general agent". Specifies applicability to an insurer, general agent, independent agencies, or a producer in terms of the penalty being reduced or eliminated for corrective action of a violation. Adds "failure to obtain information" as definition of unfair methods of competition and unfair or deceptive acts or practices. Provides that nothing in this Act shall be construed to supersede in any manner any provision of the Uniform Securities Act and nothing shall affect rights and duties that matured, penalties that were incurred, and proceedings that were begun, before the act's effective date.
Stat. § 431:10D-601 et seq.		X		Enacted 2006 (SB 2434)	Similar to the NAIC Annuity Disclosure Model.

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
<b>IDAHO</b>					
<a href="#">S. 132Z</a>	X			Signed by Governor: 4/8/10 Effective: 7/1/10	Adds s. 41-1941 to adopt key provisions of the NAIC model annuity disclosure law and allow the Director to adopt the remainder of the model by rule. The law contains two variations from the model: a 20-day free look provision reflecting current law, and a provision added by the Department of Insurance that requires the producer and company to obtain a signed copy of the disclosure document from the applicant.
<a href="#">H. 411</a>	X			Signed by Governor on 3/19/08. Effective 7/1/08.	
Proposed Regulation text: <a href="#">ID Prop Reg 18.01.09</a> Temporary Rule: <a href="#">ID Ad Reg Temporary 18.01.09</a>	X			Comments by: 8/27/08 Effective: 7/1/08	The proposed amendments to the annuity suitability rule would remove the references to seniors, making it pertinent to all consumers.
Stat. § 41-1940	X			Enacted 2005. (HB 117)	From the NAIC Senior Protection Model, contains Section 6A-C "Duties of Insurers and Insurance Producers." Language deviates from the NAIC model in section addressing exempted contracts. Excludes Sect. 6D, system of supervision, and Sect. 6E, compliance with NASD conduct rules. Applies to consumers over 65.
Rule IDAPA 18.01.09	X			Adopted 2006.	Similar to the NAIC Senior Protection Model Reg.
<b>ILLINOIS</b>					
<a href="#">Rule 130.855</a>			X	Effective: 9/8/09	The amendments to the securities rule add new provisions concerning the treatment by financial advisers of senior certifications and professional designations based on the NASAA Model.
Reg. 3120+	X			Comments by: 4/16/07. Adopted 2007 Effective: 01/01/08	Closely follows the NAIC Model Regulation for Suitability in Annuity Transactions.
<b>INDIANA</b>					
<a href="#">Rule 710 IAC 4-10-2</a>			X	Effective: 6/28/10	The new rule, based on the North American Securities Administrators Association model rule, prohibits the use of senior specific designations or certifications to imply special training or knowledge when advising senior citizens or retirees about investing, purchasing or selling securities.

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
<a href="#">Rule 760 IAC 1-72-1±</a>	X			Effective: 3/27/09	The amended rule, which closely follows the NAIC model regulation, amends provisions on suitability in annuity transactions to include all consumers by deleting references specific to seniors and the definition of a "senior consumer."
IC 27-4-9	X*			Enacted 2005. (SB 634)	*Enabling legislation authorizing the Insurance Commissioner to adopt the Senior Protection Model.
Reg. 760 IAC 1-72	X			Adopted 2006	Similar to the NAIC Senior Protection Model.
S. 171	X*			Signed by the governor 5/3/07. Effective: 01/01/08.	*Enabling legislation for Dept. to promulgate the NAIC Suitability Model.
<b>IOWA</b>					
<a href="#">Rule 191-15.68±</a>	X			Effective: 01/01/11	The rules, which follow the NAIC model regulation, amend suitability requirements in the sale of annuities, including the purchase, exchange, and replacement of annuities and the establishment of procedures to ensure compliance with such requirements. Allows that a penalty for a violation may be reduced or eliminated if corrective action for the consumer is taken promptly after a violation is discovered or if the violation is not part of a pattern or practice.
<a href="#">Bulletin 10-02</a>	X			Dated July 1, 2010	Bulletin provides notice that effective January 1, 2011, Rule 191-15.72 requires all producers selling or soliciting annuity products in Iowa to obtain four continuing education credits by an approved vendor. This one-time requirement is not a condition of license renewal. The Insurance Division's website lists approved courses and vendors.
<a href="#">Bulletin 09-04</a>	X				On March 26, 2009, the Division of Insurance issued Bulletin 09-04 addressing Life Insurance and Annuity Sales Practices, Replacements and Suitability. ACLI has received several questions concerning the reporting requirements. It appears the Division will rely on companies to implement their own monitoring system. Following is guidance we received from the Division.
Admin. Code §191-10.19(522B) & §191-15.8(3)			X	Adopted 2008 Effective: 1/1/09	Producers shall comply with rule 191-10.19(522B) in using senior-specific certifications and professional designations in the sale of life insurance and annuities.
Admin. Code §191-15.8					General suitability standards not based on NAIC Senior Protection Model. Reg. 191-15.68+ [507B] (below) amended § 191-15.8 to

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
I.C.A. § 507B.4B	X*			Enacted 2006. (SB 2364)	remove references to annuities.  Omnibus bill. Enabling legislation for Dept. to promulgate the NAIC Suitability Model. Would prohibit recommending the purchase, sale, or exchange of any life insurance policy or annuity, or any rider, endorsement, or amendment unless the person has reasonable grounds to believe that the recommendation is suitable. Applies to all ages.
Reg. 191-15.68+[507B]	X			Adopted 2006.	Close to the NAIC Suitability Model
Admin. Code §§ 191-15.61 to 191-15.67		X		Adopted 2003.	
<b>KANSAS</b>					
Reg. 40-2-14 a <a href="#">Reg. K.A.R. 81-3-6±</a>	X		X	Adopted 2005. Effective: 5/22/09	Close to the NAIC Suitability Model.  The amendments to the Office of the Securities Commissioner's regulations make it disreputable for a broker-dealer, agent, investment adviser or investment adviser representative to use a professional designation or certification that generates a deceptive inference that the user has specialized instruction in counseling senior citizens. They set out the fraudulent and unprincipled procedures that comprise justification for discipline. The amendments are based on the March 2008 North American Securities Administrators Association Model Rule on the Use of Senior-Specific Certifications and Professional Designation.
<b>KENTUCKY</b>					
Reg. 808 KAR 10:042			X	Effective: 2/6/09	Establishes standards and requirements for use of senior-specific certifications and designations in sale of securities.
Reg. 806 KAR 12:120	X			Adopted 2007 Effective 1/1/08	Similar to the NAIC Suitability Model.
Reg. 806 KAR 12:150		X		Adopted 2007 Effective 1/1/08	This new version was amended to incorporate comments received after hearings were held on June 26 with comments requested by July 6.

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<b>LOUISIANA</b>					
Reg. 89	X			Adopted 2006. Effective 1/1/07.	Similar to the NAIC Suitability Model. ACLI has confirmed with the DOI that the prop/ reg. will be published in final form on 12/20/06 with an effective date of 1/1/07. No changes were made from the original version. Applies to all ages.
<b>MAINE</b>					
Ins. Reg. ch. 915		X		Adopted 2004.	
Rule 917	X			Adopted 2007. Effective 7/1/07.	NAIC Senior Protection Model with deviations regarding age. ACLI submitted comments on 2/3/06. Applied to consumers over 60. Re-proposed with a removal of the age limitations, the deletion of Section 6(C)(1)(c) and a change to a provision concerning compliance with NASD suitability rules for variable annuities, by stating that those rules have to be at least as protective of the consumer's interests as this one. ACLI submitted comments on 11/2/06 regarding 2 deviations from the model. At ACLI's request they modified the regulation to be consistent with changes recently approved by the NAIC.
<b>MARYLAND</b>					
<a href="#">S. 774</a>			X	Signed by Governor: 5/20/10	Sets forth standards to protect consumers from dishonest, deceptive, misleading and fraudulent trade practices in the use of senior-specific certifications and professional designations in the marketing, solicitation, negotiation, sale, and purchase of, and advice given in connection with, life insurance, health insurance and annuities. Prohibits a person from using a senior-specific certification or professional designation in a way that would mislead a purchaser of life insurance, health insurance, or an annuity about specified matters. Requires the insurance commissioner, by regulation or order, to specify what constitutes a misleading use of senior-specific certifications or professional designations.
<a href="#">H. 882</a>			X	Effective: 7/1/2010	
<a href="#">H. 571</a>			X	Signed by Governor: 5/7/09 Effective: 5/7/09	As enacted, prohibits a person from using a senior or retiree credential or designation in a way that is misleading in connection with the offer, sale, or purchase of any security, or in advising another person as to the value, purchase, or sale of any security. Specifies the factors to be considered in determining whether a person is using a senior-specific certification or professional designation. (Same as HB571) [Note: "security" is defined to not include any insurance or endowment policy or annuity contract

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<a href="#">S. 684</a>			X	Signed by Governor: 5/7/09 Effective: 5/7/09	under which an insurance company promises to pay money either in a lump sum, periodically for life, or some other specified period." ]  (Same as H. 571)
Admin. Code §§ 31.15.04.01 to 31.15.04.07				Adopted 1980.	Variation of the NAIC Annuity Disclosure Model.
Reg. 31.09.12.01+	X			Adopted 2007. Effective: 7/1/07.	Similar to the NAIC Suitability Model. ACLI submitted comments on 2/1/07. Sec. 6 of the adopted reg. has been amended slightly (from the proposed reg.) to reflect that compliance with the NASD Conduct Rules satisfies compliance with the regulation.
<b>MASSACHUSETTS</b>					
Opinion Letter					The Division of Insurance published an opinion letter (PDF) August 5, 2009 on the "straight through processing" standards initiative being advocated by ACLI and the Insured Retirement Institute (formerly NAVA) that recognizes the ability to process the sale of annuities electronically in Massachusetts. <a href="#">August 6 State News Weekly</a>
Reg. 211 CMR 96	X			Adopted 2006.	Similar to the NAIC Suitability Model. Also see <a href="#">DOI Bulletin 2006-08</a> .

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<b>MICHIGAN</b>					
<a href="#">H. 6365</a>			X	<b>Introduced: 8/11/10</b>	<b>Would adopt a substantially similar version of the NAIC Senior Specific Certifications Model.</b>
<a href="#">H. 462Z</a>	X	X		Introduced: 3/18/09	Substitute for HB 4627 was approved on June 16, 2010. The ACLI, LIAM and other industry representatives expressed their concern with several provisions of the bill as it did not include key provisions of the NAIC Suitability Model as well as the NAIC Annuity Disclosure Model. The House sponsor, Rep. Constan has indicated his willingness to amend the bill on the House floor to address many of the concerns addressed by the ACLI.
M.C.L.A. 500.4151+	X			Enacted 2006. (SB 880)	Similar to the NAIC Suitability Model.
<a href="#">H. 6523</a>	X	X		Failed to pass.	Would amend the existing suitability statute as it concerns the sale of annuities as well as adds language from the NAIC Disclosure Model Regulation. The amendment to the suitability provision specifically expands information collected related to the consumer's investment objectives and adds a stipulation that a consumer should demonstrate that assets aren't liquidated to purchase an annuity.
<a href="#">H. 5728</a>	X	X		Failed to pass.	Would require employees of financial institutions to report suspected financial exploitation and expand definition of "financial institution" to include insurance companies. As amended in the House, would exclude property-casualty insurers from definition of "financial institution" but still include life insurance companies.
<b>MINNESOTA</b>					
<a href="#">H. 1853</a>			X	Enacted 2009	Adopts the NAIC model on Senior-Specific Certifications and Professional Designations in the Sale of Life Insurance and Annuities (Section 43).
Stat. § 72A.20				Enacted 1995.	Regulation of Trade Practices- Annuity Solicitation Standards.
Stat. § 60k.46				Enacted 2002.	Insurance Producers- Annuity Solicitation Standards.
<b>MISSOURI</b>					
<a href="#">Rule 20 CSR 700-1.146</a>				Effective: 7/30/08	
<a href="#">Rule 20 CSR 700-1.147</a>				Effective: 7/30/08	
<a href="#">Rule 20 CSR 700-1.148</a>				Effective: 12/30/08	

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
Rule 20 CSR 400-5.410		X		Adopted 2007. Effective: 1/30/07	Similar to the NAIC Disclosure Model.
Rule 20 CSR 700- 1.146				Adopted 2006.	Provides grounds for discipline or disqualification of producers. Require producers to have reasonable grounds for believing that the recommendation is suitable and a reasonable effort to obtain certain information.
Rule 20 CSR 700- 1.147				Adopted 2006.	Specifically addresses licensing of insurance producers, who sell variable life and variable annuity products, including written procedures, internal inspections, and review of transactions and correspondence.
<b>MONTANA</b>					
Admin. R. 6.6.801 - 6.6.806		X		Adopted 1998 and 1999.	
S. 535	X	X		Signed by the governor on 5/8/07. Effective 10/1/07.	Similar to the NAIC Disclosure and Suitability Models, however excludes variable annuities products.
<b>NEBRASKA</b>					
Rev. St. § 44-8101 to 44-8107	X			Enacted 2006. (L. 875)	Similar to the NAIC Senior Protection Model.
<a href="#">L. 117</a>	X			Signed by the governor on 5/30/07. Effective 3 calendar months after adjournment (7/17/08).	Extends the provisions of the Senior Protection in Annuity Transactions Act to all annuities and renames the act accordingly.
<b>NEVADA</b>					
Draft Rule			X		The Division of Insurance has rescheduled the rulemaking workshop on its senior designation proposed rules. The workshop is now scheduled for August 9 in Carson City while the public hearing will be held August 19. The proposed rule closely mirrors the NAIC model.
Ch. 688A+	X	X		Adopted 2005. Re-proposed and adopted in 2006.	Variation of the NAIC Annuity Disclosure Model, NAIC Suitability Model, NAIC Life Insurance Disclosure Model and NAIC Life Insurance Illustration Model. Also see <a href="#">Bulletin No. 06-004</a> .

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<b>NEW HAMPSHIRE</b>					
Admin. Code Ins. 301.06(1)					Commissioner Sevigny has published a Bulletin (07-47-AB) that outlines the Department's position on suitability standard to both life insurance and annuities. ACLI has commented to the Commissioner of Insurance on his recent suitability Bulletin 07-047-AB, expressing its deep concerns with the new compliance requirements for insurers set forth in the Bulletin.
<a href="#">Rule 305.01+</a>	X			Effective: 1/30/09	Closely following the NAIC model regulation (an exception is section 305.05(8)(e) on FINRA and requirements for recommendations of variable annuities), the new rule establishes for consumers provisions for advising them about annuity products to make certain that at the time of the transactions their insurance needs and financial goals are adequately met.
<a href="#">Rule 311.01+</a>			X	Effective: 3/1/09	The new rule on using senior specific certifications and professional designations is based on the NAIC model and establishes measures for using the designations in the solicitation, recommendation, sale or acquisition of life insurance and annuity products.
Admin. Code Ins. 306.02 to 306.9				Adopted 1983 and 2001.	Variation of the NAIC Annuity Disclosure Model.
<b>NEW JERSEY</b>					
<a href="#">Proposed Rule 11:2-23.5+</a>	X	X		Comments: 9/4/10	Proposed new rule would establish suitability standards for the sale of annuities and related disclosure requirements, including the Buyer's Guide and the required annuity contract disclosure statement. Would also include requirements for the supervision of those selling annuities.
<a href="#">S. 1745</a>			X	Effective: 7/6/10	Adopts a substantially similar version of the NASAA Model Rule on the Use of Senior-Specific Certifications and Professional Designations and applies its prohibitions to the offer, sale or purchase of a security.
Rev. Stat. § 17B:25-20				Enacted 1981 and 2005.	Limits maturity dates & surrender charges for annuities sold to seniors.
<a href="#">S. 1165</a>	X	X		Effective: 4/1/09	Provides new standards and procedures regarding annuity products solicited directly to consumers, including the prevention of fraudulent and misleading marketing of annuity products by insurers, brokers and agents; the disclosure of information regarding annuity products; and the suitability of annuity products

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
Clarification of S 1165					<p>issued to consumers. The new standards and procedures are now more closely modeled after the NAIC Model Regulations on Suitability in Annuity Transactions and Annuity Disclosure. However, there are two significant differences from the NAIC Models: (1) the disclosure form to be used by an insurer will be designed by the Insurance Commissioner; and (2) oversight of third-party suitability procedures must include periodic reviews of information by the insurer as set forth by the Insurance Commissioner.</p> <p>In response to ACLI questions, the Department of Banking and Insurance (DOBI) has provided ACLI with additional clarification regarding the implementation of S 1165, legislation concerning annuity disclosures. While the DOBI has provided guidance via Bulletin No. 09-06 and 09-12, ACLI had additional questions. Please find a copy of ACLI's questions and the DOBI's response on certain annuity disclosure matters relating to exemptions, the free look period, suitability form, and disclosure form. The DOBI is still working on the rules to implement S 1165. ACLI will update members as new information is received.</p> <p><a href="#">August 10 State News Weekly</a></p>
<a href="#">Bulletin No. 09-12</a>	X			The NJ Dept. of Banking and Insurance (DOBI) issued Bulletin No. 09-12 (PDF) on 4/20/09	<p>Bulletin is regarding individual fixed deferred and immediate annuity form filing and suitability notice requirements. The purpose of the Bulletin is to further clarify Bulletin No. 09-06, which remains in effect. Because Bulletin No. 09-06 remains in effect, the use of the Template for a Fixed Annuity Disclosure—which is based on ACLI's templates for disclosure—will continue to satisfy the fixed annuity disclosure requirements. Per the Bulletin, while the DOBI encourages immediate action to carry out the legislative intent of S1165, until the rules are adopted and the buyer's guides and annuity contract disclosure statements have been approved by the DOBI, it will not be possible for insurers to distribute these documents to consumers. However, the Bulletin further provides that all filings submitted on or after April 1, 2009 must be accompanied by or include a Buyer's Guide and Disclosure Statement that contain the required elements specified in Bulletin No. 09-06. ACLI will be contacting the DOBI to clarify exactly what insurers are required to file as of April 1, 2009.</p>
<a href="#">Bulletin No. 09-06</a>	X				<p>The New Jersey Department of Banking and Insurance issued Bulletin No. 09-06 on March 10, 2009. This Bulletin contains disclosure and suitability form requirements for individual fixed deferred and immediate annuities sold in New Jersey.</p>

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<a href="#">S.1165</a>	X	X		Signed by Gov.: 9/19/08 Effective: 4/1/09	Substitute bill differs significantly from the original S. 1165 in that it DOES NOT contain a private right of action and the new standards and procedures are now more closely modeled after the NAIC Model Regulations on Suitability in Annuity Transactions and Annuity Disclosure. However, there are two significant differences from the NAIC Models: (1) the disclosure form and suitability form to be used by an insurer will be designed by the Insurance Commissioner; and (2) oversight of third-party suitability procedures must include periodic reviews of information by the insurer as set forth by the Insurance Commissioner. Update: The department will be issuing a bulletin (instead of the regulation) regarding the forms before April 1.
<b>NEW MEXICO</b>					
<a href="#">12 N.M. Admin. Code § 11.17.1+</a>			X (NASAA)	Effective: 1/1/10	Establishes standards and requirements for use of senior-specific certifications and designations in sale of securities. (Based on NASAA Model)
13 N.M. Admin. Code §§ 9.12.1 to 9.12.13		X		Adopted 1997 and 2000.	
<b>NEW YORK</b>					
Regulatory action anticipated	X				No legislation anticipated for 2010, but regulatory action is. In the wake of a series of public hearings in 2009 conducted by New York Insurance Department on annuity suitability, Deputy Superintendent Matt Gaul has stated the Department intends to promulgate a draft regulation in early 2010 on suitability for both life insurance and annuity products. It is anticipated that such a draft will mimic the NAIC's "A" Committee's recently adopted amendments to the NAIC Suitability Model Act.
Admin. Code tit. 11 §§ 40.0 to 40.6 (Reg. 139) (1990) §§ 53-1.1 to 53-1.6 (Reg. 74)				Adopted 1990, 1997 and 2003.	Variation of the NAIC Annuity Disclosure Model addressing group annuity contracts and funding agreements.
<b>NORTH CAROLINA</b>					
<a href="#">Rule 11 NCAC 12.0461</a>			X	Effective: 2/1/10	Incorporates by reference the NAIC Model Regulation on the Use of Senior-Specific Certifications and Professional Designations, which establishes standards and requirements for the use of senior-specific certifications and professional designations in the sale of life insurance and annuities.

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
Admin. Code tit. 11 ch. 12 § .0420				Adopted 1976 and 1992.	Requires submission of suitability form.
Gen. Statutes §58-60+		X		Enacted 2005. (HB 655)	Omnibus bill including NAIC Annuity Disclosure model language.
H. 731	X			Signed by the Governor 7/28/07. Effective 1/1/08.	Among other things, enacts the "Suitability in Annuity Transactions Act" and is similar to the NAIC Suitability in Annuity Transactions Model Regulation. Deviations from the NAIC Model include sections relating to a requirement for an application for annuities and surrender fees on death benefits. Amends Article 58 of Chapter 58 of the Statutes relating to the portability of group life insurance. Defines "portability" to mean "the prerogative to continue existing group life insurance coverage, or access alternate group life insurance coverage, that may be provided by a group life insurance policy to an individual insured after the individual's affiliation with the initial group terminates." Provides for the applicability of certificates and prohibitions for portability of group life insurance. Section 7.6, also strikes by reference law that required groups must contain 10 or more lives to qualify for a group life insurance product. The Suitability in Annuity Transactions Act becomes effective January 1, 2008 and applies to violations occurring on or after that date.
<b>NORTH DAKOTA</b>					
S. 2155	X			Signed by the Governor 4/12/07. Effective: 8/1/07.	Similar to the NAIC Suitability Model. There is a deviation in the Mitigation of Responsibility section. It appears to be a drafting error and is expected to be corrected before the hearing.
Admin. Code § 45-02-02-14				Adopted 1984 and 2001.	Passed Senate unanimously with an amendment correcting the deviation in the section mentioned above.  Rules cover recommendations to consumers over 65.
<b>OHIO</b>					
<a href="#">Rule 3901-5-11</a>			X	Effective: 7/1/09	Creates procedures and prerequisites in the application of senior-specific certifications and designations by insurance agents in the counseling, sale, solicitation or negotiation of life or health insurance policies or annuity products.
Reg. 3901-6-14		X		Adopted: 2007. Effective: 3/1/07.	Similar to the NAIC Annuity Disclosure Model.
Reg. 3901-6-13	X			Adopted: 2007.	Similar to the NAIC Suitability Model.

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
<b>OKLAHOMA</b>					
<a href="#">Rule Chapter 25</a>	X			Effective: 7/14/10	Per ACLI's request, Oklahoma has adopted the NAIC annuity training rules (Section 7 of the NAIC Suitability in Annuity Transactions Model Revisions).
<a href="#">Rule 365:25+</a>			X	Effective: 7/14/09	The rule amends provisions on standards for determining if an insurance company is in a hazardous financial condition, requirements for prepaid funeral benefits, conversion from trust to insurance funded contracts, commissioner's authority, and viatical settlement licensing and reporting requirements. Adds a new regulation on the use of senior-specific certifications and professional designations in the sale of life insurance and annuities and new sections on viatical settlement standards for evaluation of reasonable payments for terminally ill insureds, advertising filing requirements, prohibited practices, insurance company practices, and the transition period for existing licenses. Also revokes Subchapter 13 on the regulation of life settlements and adds new appendices for a required brochure and forms for viatical settlements.
Rule 365:25-17	X			Adopted 2006.	Similar to the NAIC Suitability Model.
Rule 365:25-19-1		X		Adopted 2006.	Similar to the NAIC Annuity Disclosure Model.
<b>OREGON</b>					
<a href="#">Rule 836-080-0160</a>			X	Effective: 11/1/09	The proposed new rule would Establishes criteria to safeguard consumers from deceptive and dishonest marketing practices. It provides protection relating to the use of distinctive descriptions and certifications in the solicitation, transaction or acquisition of, or counsel made, concerning an insurance product or in offering advice as to the value of or the suitability of purchasing insurance. The adopted rule goes beyond the NAIC model and applies to all designations, not just those used in the senior market.
OAR 836-080-0090				Adopted 2004.	General suitability standards not based on NAIC Senior Protection Model.
OAR 836-051-0900		X		Hearing: 6/16/08 Comments: 6/24/08 Effective: 8/15/08	The Insurance Division has started a rulemaking process to adopt the Annuity Disclosure Model by rule. A rulemaking advisory committee meeting will be held 5/5.

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<b>PENNSYLVANIA</b>					
<a href="#">H. 2420</a>			X	Introduced: 4/15/10	Follows the NAIC model and includes Section 5(D) from the model, missing in an earlier bill. The penalties provision allows the Commissioner to order restitution. The possibility of using a regulation rather than statute is still preferred, but has yet to be produced by the Insurance Department.
<a href="#">H. 200Z</a>			X	Intro. & sent to House Insurance Cmte. on 9/28/09.	Would provide for the regulation of senior-specific certifications and professional designations in the sale of life insurance and annuities and impose penalties. Based on NAIC Senior Specific Designations Model.
<a href="#">H. 1119</a>	X			Intro & sent to House Insurance Cmte 3/26/09. Passed House on 6/16/09 and sent to Senate Cmte on Banking and Insurance.	Would provide for the suitability of annuity transactions. Would closely represent the NAIC Suitability in Annuity Transactions Model Act.
<a href="#">S. 23Z</a>	X			Signed by the Governor: 3/22/10  Effective: 9/18/10	As enacted, deviates from the NAIC model by the added language in Section 403-B(e) Compliance with other rules, "registered under the Securities Act of 1933 (48 Stat. 74, 15 U.S.C. § 77a et seq.) or rules and regulations adopted under the Securities Act of 1933." This language appears to exclude private placements, which are variable annuities, but not registered with the SEC. ACLI is seeking a fix to amend the language during the next legislative session.
Admin. Code tit. 31 §§ 85.38 to 85.39				Adopted 1978.	Variation of the NAIC Annuity Disclosure Model addressing variable annuity and variable accumulation annuity contracts.
<b>RHODE ISLAND</b>					
Reg. 12	X			Adopted 2006.	Similar to the NAIC Suitability Model.
<a href="#">Reg. 41</a>		X		Effective: 9/30/09	The new regulation stipulates the minimum information that is required to be disclosed and the manner for disclosing it relating to the sale of annuity contracts. It makes certain that consumers comprehend specific essential attributes of annuity contracts and is based on the NAIC model.
<a href="#">Reg. 112</a>			X	Effective: 5/26/09	Based on the NAIC model, the new regulation on senior specifications was adopted to offer continuity with other states. It establishes criteria to protect consumers from deceptive marketing practices concerning the use of senior-specific certifications and professional designations in the purchase, solicitation, sale or advice made in connection with life insurance or annuity products.

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<b>SOUTH CAROLINA</b>					
Ins. Reg. 69-39				Adopted 1986.	Older version of the NAIC Annuity Disclosure Model.
<a href="#">Reg. 69-40.1</a>			X	Effective: 5/28/10	Based on the NAIC model regulation, establishes standards and requirements for the use of senior-specific certifications and designations in the sale of life insurance and annuities.
<b>SOUTH DAKOTA</b>					
S. 37	X			Signed by governor 3/11/08; Effective 7/1/08.	Establishes suitability requirements for annuities. This law is a legislative enactment of the NAIC Model Annuity Suitability Regulation.
<b>TENNESSEE</b>					
<a href="#">Prop. Rule 0780-01-92-.01+</a>			X	Hearing date: 3/17/10 Comments: No date given	Proposed new rule would establish standards and requirements for the use of senior-specific certifications and professional designations in the sale of life insurance and annuity products (NAIC Model)
TN Ad Reg 0780-01-86+	X			Hearing: 3/20/07 Effective: 7/6/08	Similar to the NAIC Suitability Model.
<b>TEXAS</b>					
<a href="#">H. 1294</a>			X	Signed by the governor 6/19/09	As enacted, relates to the use of senior-specific certifications and professional designations in the sale of life insurance and annuities. Follows the NAIC Senior Designations and Professional Certifications Model Regulation. Also includes agent education requirements in the sale of annuity products and applicable only to resident agents. Provides an April 1, 2010 compliance date for the agent continuing education requirements. Effective date is September 1, and applies only to the solicitation of, sale of, or advice made in connection with, a life insurance or annuity product by an insurance agent on or after January 1, 2010.
<a href="#">H. 4492</a>	X			Signed by Gov: 6/19/09 Effective: 9/1/09. Chapter No. 1093	As enacted, amends the suitability law to address annuities registered under the Securities Act of 1933 and update reference from NASD to FINRA.
Draft Rules		X			Department is working on drafting rules to adopt the NAIC Annuity Disclosure Model Regulation. They are also interested in adopting the ACLI annuity disclosure template for companies to use in Texas, which may likely be done through a bulletin after the disclosure rules are adopted. ACLI staff will continue discussions with Department staff to answer any questions they may have and help

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
H. 2761	X			Signed by the governor on 6/15/07. Effective 9/1/07.	ensure that the annuity disclosure rules mirror the agreed upon language found in H. 1293, which was vetoed by Governor Rick Perry after the 2009 legislative session.  Substantively adopts the NAIC Suitability of Annuity Transactions Model Regulation.
<b>UTAH</b>					
<a href="#">R590-252</a>			X	Effective: 2/25/09	The new rule institutes criteria for using senior-specific certifications and professional designations by insurance producers and consultants, broker-dealers and investment advisors in the sale of life insurance, annuities, and accident and health products.
R590-230	X			Adopted 2006.	Similar to the NAIC Suitability Model.
R590-229-1		X		Adopted 2004.	
<b>VERMONT</b>					
<a href="#">H. 222</a>			X*	Signed by Governor 6/1/09. This act shall take effect on July 1, 2009, except that Secs. 1, 2, and 5 of this act shall take effect January 1, 2010.	Creates new law authorizing the Commissioner of Business, Insurance, Securities and Health Care Administration (BISHCA) to extensively regulate life settlements, while specifically prohibiting stranger-originated life insurance (STOLI) transactions. Authorizes BISHCA to adopt rules that would govern credentials, certifications, and designations of those holding themselves out as possessing special levels of expertise regarding senior investments.
<b>VIRGINIA</b>					
<a href="#">Reg 14 VAC 5-43-10+</a>			X	Effective: 5/15/09	The new regulation, which closely follows the NAIC model regulation, establishes standards and requirements for the use of senior-specific certifications and designations by insurance agents in the marketing, sale, or purchase of a life or accident and health insurance policy, or annuity products. Applicability includes the marketing, sale, or purchase of disability income insurance policies, long-term care insurance policies, long-term care partnership policies, and fixed and variable annuities.
14 VAC 5-30-10+				Adopted: 2006. Effective: 4/1/07	Life Insurance and Annuity Replacements
Rule Ch. 45	X			Adopted: 2006. Effective: 4/1/07.	Closely follows the NAIC Suitability Model with the exception of the Mitigation of Responsibility section.

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
<b>WASHINGTON</b>					
Admin. Code R. §§ 284-23-300 to 284-23-380				Adopted 1980.	Older version of the NAIC Annuity Disclosure Model.
<a href="#">H. 1563</a>	X			Introduce and sent to House Cmte on Financial Institutions and Insurance on 1/23. Sent to House Cmte on Financial Institutions, Housing and Insurance 1/28. Do Pass as substituted on 2/17. Measure carried over.	Would require that annuities sold in the state be appropriate for the age and financial situation of the owner. Would set forth various requirements for insurers and producers concerning the sale of annuities. Would require the insurance commissioner to adopt by rule, annuity suitability standards, upon reviewing standards previously established by the NAIC and other states.
<a href="#">S. 5671</a>	X			Signed by governor 3/30/09. Chapter 18. Effective 7/26/09	(Same as H. 1563) Requires that annuities sold in the state be appropriate for the age and financial situation of the owner. Sets forth various requirements for insurers and producers concerning the sale of annuities. Requires the Commissioner to adopt by rule, annuity suitability standards, upon reviewing standards previously established by the NAIC and other states. Includes the Mitigation of Responsibility section of the NAIC model and updates the FINRA safe harbor language to refer to "registered" annuities. Requires the Commissioner to notify the Legislature if a change is made in the types of annuities subject to registration under the Securities Act of 1933.
<b>WEST VIRGINIA</b>					
<a href="#">Prop. Rule 114-11B</a>	X			Comments: 7/15/10	Proposed changes to current Suitability in Annuity Transactions Rule so that the Rule tracks the recently adopted amendments to the NAIC Model (April, 2010). The proposed changes generally track the NAIC Model.
<a href="#">Rule 114-89</a>			X	Effective: 7/1/10	Establishes standards and requirements for the use of senior-specific certifications and professional designations in the sale of life insurance and annuities. (NAIC Senior Designations Model)
<a href="#">Rule 114-11E</a>		X		Effective: 7/16/10	Establishes requirements for the disclosure of information in relation to the sale of annuity contracts. Includes requirements for the content of the disclosure document and the Buyer's Guide. (NAIC Annuity Disclosure Model)

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
<a href="#">S.40Z</a>		X	X	Signed by Governor: 4/2/10 Effective: 3/13/10	This bill adopts various regulations, including Annuity Disclosure (Prop. Rule 114-11E) and Use of Senior Designation (Prop. Rule 114-89). While the legislation itself is effective, ACLI is working with the Insurance Department on effective dates for the Rules.
Code of State Rules § 114-11-6(g)				Adopted 1974.	General suitability standard not based on the NAIC Suitability Model.
<a href="#">Rule 114-11B-1+</a>	X			Comments date: 7/2/07 Adopted: 2008 Effective: 8/1/08	Regulation adopted by WV S. 417 on 3/16/08. This new rule, based on the NAIC model, establishes requirements for insurers and insurance producers in determining the financial suitability of annuity products prior to recommending a product to consumers. Includes record retention requirements.
<b>WISCONSIN</b>					
<a href="#">S. 57Z</a>	X			Signed by Governor: 5/13/10 Effective: 5/1/11 Producers who sell annuities have to complete the training by November 1, 2011. New producers on or after May 1, 2011 have to complete the training before selling annuities.	Adopts a substantially similar version of the revised NAIC Model Law on Annuity Suitability with a few deviations that provide for greater rule-making authority by the Commissioner; provide penalties; and allow the Commissioner to review and take action against any violations.
<a href="#">Rule Ins. 6.90</a>			X	Effective: 1/1/10	The new rule creates criteria to shield consumers from deceitful practices with respect to the use of senior-specific certifications and professional designations in the advertising, solicitation, sale or purchase of life insurance, annuity products or health insurance. It follows closely the NAIC model with two discrepancies. The new rule adds advertising to the list of practices and conduct, and health insurance to the list of products to which the rule applies.
<a href="#">S. 294</a>	X			Signed by governor 3/26/08. Effective 3/28/08 except for following sections: Insurance Form Filing is effective 7/1/08 and Suitability of Annuities is effective 10/1/08.	Enacts the NAIC Interstate Insurance Product Regulation Compact with slight deviations. Amends the suitability of annuity sales statutes to make them apply to consumers of all ages, not just to a person 65 or older. This makes the statute consistent with the NAIC Suitability in Annuity Transactions Model Regulation. Provides that, with a number of specified exceptions, a form first used on or after the effective date of the provision that has not already been filed by

Legislative or Regulatory Citation	Suitability Model	Annuity Disclosure Model	Senior Designation	Status	Comments
Stat. § 628.347	X			Enacted 2004.	that date may be used without approval by the commissioner. The specified exceptions, which must still be filed and approved before use, include, among others, forms for long-term care insurance. The Committee met on 4/22 and heard presentations from Jim Mumford of the Iowa Department, IMSA, and FINRA regarding their activities on suitability. The Committee has recently been given the task of developing baseline supervision standards for the NAIC Suitability of Annuity Sales Working Group.
Admin. Code § INS. 2.15				Adopted 1982 & 1989.	Applies to consumers over 65. (SB 320) Variation of NAIC Annuity Disclosure Model.
<b>WYOMING</b>					
<a href="#">Rule 62</a>			X	Effective: 4/23/10	The new rule, which deviates from the NAIC model regulation, establishes standards and requirements for the use of senior-specific certifications and designations in the sale of annuities, accident and health insurance, and life insurance. Specifies prohibited uses of such certifications and designations.
Ins. Reg. Ch. 27 § 11				Adopted 1968 & 1997.	Variable contract regulation on suitability of sales.

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## FINRA Rule 2330: Suitability and Supervision in the Sale of Variable Annuity Contracts

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### I. Overview and Scope

A. FINRA [Rule 2330](#) [Formerly NASD Rule 2821], which governs suitability and supervision in the sale of variable annuity contracts, was approved by the SEC in 2008, and was under development since 2004. The rule evolved through six different stages, five at the SEC, and one at FINRA.

B. This outline will summarize the elements of Rule 2330, and discuss its administrative history to illuminate FINRA's purpose and intent.

### II. Substantive Overview: Rule 2330 has four primary provisions

A. Requirements governing recommendations, including a suitability obligation, specifically tailored to deferred variable annuity transactions;

B. Principal review and approval obligations;

C. A specific requirement for broker-dealers to establish and maintain written supervisory procedures reasonably designed to achieve compliance with the rule's standards; and,

D. A targeted training requirement for broker-dealers' associated persons, including registered principals.

### III. The Rule's Requirements in Greater Detail

A. Revised Rule 2330 established the following specific requirements:

1. *Recommendation Requirements.* When recommending a deferred variable annuity transaction, Rule 2330 requires broker-dealers and salespersons to have a reasonable basis to believe that the: customer *has been informed of, in a general fashion,* the various features of the deferred variable annuity,

- a) customer *would benefit from* certain features of a deferred variable annuity (e.g., tax-deferred growth, annuitization or a death benefit); and
- b) the deferred variable annuity *as a whole* and the underlying sub-accounts or riders are suitable for the particular customer.
- c) the particular deferred variable annuity that the registered representative is recommending, the underlying subaccounts to which funds are allocated at the time of the purchase or exchange of the deferred variable annuity, and the riders and similar product enhancements are suitable (and in the case of an exchange, the transaction as a whole also is suitable) for the customer based on the information the registered representative is required to make a reasonable effort to obtain.

2. Revised Rule 2330 requires these determinations to be *documented and signed* by the salesperson recommending the transaction.

- a) Rule 2330 would also require salespersons to make *reasonable efforts* to obtain information concerning customers' age, annual income, financial situation and needs, investment experience, investment objectives, intended use of the variable annuity, investment time horizon, existing investment and insurance holdings, liquidity needs, liquid net worth, risk tolerance, tax status and other information used by the salesperson in making recommendations.

3. *Supervisory Review.* Rule 2330(c) requires that a principal review each variable annuity purchase or exchange within seven business days after the signed application arrives at the broker-dealer's office of supervisory jurisdiction in good order. A registered principal shall review and determine whether he or she approves of the purchase or exchange of the deferred variable annuity.

- a) In reviewing the transaction, the registered principal would need to take into account the extent to which:
  - the customer would benefit from certain features of a deferred variable annuity;
  - the customer's age or liquidity needs make the investment inappropriate; and,
  - the customer involved an exchange of a deferred variable annuity: will incur surrender charges, face a new surrender period, lose death or existing benefits,
  - have increased mortality and expense fees, appears to have a need for any potential product enhancements and

improvements, or had another deferred variable annuity exchange within the preceding 36 months.

- Under Rule 2330, the supervisory review standards must be signed and documented by the registered principal that reviewed and approved the transaction.

4. *Supervisory Procedures.* Rule 2330 requires broker-dealers to establish and maintain specific written supervisory procedures reasonably designed to achieve and evidence compliance with the standards in Rule 2330. The broker-dealer must have procedures to screen and have principal review of the recommendations requirements in Rule 2330, and determine whether the salesperson has a particularly high rate of effecting deferred variable annuity exchanges.

5. *Training.* Under the proposal, broker-dealers would need to develop and document specific training policies or programs designed to ensure that salespersons recommending transactions, and registered principals who review transactions, in deferred variable annuities comply with the requirements of Rule 2330 and that they understand the material features of deferred variable annuities, including liquidity issues, sales charges, fees, tax treatment, and market risks.

6. *Automated Supervisory Review.* FINRA's submission on the rule indicated that the rule would not preclude firms from using automated supervisory systems, or a mix of automated and manual supervisory systems, to facilitate compliance with the rule.

a) In addition, FINRA delineated what, at a minimum, a principal would need to do if his or her firm intends to rely on automated supervisory systems to comply with the proposed rule.

b) Specifically, a principal would need to (1) approve the criteria that the automated supervisory system uses, (2) audit and update the system as necessary to ensure compliance with the proposed rule, (3) review exception reports that the system creates, and (4) remain responsible for each transaction's compliance with the proposed rule.

c) Finally, FINRA noted that a principal would be responsible for any deficiency in the system's criteria that would result in the system not being reasonably designed to comply with the rule.

7. *Tax Qualified Plans.* Rule 2330 does not apply to variable annuity transactions made in connection with tax-qualified, employer-sponsored retirement or benefit plans that either are defined as a "qualified plan" under Section 3(a)(12)(C) of the Exchange Act or meet the requirements of Internal Revenue Code Sections 403(b) or 457(b), unless, in the case of any plan, the broker-dealer makes recommendations to individual plan participants regarding the variable annuity.

#### IV. Review and Explanation of (Revised) Rule 2330

##### A. Supervisory review standards changed

1. FINRA enlarged the time period for supervisory review to seven days after the signed application arrives at the broker-dealer's OSJ in good order.

a) Compare to *prior* draft: "Prior to transmitting a customer's application for a deferred variable annuity to the issuing insurance company for processing, but *no later than seven business days after the customer signs the application*, a registered principal shall review and determine whether he or she approves of the purchase or exchange of the deferred variable annuity."

b) Compare to earlier draft: the third amendment required the principal must review and approve the transaction "[n]o later than *two business days following* the date when a member or person associated with a member *transmits a customer's application* for a deferred variable annuity to the issuing insurance company for processing or *five business days from the transmittal date* if additional contact with the customer or person associated with the member is necessary in the course of the review."

2. FINRA rationale: ensuring that all broker-dealers have adequate time to perform a thorough principal review of these transactions.

a) In view of the variety of features and provisions in connection with the issuance of deferred variable annuity contracts, FINRA became persuaded that principal review of variable annuity sales requires greater time than reviews of many other securities transactions.

b) The provision of a reasonable amount of time for pre-transmittal review, however, posed potential problems related to other rules concerning the prompt handling of customer funds.

(1) For instance, FINRA Rule 2330 states generally that member firms shall not make improper use of customer funds, and FINRA Rule 2820 specifically requires member firms to "transmit promptly" the application and the purchase payment for a variable contract to the issuing insurance company.

(2) Similarly, Rules 15c3-1 and 15c3-3 under the 1934 Act require certain member firms to promptly transmit and forward funds.

(3) Rules 15c3-1(c)(9) and (10) under the 1934 Act define the terms "promptly transmit and deliver" and "promptly

forward” funds as meaning “no later than noon of the next business day after receipt of such funds.”

3. FINRA solution to regulatory conflicts with prompt pricing standards:
  - a) FINRA asked for, and obtained from the SEC, regulatory relief regarding Rules 15c3-1 and 15c3-3 when the same circumstances exist. As a companion to the rule approval, the SEC provided an exemptive order from the prompt pricing provisions.
  - b) FINRA made clear that a broker-dealer that is holding an application for a deferred variable annuity and a non-negotiated check from a customer written to an insurance company for a period of seven business days or less would not be in violation of FINRA Rules 2330 if the reason that the application and check are being held is to allow a principal to complete his or her review of the transaction pursuant to proposed Rule 2330.

#### B. Recommendation requirements revised

1. FINRA revised proposed Rule 2821 to state that “[n]o member or person associated with a member shall recommend to any customer the purchase or exchange of a deferred variable annuity unless such member or person associated with a member *has a reasonable basis to believe* that the transaction is suitable in accordance with Rule 2310.”
2. FINRA is substituting the phrase “has a reasonable basis to believe” for “has determined,” which appeared in the prior draft of the rule.
3. FINRA rationale: FINRA softened the review requirement in response to comments that the reasonable basis standard was more strict than with other similar financial products.

C. Non-recommended transactions conditionally excluded. FINRA revised the rule conditionally so that it does not apply to non-recommended transactions, such as situations where the member is acting solely as an order taker. FINRA believed Rule 2821 should not prevent a fully informed customer from making his or her own investment decision.

1. Conditional exclusion from rule, however.
  - a) A registered principal “may authorize the processing of the transaction if the registered principal determines that the transaction was not recommended and that the customer, after being informed of the reason why the registered principal has not approved the transaction, affirms that he or she wants to proceed with the purchase or exchange of the deferred variable annuity.”
2. FINRA rationale:
  - a) Change allows a customer to decide to continue with the non-

- b) recommended purchase or exchange of a deferred variable annuity notwithstanding the broker-dealer's belief that the transaction would be viewed as unsuitable if it had been recommended.
- c) The new requirement that the principal independently determine that the transaction was not recommended adds another layer of protection. Requirement "should discourage salespersons from attempting to bypass compliance requirements for recommended sales by simply checking the 'not recommended' box on a form."
- d) Customers must indicate an explicit intent to continue with the non-recommended transaction notwithstanding the unsuitability determination, which will help ensure that the customer's decision is an informed one.

D. "*Undue concentration*" standard eliminated. FINRA eliminated prior requirements that registered principals consider "the extent to which the amount of money invested would result in an undue concentration in a deferred variable annuity."

E. The annuity or deferred variable annuities should be evaluated in "the context of the customer's overall investment portfolio."

1. FINRA Rationale:

- a) Requirement was unclear and could cause confusion. Because other provisions in Rule 2330 already capture the important aspects of this "undue concentration" determination, FINRA has eliminated it as superfluous.

F. Generic disclosure allowed

- 1. Under recommendation requirements, FINRA clarified that required disclosure may be generic and not specific to the product. Clarification now requires that "the customer has been informed, *in general terms*, of various features of deferred variable annuities. . . ."

2. FINRA rationale:

- a) Simply a clearer statement of original rule's intent.

G. "Unique features" requirement relaxed and expanded

- 1. Provision now states that salesperson must have "a reasonable basis to believe that . . . the customer would benefit from certain features of deferred variable annuities, such as tax-deferred growth, annuitization, or a death or living benefit."

2. FINRA Rationale:

a) FINRA accepted commenters' position that there are other financial products that have features similar to those of a deferred variable annuity, so a requirement that the customer would benefit from the *unique* features was relaxed to benefiting from *certain* features.

b) Living benefits added to the list of certain features that may be beneficial for customer in addition to death benefit.

#### H. Required surveillance practices for replacement activities clarified

1. FINRA indicated that principal need not examine every transaction when salesperson has a potentially higher rate of replacement sales. FINRA emphasized instead review on a periodic basis via exception reporting rather than as part of the principal review of each exchange transaction

2. FINRA revised the supervisory procedures guarding against inappropriate replacement practices so that, "the member also must (1) implement surveillance procedures to determine if the member's associated persons have rates of effecting deferred variable annuity exchanges that raise for review whether such rates of exchanges evidence conduct inconsistent with the applicable provisions of this Rule, other applicable FINRA rules, or the federal securities laws ("inappropriate exchanges") and (2) have policies and procedures reasonably designed to implement corrective measures to address inappropriate exchanges and the conduct of associated persons who engage in inappropriate exchanges."

### V. ACLI Views on Rule 2330: Guideposts to Administrative History

#### A. Principal Review Provisions

1. ACLI recommend adding a further refinement allowing additional time, with customer consent, for processing to resolve incomplete portions of the application. ACLI's submission can be found at <http://sec.gov/comments/sr-finra-2008-019/finra2008019-14.pdf>

2. This suggestion follows the policy embodied in Rule 22c-1 under the Investment Company Act of 1940 allowing pricing of customer orders to extend beyond this rule's 5 day time period, with customer consent, to resolve deficiencies in the application.

a) The added time period for clarification of application deficiencies could be modeled after provisions in Rule 22c-1.

b) The recommended refinement would fulfill customer objectives and price the contract more promptly than if the application were suspended, returned and refilled.

c) By mandating advance consent and explanation before any delays to complete the application, customers will be protected and in control.

#### B. Non-recommended Transactions.

1. ACLI supported the application of the amended rule to recommended transactions only.
2. ACLI commended FINRA's flexibility and its willingness to carefully reconsider this issue. This revision will promote consistent, enterprise-wide uniformity in compliance practices.

#### C. Suspense Account Issues

1. ACLI noted that some life insurers believe the amended rule's treatment of suspense account issues may be feasible under their operation and structure, if certain aspects of the standards are changed.
2. ACLI noted that other companies, however, found that the revised rule would present significant problems for the movement of money after receipt from the customer.
3. ACLI suggested an alternative that would allow immediate transmittal to the insurance company suspense account without conditions, and would facilitate broker-dealer communication with life insurers once the principal's suitability review has been approved or rejected.
  - a) Customer funds could not be transferred from suspense accounts at the insurance company without completion of registered principal approval.
  - b) Such an amendment to the Rule will have the positive effect of promoting communication between the broker-dealer and the insurance company regarding the suitability of the recommendation, a positive step in ensuring the suitability of variable annuity sales.

#### D. Process Issues

1. The FINRA amendments introduce "supplementary material" for the first time in Rule 2821. ACLI noted that the legal status of these appendages is imprecise and unclear.
  - a) The latest proposal does not explain the purpose or intent of the rule's supplementary material. It is far preferable for administrative rulemaking to have all applicable provisions appear in the text of the rule rather than in "supplementary material."
  - b) ACLI observed that during the four year evolution and amendment of Rule 2821 [now renumbered as Rule 2330], FINRA

has not provided any analysis of the proposal's economic and competitive impact. ACLI recommended that these economic reviews be developed and specifically reviewed by the SEC.

## VI. Other Industry Comments: Guideposts to Administrative History

### A. Principal review timetable

1. One Commentator supported the proposal to start the seven day principal approval period when a broker-dealer receives a "correct and complete" application at an office of supervisory jurisdiction ("OSJ") of the firm, and believed the standard is workable and should generally provide sufficient time for principal review. See comment filed by the Committee of Annuity Insurers, <http://www.sec.gov/comments/sr-finra-2008-019/finra2008019-10.pdf>

a) The Commentator, however, sought clarification that the trigger date does not begin when an application is received at any OSJ of the firm. Id. According to the commentator,, in order to be "correct and complete" the application must be received at the particular OSJ designated by the firm for processing such applications.

b) The Commentator also suggested that suggests that the Rule be revised to address infrequent situations when seven business days will not be a sufficient amount of time for the registered principal to conduct the required review. Id.

(1) For example, it was anticipated that there will be situations where a "complete and correct" application is received but a registered principal conducting a review needs further information or documentation from the selling representative or the customer.

(2) In order to address such situations, the Commentator believed that the Rule should permit a broker-dealer to obtain the consent of the customer to delay the seven day period. The letter noted that this exception could be patterned upon the provisions of Rule 22c-1 under the Investment Company Act of 1940. Id.

(a) The provisions of Rule 22c-1 relating to the two day/ five day procedure and the possibility of the customer consenting to a delay were adopted by the SEC in 1985, and have worked well for both customers and the industry for over twenty years.

(b) Rule 22c-1 provides that, in complying with the "two day/five day" time period to price the payments under a variable annuity contract, the insurance company may, if the application for the variable

annuity is incomplete, refrain from returning the initial purchase payment when the two day/five day period expires if “the prospective purchaser specifically consents to the insurer retaining the purchase payment until the application is made complete.”

(c) Under Rule 22c-1, the prospective purchaser must be informed of the reasons for the delay in pricing the contract.

## **VII. Administrative History of Rule 2821 [now renumbered as Rule 2330]**

A. *Round Six.* On April 17, 2008, FINRA filed an amendment with the SEC requesting delayed implementation on provisions of Rule 2821.

1. On May 5, 2008, Rule 2821 [now renumbered as Rule 2330] became effective, except for paragraphs (c) and (d), which involve principal review, non-recommended transactions, and handling of customer funds pending supervisory approval.
2. The FINRA amendment requests an order from the SEC revising the implementation timetables for Rule 2821 (c) and (d) until 180 days after the SEC approves further supplemental changes to the rule. The rule’s effectiveness, therefore, will have two stages, with one date certain and another yet to be determined.
3. FINRA’s fifth amendment can be found at <http://sec.gov/rules/sro/finra/2008/34-57920.pdf>

B. *Round Five.* On March 5, 2007, FINRA filed its fourth amendment to the initial 2005 filing with the SEC on proposed Rule 2821 [now renumbered as Rule 2330] governing suitability and supervision in the sale of individual variable annuity contracts.

1. The fourth amendment dealt principally with modifications to supervisory review standards and recommendation requirements.
2. FINRA’s fourth amendment can be found at [http://www.nasd.com/web/groups/rules\\_regs/documents/rule\\_filing/nasdw\\_018737.pdf](http://www.nasd.com/web/groups/rules_regs/documents/rule_filing/nasdw_018737.pdf) .

C. *Round Four.* On November 15, 2006, FINRA filed its third amendment to the initial 2005 filing with the SEC, which is discussed below. FINRA requested prompt SEC approval of the rule without the opportunity for notice and public

D. comment.

1. In brief, the third amendment addressed, among other things: the time period for supervisory review; non-recommended transactions; undue concentration criteria; specificity of disclosure; and recommendation requirements.
2. FINRA's third amendment to the proposal appears at [http://www.nasd.com/RulesRegulation/RuleFilings/2004RuleFilings/NASDW\\_012781](http://www.nasd.com/RulesRegulation/RuleFilings/2004RuleFilings/NASDW_012781) .
3. As of November 15, 2006, the SEC staff did not intend to renounce FINRA proposal for public comment in light of amendment three. See comments of Catherine McGuire at ALI-ABA Seminar on Life Insurance Company Products (Nov. 15, 2006) at program MP3 §01:25:40.

E. Round Three. On June 6, 2006, the Securities and Exchange Commission invited comment on a revised FINRA suitability and supervision rule for variable annuity transactions recommended by registered representatives of broker-dealers. See Release No. 34-54023; File No. SR-NASD-2004-183, which appears at <http://www.sec.gov/rules/sro/nasd/2006/34-54023.pdf> .NASD filed two amendments to its initial 2005 rule proposal, at:

- a) [http://www.nasd.com/web/groups/rules\\_regs/documents/rule\\_filing/nasdw\\_016480.pdf](http://www.nasd.com/web/groups/rules_regs/documents/rule_filing/nasdw_016480.pdf)
- b) [http://www.nasd.com/web/groups/rules\\_regs/documents/rule\\_filing/nasdw\\_014678.pdf](http://www.nasd.com/web/groups/rules_regs/documents/rule_filing/nasdw_014678.pdf)

2. Over 1964 letters of comment were filed on the 2006 revisions, with the vast majority opposing all or parts of the FINRA initiative. A tiny fraction of the comments supported FINRA action. See the comment file at <http://www.sec.gov/rules/sro/nasd/nasd2004183.shtml>

F. *Round Two*. On July 19, 2005, the Securities and Exchange Commission invited comment on FINRA's initial free-standing suitability and supervision rule for variable annuity transactions recommended by registered representatives of broker-dealers. See Release No. 34-52046A; File No. SR-NASD-2004-183, which appears at <http://www.sec.gov/rules/sro/nasd/34-52046a.pdf> .

1. The SEC granted a 21-day extension to the initial 2005 comment period at Release No. 34-52191(Aug. 2, 2005) [File No. SR-NASD-2004-183] in response to ACLI's request dated July 27, 2005 (located in the comment file at <http://www.sec.gov/rules/sro/nasd/nasd2004183/cbwilkerson072705.pdf> ).
2. The actual text of the proposal did not appear in the SEC's invitation of comment directly, but only through cross reference to FINRA's general website address. The text appears in full at [http://www.nasd.com/web/groups/rules\\_regs/documents/rule\\_filing/nasdw\\_012780.pdf](http://www.nasd.com/web/groups/rules_regs/documents/rule_filing/nasdw_012780.pdf)

3. Most of the 1396 commentators opposed Rule 2821, and either recommended its elimination or substantial overhaul, as discussed below. See <http://www.sec.gov/rules/sro/nasd/nasd2004183.shtml>.

G. *Round One.* Prior to the SEC invitation of comment, FINRA solicited comment in June 2004, on an earlier version of the proposal that sought to formally codify several interpretive positions on supervision and suitability in a rule of conduct, and would have required broker-dealers to prepare and deliver a written point-of-sale document to customers.

1. The proposal appeared in FINRA Notice to Members 04-45. See <http://www.nasdr.com/pdf-text/0445ntm.pdf>. and Wilkerson, Proposed Variable Annuity Suitability Rule and Risk Disclosure Statement, ALI-ABA Conference on Life Insurance Company Products (Nov. 2002).
2. FINRA's draft proposal elicited 1,129 letters of comment.
  - a) According to the release, only fourteen of the commentators fully supported the proposal, and twenty offered partial or qualified support.
  - b) Using FINRA's numbers, 97% of the commentators opposed the initiative.
3. Companion Action by FINRA and SEC
  - a) On the same day of this FINRA rule proposal, the SEC and FINRA issued a joint report on inspection examination observations about the sale of variable insurance products.
    - (1) The joint report, which is referenced in ACLI General Bulletin No. 04-053, highlights both good practices by broker-dealers, as well as practices needing improvement.
    - (2) A copy of the report can be found at <http://www.sec.gov/news/studies/secnasdvip.pdf>
  - b) The SEC also issued an alert on June 9, 2004 "to remind investors that variable annuities are not suitable for all consumers, especially investors who need the money in the short term or who borrow against their home mortgage in order to purchase a variable annuity or variable life insurance product."
    - (1) The SEC's new alert is entitled Variable Annuities and Variable Life Products: Questions to Ask, and can be found at <http://www.sec.gov/investor/pubs/varaquestions.htm>
    - (2) SEC Chairman William Donaldson stated "[i]t is critical that broker-dealers ensure that the securities they sell are appropriate for the individual investor. Given the complexity of variable annuities, extra care is required. The findings of these examinations show that many firms should take steps to improve their practices. Investors

considering purchasing a variable annuity can obtain information about the product from the SEC and FINRA.”

## VIII. Implementation Timetable and History

A. The implementation dates on this new FINRA Rule have experienced several revisions.

B. On April 17, 2008, FINRA filed an amendment with the SEC requesting delayed implementation on provisions of Rule 2821, a new variable annuity suitability and supervision rule.

1. In part, the amendment responds to industry requests that FINRA delay the rule’s implementation because several aspects of the proposed rule needed further clarification, and because the costs of developing systems in light of the evolving clarifications would be unnecessarily increased.

C. On May 5, 2008, Rule 2821 became effective, except for paragraphs (c) and (d), which involve principal review, non-recommended transactions, and handling of customer funds pending supervisory approval.

D. Originally, the SEC approved Rule 2821 on September 13, 2007 with an effectiveness date of May 5, 2008. On September 7, 2007, the U.S. Securities and Exchange Commission approved new FINRA Rule 2821, which establishes suitability and supervision standards for variable annuity sales. See 72 Fed. Reg. 177 (September 13, 2007) at 52403.

a) On January 29, 2008, however, the SEC issued an order at FINRA’s request bifurcating implementation of Rule 2821 because of continued industry concerns about its proper application.

b) The SEC order granted (i) delayed implementation of paragraphs (c) and (d) until August 4, 2008 to allow FINRA time to address the challenged provision, and (ii) retained the original implementation date of May 5, 2008 for paragraphs (a), (b), and (e), that largely govern sales practice and training issues.

2. FINRA requested the amendment in response to interpretive and operational issues. ACLI asked FINRA to allow more time for systems development on Rule 2821, particularly in light of several outstanding operational issues.

a) On interpretive clarifications, ACLI recommended (i) additional

b) time for principal review when applications are incomplete; (ii) exclusion of non-recommended transactions from principal review; and, (iii) authorized deposit of customers' initial premium payments in life insurers' suspense accounts pending principal review of the transaction.

c) In its meetings with the SEC and FINRA about delayed implementation and substantive clarification, ACLI strongly recommended that the SEC circulate subsequent revisions to the rule for notice and comment before approving the rule (i) to give all interested parties a fair opportunity to address the revisions, and (ii) to avoid further rule postponements and associated system expenses. The SEC staff indicated that it would not grant an order of approval until after the opportunity for notice and comment this time. In contrast, the September 7, 2007, SEC order had approved FINRA's Rule 2821 [now renumbered Rule 2330] amendments and instituted effectiveness dates, while inviting comment after-the-fact.

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## **The NAIC Annuity Disclosure Model Regulation: Disclosure Standards in Annuity Distribution**

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### **I. Scope of Outline**

A. This outline summarizes the elements of the NAIC Annuity Disclosure Model Regulation, the required Disclosure Statement and the required NAIC Buyer's Guide to Fixed Deferred Annuities, including a supplement for Equity Indexed Annuities.

B. The NAIC Annuity Disclosure Model Regulation can be found at NAIC Model Reporting Service 245-I (April 2006).

### **II. Objective of the Annuity Disclosure Model Regulation**

A. To provide standards for the disclosure of certain minimum information about annuity contracts to protect consumers and foster consumer education.

1. The regulation specifies the minimum information which must be disclosed and the method and timing of delivering it.
2. The regulation seeks to ensure that purchasers of annuity contracts understand certain basic features of annuity contracts.

### **III. Annuities Covered by the Regulation**

A. All group and individual annuity contracts, except:

1. Registered or non-registered variable annuities.
2. Immediate and deferred annuities having only non-guaranteed elements.

3. Annuities used to fund:

- a) An employee pension plan which is covered by the Employee Retirement Income Security Act (ERISA);
- b) A plan described by Sections 401(a), 401(k) or 403(b) of the Internal Revenue Code, where the plan, for purposes of ERISA, is established or maintained by an employer,
- c) A governmental or church plan defined in Section 414 or a deferred compensation plan of a state or local government or a tax exempt organization under Section 457 of the Internal Revenue Code; or
- d) A nonqualified deferred compensation arrangement established or maintained by an employer or plan sponsor.

4. Structured Settlement Annuities.

5. Note: Under the model regulation, states may optionally elect to exclude charitable gift annuities and structured settlement annuities also.

#### **IV. Information Mandated in Required NAIC Disclosure Statement**

- A. The generic name of the contract, the company product name, if different, form number, and the fact that it is an annuity;
- B. The insurer's name and address;
- C. A description of the contract and its benefits, emphasizing its long-term nature, including examples where appropriate:
  - 1. The guaranteed, non-guaranteed and determinable elements of the contract, and their limitations, if any, and an explanation of how they operate;
  - 2. An explanation of the initial crediting rate, specifying any bonus or introductory portion, the duration of the rate and the fact that rates may change from time to time and are not guaranteed;
  - 3. Periodic income options both on a guaranteed and non-guaranteed basis;
  - 4. Any value reductions caused by withdrawals from or surrender of the contract;
  - 5. How values in the contract can be accessed;
  - 6. The death benefit, if available, and how it will be calculated;

7. A summary of the federal tax status of the contract and any penalties applicable on withdrawal of values from the contract; and
  8. Impact of any rider, such as a long-term care rider.
- D. Specific dollar amount or percentage charges and fees, which must be listed with an explanation of how they apply.
- E. Information about the current guaranteed rate for new contracts that contains a clear notice that the rate is subject to change.
- F. Insurers must define terms used in the disclosure statement in language understandable by a typical person in the target market.

**V. Required NAIC Buyer's Guide to Fixed Deferred Annuities (appears at the end of the outline).**

- A. A Buyer's Guide prepared by the NAIC provides information about different aspects of annuities, such as
1. What an annuity is.
  2. Descriptions of the different kinds of annuities.
    - a) Single premium or multiple premium.
    - b) Immediate or deferred.
    - c) Fixed or variable.
  3. How interest rates are set for the deferred variable annuity.
    - a) Explanation of current interest rate.
    - b) Explanation of minimum guaranteed rate.
    - c) Explanation of multiple interest rates.
  4. Description of charges in the contract.
    - a) Surrender or withdrawal charges.
    - b) Free withdrawal features.
    - c) Contract fee.
    - d) Transaction fee.
    - e) Percentage of premium charge.
    - f) Premium tax charge.

## 5. Fixed Annuity Benefits

- a) Annuity income payments.
- b) Annuity payment options.
  - (1) Life only.
  - (2) Life annuity with period certain.
  - (3) Joint and survivor.

## VI. Timetable for Delivery of Required Disclosure Statement and Buyer's Guide:

A. At or before the time of application if annuity application is taken in a *face-to-face meeting*.

B. No later than five (5) business days after the completed application is received by the insurer, if annuity application is taken by means *other than in a face-to-face meeting*.

- 1. With applications received from a *direct solicitation through the mail*:
  - a) Inclusion of a Buyer's Guide and Disclosure Statement in the direct mail solicitation satisfies the requirement for delivery no later than five (5) business days after receipt of the application.
- 2. *For applications received via the Internet*:
  - a) Taking reasonable steps to make the Buyer's Guide and Disclosure Statement available for viewing and printing on the insurer's website satisfies the requirement for delivery no later than five (5) business day of receipt of the application.
- 3. Annuity solicitations in other than face-to-face meetings must include a statement that the proposed applicant may contact the insurance department of the state for a free annuity Buyer's Guide. Alternatively, the insurer may include a statement that the prospective applicant may contact the insurer for a free annuity Buyer's Guide.
- 4. *Extended Free-Look Period*: where the Buyer's Guide and disclosure document are not provided at or before the time of application, a free look period of no less than fifteen (15) days shall be provided for the applicant to return the annuity contract without penalty. The free look runs concurrently with any other free look provided under state law or regulation.

## VII. Required Report to Contract Owners

A. For annuities in the payout period with changes in non-guaranteed elements and for the accumulation period of a deferred annuity, the insurer

must provide each contract owner with a report, *at least annually*, on the status of the contract that contains at least the following information:

1. The beginning and end date of the current report period;
2. The accumulation and cash surrender value, if any, at the end of the previous report period and at the end of the current report period;
3. The total amounts, if any, that have been credited, charged to the contract value or paid during the current report period; and
4. The amount of outstanding loans, if any, as of the end of the current report period.

**VIII. A State-by-State Index** to the NAIC Annuity Disclosure Model Regulation Appears on page 11 following the outline on the NAIC Suitability in Annuity Transactions Model Regulation.

**IX. NAIC Buyer's Guide: Appears on Pages Immediately Following This Outline**

- A. Fixed Deferred Annuities are highlighted at the front of the Guide.
- B. Equity Index Annuities are highlighted in a supplement at the back of the Guide.

### **Annuity Buyer's Guide**

Prepared by the National Association of Insurance Commissioners

The National Association of Insurance Commissioners is an association of state insurance regulatory officials. This association helps the various insurance departments to coordinate insurance laws for the benefit of all consumers.

This guide does not endorse any company or policy.

#### ***Reprinted by XYZ Life Insurance Company***

It is important that you understand the differences among various annuities so you can choose the kind that best fits your needs. This guide focuses on fixed deferred annuity contracts. There is, however, a brief description of variable annuities. If you're thinking of buying an equity-indexed annuity, an appendix to this guide will give you specific information. This Guide isn't meant to offer legal, financial or tax advice. You may want to consult independent advisors. At the end of this Guide are questions you should ask your agent or the company. Make sure you're satisfied with the answers before you buy.

#### **WHAT IS AN ANNUITY?**

An annuity is a contract in which an insurance company makes a series of income payments at regular intervals in return for a premium or premiums you have paid. Annuities are most often bought

for future retirement income. Only an annuity can pay an income that can be guaranteed to last as long as you live.

An annuity is neither a life insurance nor a health insurance policy. It's not a savings account or a savings certificate. You shouldn't buy an annuity to reach short-term financial goals.

Your value in an annuity contract is the premiums you've paid, less any applicable charges, plus interest credited. The insurance company uses the value to figure the amount of most of the benefits that you can choose to receive from an annuity contract. This guide explains how interest is credited as well as some typical charges and benefits of annuity contracts.

A deferred annuity has two parts or periods. During the accumulation period, the money you put into the annuity, less any applicable charges, earns interest. The earnings grow tax-deferred as long as you leave them in the annuity. During the second period, called the payout period, the company pays income to you or to someone you choose.

## **WHAT ARE THE DIFFERENT KINDS OF ANNUITIES?**

This guide explains major differences in different kinds of annuities to help you understand how each might meet your needs. But look at the specific terms of an individual contract you're considering and the disclosure document you receive. If your annuity is being used to fund or provide benefits under a pension plan, the benefits you get will depend on the terms of the plan. Contact your pension plan administrator for information.

This Buyer's Guide will focus on individual fixed deferred annuities.

### **Single Premium or Multiple Premium**

You pay the insurance company only one payment for a single premium annuity. You make a series of payments for a multiple premium annuity. There are two kinds of multiple premium annuities. One kind is a flexible premium contract. Within set limits, you pay as much premium as you want, whenever you want. In the other kind, a scheduled premium annuity, the contract spells out your payments and how often you'll make them.

### **Immediate or Deferred**

With an immediate annuity, income payments start no later than one year after you pay the premium. You usually pay for an immediate annuity with one payment.

The income payments from a deferred annuity often start many years later. Deferred annuities have an accumulation period, which is the time between when you start paying premiums and when income payments start.

### **Fixed or Variable**

#### **• Fixed**

During the accumulation period of a fixed deferred annuity, your money (less any applicable charges) earns interest at rates set by the insurance company or in a way spelled out in the annuity contract. The company guarantees that it will pay no less than a minimum rate of interest. During the

payout period, the amount of each income payment to you is generally set when the payments start and will not change.

- **Variable**

During the accumulation period of a variable annuity, the insurance company puts your premiums (less any applicable charges) into a separate account. You decide how the company will invest those premiums, depending on how much risk you want to take. You may put your premium into a stock, bond or other account, with no guarantees, or into a fixed account, with a minimum guaranteed interest. During the payout period of a variable annuity, the amount of each income payment to you may be fixed (set at the beginning) or variable (changing with the value of the investments in the separate account).

### **HOW ARE THE INTEREST RATES SET FOR MY FIXED DEFERRED ANNUITY?**

During the accumulation period, your money (less any applicable charges) earns interest at rates that change from time to time. Usually, what these rates will be is entirely up to the insurance company.

#### **Current Interest Rate**

The current rate is the rate the company decides to credit to your contract at a particular time. The company will guarantee it will not change for some time period.

- The initial rate is an interest rate the insurance company may credit for a set period of time after you first buy your annuity. The initial rate in some contracts may be higher than it will be later. This is often called a bonus rate.

- The renewal rate is the rate credited by the company after the end of the set time period. The contract tells how the company will set the renewal rate, which may be tied to an external reference or index.

#### **Minimum Guaranteed Rate**

The minimum guaranteed interest rate is the lowest rate your annuity will earn. This rate is stated in the contract.

#### **Multiple Interest Rates**

Some annuity contracts apply different interest rates to each premium you pay or to premiums you pay during different time periods.

Other annuity contracts may have two or more accumulated values that fund different benefit options. These accumulated values may use different interest rates. You get only one of the accumulated values depending on which benefit you choose.

### **WHAT CHARGES MAY BE SUBTRACTED FROM MY FIXED DEFERRED ANNUITY?**

Most annuities have charges related to the cost of selling or servicing it. These charges may be subtracted directly from the contract value. Ask your agent or the company to describe the charges that apply to your annuity. Some examples of charges, fees and taxes are:

## **Surrender or Withdrawal Charges**

If you need access to your money, you may be able to take all or part of the value out of your annuity at any time during the accumulation period. If you take out part of the value, you may pay a withdrawal charge. If you take out all of the value and surrender, or terminate, the annuity, you may pay a surrender charge. In either case, the company may figure the charge as a percentage of the value of the contract, of the premiums you've paid or of the amount you're withdrawing. The company may reduce or even eliminate the surrender charge after you've had the contract for a stated number of years. A company may waive the surrender charge when it pays a death benefit.

Some annuities have stated terms. When the term is up, the contract may automatically expire or renew. You're usually given a short period of time, called a window, to decide if you want to renew or surrender the annuity. If you surrender during the window, you won't have to pay surrender charges. If you renew, the surrender or withdrawal charges may start over.

In some annuities, there is no charge if you surrender your contract when the company's current interest rate falls below a certain level. This may be called a bail-out option.

In a multiple-premium annuity, the surrender charge may apply to each premium paid for a certain period of time. This may be called a rolling surrender or withdrawal charge.

Some annuity contracts have a market value adjustment feature. If interest rates are different when you surrender your annuity than when you bought it, a market value adjustment may make the cash surrender value higher or lower. Since you and the insurance company share this risk, an annuity with a MVA feature may credit a higher rate than an annuity without that feature.

Be sure to read the Tax Treatment section and ask your tax advisor for information about possible tax penalties on withdrawals.

### **Free Withdrawal**

Your annuity may have a limited free withdrawal feature. That lets you make one or more withdrawals without a charge. The size of the free withdrawal is often limited to a set percentage of your contract value. If you make a larger withdrawal, you may pay withdrawal charges. You may lose any interest above the minimum guaranteed rate on the amount withdrawn. Some annuities waive withdrawal charges in certain situations, such as death, confinement in a nursing home or terminal illness.

### **Contract Fee**

A contract fee is a flat dollar amount charged either once or annually.

### **Transaction Fee**

A transaction fee is a charge per premium payment or other transaction.

### **Percentage of Premium Charge**

A percentage of premium charge is a charge deducted from each premium paid. The percentage may be lower after the contract has been in force for a certain number of years or after total premiums paid have reached a certain amount.

### **Premium Tax**

Some states charge a tax on annuities. The insurance company pays this tax to the state. The company may subtract the amount of the tax when you pay your premium, when you withdraw your contract value, when you start to receive income payments or when it pays a death benefit to your beneficiary.

### **WHAT ARE SOME FIXED DEFERRED ANNUITY CONTRACT BENEFITS?**

#### **Annuity Income Payments**

One of the most important benefits of deferred annuities is your ability to use the value built up during the accumulation period to give you a lump sum payment or to make income payments during the payout period. Income payments are usually made monthly but you may choose to receive them less often. The size of income payments is based on the accumulated value in your annuity and the annuity's benefit rate in effect when income payments start. The benefit rate usually depends on your age and sex, and the annuity payment option you choose. For example, you might choose payments that continue as long as you live, as long as your spouse lives or for a set number of years.

There is a table of guaranteed benefit rates in each annuity contract. Most companies have current benefit rates as well. The company can change the current rates at any time, but the current rates can never be less than the guaranteed benefit rates. When income payments start, the insurance company generally uses the benefit rate in effect at that time to figure the amount of your income payment.

Companies may offer various income payment options. You (the owner) or another person that you name may choose the option. The options are described here as if the payments are made to you.

- **Life Only** - The company pays income for your lifetime. It doesn't make any payments to anyone after you die. This payment option usually pays the highest income possible. You might choose it if you have no dependents, if you have taken care of them through other means or if the dependents have enough income of their own.

- **Life Annuity with Period Certain** - The company pays income for as long as you live and guarantees to make payments for a set number of years even if you die. This period certain is usually 10 or 20 years. If you live longer than the period certain, you'll continue to receive payments until you die. If you die during the period certain, your beneficiary gets regular payments for the rest of that period. If you die after the period certain, your beneficiary doesn't receive any payments from your annuity. Because the "period certain" is an added benefit, each income payment will be smaller than in a life-only option.

- **Joint and Survivor** - The company pays income as long as either you or your beneficiary lives. You may choose to decrease the amount of the payments after the first death. You may also be able to choose to have payments continue for a set length of time. Because the survivor feature is an added benefit, each income payment is smaller than in a life-only option.

### **Death Benefit**

In some annuity contracts, the company may pay a death benefit to your beneficiary if you die before the income payments start. The most common death benefit is the contract value or the premiums paid, whichever is more.

### **CAN MY ANNUITY'S VALUE BE DIFFERENT DEPENDING ON MY CHOICE OF BENEFIT?**

While all deferred annuities offer a choice of benefits, some use different accumulated values to pay different benefits. For example, an annuity may use one value if annuity payments are for retirement benefits and a different value if the annuity is surrendered. As another example, an annuity may use one value for long-term care benefits and a different value if the annuity is surrendered. You can't receive more than one benefit at the same time.

### **WHAT ABOUT THE TAX TREATMENT OF ANNUITIES?**

Below is a general discussion about taxes and annuities. You should consult a professional tax advisor to discuss your individual tax situation.

Under current federal law, annuities receive special tax treatment. Income tax on annuities is deferred, which means you aren't taxed on the interest your money earns while it stays in the annuity. Tax-deferred accumulation isn't the same as tax-free accumulation. An advantage of tax deferral is that the tax bracket you're in when you receive annuity income payments may be lower than the one you're in during the accumulation period. You'll also be earning interest on the amount you would have paid in taxes during the accumulation period. Most states' tax laws on annuities follow the federal law.

Part of the payments you receive from an annuity will be considered as a return of the premium you've paid. You won't have to pay taxes on that part. Another part of the payments is considered interest you've earned. You must pay taxes on the part that is considered interest when you withdraw the money. You may also have to pay a 10% tax penalty if you withdraw the accumulation before age 59 1/2. The Internal Revenue Code also has rules about distributions after the death of a contract holder.

Annuities used to fund certain employee pension benefit plans (those under Internal Revenue Code Sections 401(a), 401(k), 403(b), 457 or 414) defer taxes on plan contributions as well as on interest or investment income. Within the limits set by the law, you can use pretax dollars to make payments to the annuity. When you take money out, it will be taxed.

You can also use annuities to fund traditional and Roth IRAs under Internal Revenue Code Section 408. If you buy an annuity to fund an IRA, you'll receive a disclosure statement describing the tax treatment.

### **WHAT IS A "FREE LOOK" PROVISION?**

Many states have laws which give you a set number of days to look at the annuity contract after you buy it. If you decide during that time that you don't want the annuity, you can return the contract and get all your money back. This is often referred to as a free look or right to return period. The free look period should be prominently stated in your contract. Be sure to read your contract carefully during the free look period.

### **HOW DO I KNOW IF A FIXED DEFERRED ANNUITY IS RIGHT FOR ME?**

The questions listed below may help you decide which type of annuity, if any, meets your retirement planning and financial needs. You should think about what your goals are for the money you may put into the annuity. You need to think about how much risk you're willing to take with the money. Ask yourself:

- How much retirement income will I need in addition to what I will get from Social Security and my pension?

- Will I need that additional income only for myself or for myself and someone else?
- How long can I leave my money in the annuity?
- When will I need income payments?
- Does the annuity let me get money when I need it?
- Do I want a fixed annuity with a guaranteed interest rate and little or no risk of losing the principal?
- Do I want a variable annuity with the potential for higher earnings that aren't guaranteed and the possibility that I may risk losing principal?
- Or, am I somewhere in between and willing to take some risks with an equity-indexed annuity?

#### **WHAT QUESTIONS SHOULD I ASK MY AGENT OR THE COMPANY?**

- Is this a single premium or multiple premium contract?
- Is this an equity-indexed annuity?
- What is the initial interest rate and how long is it guaranteed?
- Does the initial rate include a bonus rate and how much is the bonus?
- What is the guaranteed minimum interest rate?
- What renewal rate is the company crediting on annuity contracts of the same type that were issued last year?
- Are there withdrawal or surrender charges or penalties if I want to end my contract early and take out all of my money? How much are they?
- Can I get a partial withdrawal without paying surrender or other charges or losing interest?
- Does my annuity waive withdrawal charges for reasons such as death, confinement in a nursing home or terminal illness?
- Is there a market value adjustment (MVA) provision in my annuity?
- What other charges, if any, may be deducted from my premium or contract value?

- If I pick a shorter or longer payout period or surrender the annuity, will the accumulated value or the way interest is credited change?
- Is there a death benefit? How is it set? Can it change?
- What income payment options can I choose? Once I choose a payment option, can I change it?

### **FINAL POINTS TO CONSIDER**

Before you decide to buy an annuity, you should review the contract. Terms and conditions of each annuity contract will vary.

Ask yourself if, depending on your needs or age, this annuity is right for you. Taking money out of an annuity may mean you must pay taxes. Also, while it's sometimes possible to transfer the value of an older annuity into a new annuity, the new annuity may have a new schedule of charges that could mean new expenses you must pay directly or indirectly.

You should understand the long-term nature of your purchase. Be sure you plan to keep an annuity long enough so that the charges don't take too much of the money you put in. Be sure you understand the effect of all charges.

If you're buying an annuity to fund an IRA or other tax-deferred retirement program, be sure that you're eligible. Also, ask if there are any restrictions connected with the program.

Remember that the quality of service that you can expect from the company and the agent is a very important factor in your decision.

When you receive your annuity contract, **READ IT CAREFULLY!!** Ask the agent and company for an explanation of anything you don't understand. Do this before any free look period ends.

Compare information for similar contracts from several companies. Comparing products may help you make a better decision.

If you have a specific question or can't get answers you need from the agent or company, contact your state insurance department.

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## **APPENDIX I-EQUITY-INDEXED ANNUITIES**

This appendix to the Buyer's Guide for Fixed Deferred Annuities will focus on equity-indexed annuities. Like other types of fixed deferred annuities, equity-indexed annuities provide for annuity income payments, death benefits and tax-deferred accumulation. You should read the Buyer's Guide for general information about those features and about provisions such as withdrawal and surrender charges.

### **WHAT ARE EQUITY-INDEXED ANNUITIES?**

An equity-indexed annuity is a fixed annuity, either immediate or deferred, that earns interest or provides benefits that are linked to an external equity reference or an equity index. The value of the index might be tied to a stock or other equity index. One of the most commonly used indices is Standard & Poor's 500 Composite Stock Price Index (the S&P 500), which is an equity index. The value of any index varies from day to day and is not predictable. (Note: S&P 500 is a registered trademark of the McGraw-Hill Companies, Inc., used with permission.)

When you buy an equity-indexed annuity you own an insurance contract. You are not buying shares of any stock or index.

While immediate equity-indexed annuities may be available, this appendix will focus on deferred equity-indexed annuities.

### **HOW ARE THEY DIFFERENT FROM OTHER FIXED ANNUITIES?**

An equity-indexed annuity is different from other fixed annuities because of the way it credits interest to your annuity's value. Some fixed annuities only credit interest calculated at a rate set in the contract. Other fixed annuities also credit interest at rates set from time to time by the insurance company. Equity-indexed annuities credit interest using a formula based on changes in the index to which the annuity is linked. The formula decides how the additional interest, if any, is calculated and credited. How much additional interest you get and when you get it depends on the features of your particular annuity.

Your equity-indexed annuity, like other fixed annuities, also promises to pay a minimum interest rate. The rate that will be applied will not be less than this minimum guaranteed rate even if the index-linked interest rate is lower. The value of your annuity also will not drop below a guaranteed minimum. For example, many single premium contracts guarantee the minimum value will never be less than 90 percent of the premium paid, plus at least 3% in annual interest (less any partial withdrawals). The guaranteed value is the minimum amount available during a term for withdrawals, as well as for some annuitizations (see "Annuity Income Payments") and death benefits. The insurance company will adjust the value of the annuity at the end of each term to reflect any index increases.

### **WHAT ARE SOME EQUITY-INDEXED ANNUITY CONTRACT FEATURES?**

Two features that have the greatest effect on the amount of additional interest that may be credited to an equity-indexed annuity are the indexing method and the participation rate. It is important to understand the features and how they work together. The following describes some other equity-indexed annuity features that affect the index-linked formula.

### **Indexing Method**

The indexing method means the approach used to measure the amount of change, if any, in the index. Some of the most common indexing methods, which are explained more fully later on, include annual reset (ratcheting), high-water mark and point-to-point.

### **Term**

The index term is the period over which index-linked interest is calculated; the interest is credited to your annuity at the end of a term. Terms are generally from one to ten years, with six or seven years being most common. Some annuities offer single terms while others offer multiple, consecutive terms. If your annuity has multiple terms, there will usually be a window at the end of each term, typically 30 days, during which you may withdraw your money without penalty. For installment premium annuities, the payment of each premium may begin a new term for that premium.

### **Participation Rate**

The participation rate decides how much of the increase in the index will be used to calculate index-linked interest. For example, if the calculated change in the index is 9% and the participation rate is 70%, the index-linked interest rate for your annuity will be 6.3% ( $9\% \times 70\% = 6.3\%$ ). A company may set a different participation rate for newly issued annuities as often as each day. Therefore, the initial participation rate in your annuity will depend on when it is issued by the company. The company usually guarantees the participation rate for a specific period (from one year to the entire term). When that period is over, the company sets a new participation rate for the next period. Some annuities guarantee that the participation rate will never be set lower than a specified minimum or higher than a specified maximum.

### **Cap Rate or Cap**

Some annuities may put an upper limit, or cap, on the index-linked interest rate. This is the maximum rate of interest the annuity will earn. In the example given above, if the contract has a 6% cap rate, 6%, and not 6.3%, would be credited. Not all annuities have a cap rate.

### **Floor on Equity Index-Linked Interest**

The floor is the minimum index-linked interest rate you will earn. The most common floor is 0%. A 0% floor assures that even if the index decreases in value, the index-linked interest that you earn will be zero and not negative. As in the case of a cap, not all annuities have a stated floor on index-linked interest rates. But in all cases, your fixed annuity will have a minimum guaranteed value.

### **Averaging**

In some annuities, the average of an index's value is used rather than the actual value of the index on a specified date. The index averaging may occur at the beginning, the end, or throughout the entire term of the annuity.

### **Interest Compounding**

Some annuities pay simple interest during an index term. That means index-linked interest is added to your original premium amount but does not compound during the term. Others pay compound interest during a term, which means that index-linked interest that has already been credited also earns interest in the future. In either case, however, the interest earned in one term is usually compounded in the next.

### **Margin/Spread/Administrative Fee**

In some annuities, the index-linked interest rate is computed by subtracting a specific percentage from any calculated change in the index. This percentage, sometimes referred to as the "margin," "spread," or "administrative fee," might be instead of, or in addition to, a participation rate. For example, if the calculated change in the index is 10%, your annuity might specify that 2.25% will be subtracted from the rate to determine the interest rate credited. In this example, the rate would be 7.75% ( $10\% - 2.25\% = 7.75\%$ ). In this example, the company subtracts the percentage only if the change in the index produces a positive interest rate.

### **Vesting**

Some annuities credit none of the index-linked interest or only part of it, if you take out all your money before the end of the term. The percentage that is vested, or credited, generally increases as the term comes closer to its end and is always 100% at the end of the term.

## **HOW DO THE COMMON INDEXING METHODS DIFFER?**

### **Annual Reset**

Index-linked interest, if any, is determined each year by comparing the index value at the end of the contract year with the index value at the start of the contract year. Interest is added to your annuity each year during the term.

### **High-Water Mark**

The index-linked interest, if any, is decided by looking at the index value at various points during the term, usually the annual anniversaries of the date you bought the annuity. The interest is based on the difference between the highest index value and the index value at the start of the term. Interest is added to your annuity at the end of the term.

### **Low-Water Mark**

The index-linked interest, if any, is determined by looking at the index value at various points during the term, usually the annual anniversaries of the date you bought the

annuity. The interest is based on the difference between the index value at the end of the term and the lowest index value. Interest is added to your annuity at the end of the term.

#### Point-to-Point

The index-linked interest, if any, is based on the difference between the index value at the end of the term and the index value at the start of the term. Interest is added to your annuity at the end of the term.

### **WHAT ARE SOME OF THE FEATURES AND TRADE-OFFS OF DIFFERENT INDEXING METHODS?**

Generally, equity-indexed annuities offer preset combinations of features. You may have to make trade-offs to get features you want in an annuity. This means the annuity you chose may also have features you don't want.

<b>Features</b>	<b>Trade-Offs</b>
<p><b>Annual Reset</b></p> <p>Since the interest earned is "locked in" annually and the index value is "reset" at the end of each year, future decreases in the index will not affect the interest you have already earned. Therefore, your annuity using the annual reset method may credit more interest than annuities using other methods when the index fluctuates up and down often during the term. This design is more likely than others to give you access to index-linked interest before the term ends.</p>	<p>Your annuity's participation rate may change each year and generally will be lower than that of other indexing methods. Also an annual reset design may use a cap or averaging to limit the total amount of interest you might earn each year.</p>
<p><b>High-Water Mark</b></p> <p>Since interest is calculated using the highest value of the index on a contract anniversary during the term, this design may credit higher interest than some other designs if the index reaches a high point early or in the middle of the term, then drops off at the end of the term.</p>	<p>Interest is not credited until the end of the term. In some annuities, if you surrender your annuity before the end of the term, you may not get index-linked interest for that term. In other annuities, you may receive index-linked interest, based on the highest anniversary value to date and the annuity's vesting schedule. Also, contracts with this design may have a lower participation rate than annuities</p>

using other designs or may use a cap to limit the total amount of interest you might earn.

### Low-Water Mark

Since interest is calculated using the lowest value of the index prior to the end of the term, this design may credit higher interest than some other designs if the index reaches a low point early or in the middle of the term and then rises at the end of the term.

Interest is not credited until the end of the term. With some annuities, if you surrender your annuity before the end of the term, you may not get index-linked interest for that term. In other annuities, you may receive index-linked interest based on a comparison of the lowest anniversary value to date with the index value at surrender and the annuity's vesting schedule. Also, contracts with this design may have a lower participation rate than annuities using other designs or may use a cap to limit the total amount of interest you might earn.

### Point-to-Point

Since interest cannot be calculated before the end of the term, use of this design may permit a higher participation rate than annuities using other designs.

Since interest is not credited until the end of the term, typically six or seven years, you may not be able to get the index-linked interest until the end of the term.

## **WHAT IS THE IMPACT OF SOME OTHER EQUITY-INDEXED ANNUITY PRODUCT FEATURES?**

### **Cap on Interest Earned**

While a cap limits the amount of interest you might earn each year, annuities with this feature may have other product features you want, such as annual interest crediting or the ability to take partial withdrawals. Also, annuities that have a cap may have a higher participation rate.

### **Averaging**

Averaging at the beginning of a term protects you from buying your annuity at a high point, which would reduce the amount of interest you might earn. Averaging at the end of the term protects you against severe declines in the index and losing index-linked interest as a result. On the other hand, averaging may reduce the amount of index-linked interest you earn when the index rises either near the start or at the end of the term.

### **Participation Rate**

The participation rate may vary greatly from one annuity to another and from time to time within a particular annuity. Therefore, it is important for you to know how your annuity's

participation rate works with the indexing method. A high participation rate may be offset by other features, such as simple interest, averaging, or a point-to-point indexing method. On the other hand, an insurance company may offset a lower participation rate by also offering a feature such as an annual reset indexing method.

### **Interest Compounding**

It is important for you to know whether your annuity pays compound or simple interest during a term. While you may earn less from an annuity that pays simple interest, it may have other features you want, such as a higher participation rate.

### **WHAT WILL IT COST ME TO TAKE MY MONEY OUT BEFORE THE END OF THE TERM?**

In addition to the information discussed in this Buyer's Guide about surrender and withdrawal charges and free withdrawals, there are additional considerations for equity-indexed annuities. Some annuities credit none of the index-linked interest or only part of it if you take out money before the end of the term. The percentage that is vested, or credited, generally increases as the term comes closer to its end and is always 100% at the end of the term.

### **ARE DIVIDENDS INCLUDED IN THE INDEX?**

Depending on the index used, stock dividends may or may not be included in the index's value. For example, the S&P 500 is a stock price index and only considers the prices of stocks. It does not recognize any dividends paid on those stocks.

### **HOW DO I KNOW IF AN EQUITY-INDEXED ANNUITY IS RIGHT FOR ME?**

The questions listed below may help you decide which type of annuity, if any, meets your retirement planning and financial needs. You should consider what your goals are for the money you may put into the annuity. You need to think about how much risk you're willing to take with the money. Ask yourself:

Am I interested in a variable annuity with the potential for higher earnings that are not guaranteed and willing to risk losing the principal?

Is a guaranteed interest rate more important to me, with little or no risk of losing the principal?

Or, am I somewhere in between these two extremes and willing to take some risks?

### **HOW DO I KNOW WHICH EQUITY-INDEXED ANNUITY IS BEST FOR ME?**

As with any other insurance product, you must carefully consider your own personal situation and how you feel about the choices available. No single annuity design may have all the features you want. It is important to understand the features and trade-offs available so you can choose the annuity that is right for you. Keep in mind that it may be misleading to compare one annuity to another unless you compare all the other features of each annuity. You must decide for yourself what combination of features makes the most sense for you. Also remember that it is not possible to predict the future behavior of an index.

## **QUESTIONS YOU SHOULD ASK YOUR AGENT OR THE COMPANY**

You should ask the following questions about equity-indexed annuities in addition to the questions in the Buyer's Guide to Fixed Deferred Annuities.

- How long is the term?
- What is the guaranteed minimum interest rate?
- What is the participation rate? For how long is the participation rate guaranteed?
- Is there a minimum participation rate?
- Does my contract have an interest rate cap? What is it?
- Does my contract have an interest rate floor? What is it?
- Is interest rate averaging used? How does it work?
- Is interest compounded during a term?
- Is there a margin, spread, or administrative fee? Is that in addition to or instead of a participation rate?
- What indexing method is used in my contract?
- What are the surrender charges or penalties if I want to end my contract early and take out all of my money?
- Can I get a partial withdrawal without paying charges or losing interest? Does my contract have vesting? If so, what is the rate of vesting?

### **Final Points to Consider**

Remember to read your annuity contract carefully when you receive it. Ask your agent or insurance company to explain anything you don't understand. If you have a specific complaint or can't get answers you need from the agent or company, contact your state insurance department.

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## **NAIC Insurance and Annuities Replacement Model Regulation: A Systemic Approach to Appropriate Sales Practices**

Carl B. Wilkerson, Vice President & Chief Counsel-Securities & Litigation  
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### **I. NAIC Insurance and Annuities Replacement Model Regulation**

A. In June 2000, the NAIC adopted substantial amendments to the 1998 Insurance and Annuities Replacement Model Regulation. This regulation establishes substantial protections for consumers through required systems of supervision, control, monitoring, and recordkeeping for insurers and producers. Additionally, the regulation requires plain-English notices, and signed disclosure about the replacement transaction.

1. The NAIC's Model Regulation and amendments promote uniformity among state insurance regulations.
2. Citation: Insurance and Annuities Replacement Model Regulation, NAIC Model Regulation Service-July 2000 at III-621-1.

#### **B. Approach of the amended regulation**

1. The amended regulation establishes duties for insurance producers, replacing insurers, and existing insurers designed to protect consumers.
  - a. For example, insurers using insurance producers must, among other things:
    - (1) *Maintain a system of supervision and control;*
    - (2) *Have the capacity to monitor each producer's life and annuity replacements for that insurer;*
    - (3) *Ascertain that required sales material and illustrations are complete and accurate;* and
    - (4) *Maintain records of required notification forms and illustrations that can be produced.*
  - b. A required notice of replacement must be presented, read to consumers, and signed by the producer and consumer.
2. The regulation lists illustrative violations, and establishes penalties that may include the revocation or suspension of a producer's or company's license, monetary fines, and forfeiture of commissions or compensation. Commissioners may require insurers to make

restitution, and restore policy values with interest when violation are material to the sale. [See, Section 8 of the regulation].

#### C. Overview of Issue

1. A replacement occurs when an individual uses existing life insurance policy or annuity contract values to purchase a new policy or contract.
2. A replacement may involve the use of the entire value of an existing policy or contract, as in the case of a surrender, or it may involve the use of only a portion of the existing values.
3. Under the NAIC Model as amended in 2000, the use of *any* portion of the values of an existing policy or contract to purchase a new policy or contract constitutes replacement, including borrowing, assigning dividends, lapsing, or forfeiting.
  - a. External replacement occurs when a company replaces the life or annuity product of another company.
  - b. Internal replacement occurs when a company replaces a life or annuity contract that it has already issued.

#### D. *Purpose* of the Amended NAIC Replacement Regulation

1. To regulate the activities of insurers and producers with respect to the replacement of existing life insurance and annuities.
2. To protect the interests of life insurance and annuity purchasers by establishing minimum standards of conduct to be observed in replacement or financed purchase transactions, and to:
  - a. Assure that purchasers receive information with which a decision can be made in his or her own best interest;
  - b. Reduce the opportunity for misrepresentation and incomplete disclosure; and
  - c. Establish penalties for failure to comply with the regulation.

#### E. Regulation *Applies to Variable Life Insurance and Variable Annuity Replacements*

1. The term *replacement* is defined in the regulation to mean a transaction in which a new policy or contract is to be purchased, and it is known or should be known to the proposing producer, or to the proposing insurer if there is no producer, that by reason of the transaction, an existing policy or contract has been or is to be:
  - a. Lapsed, forfeited, surrendered or partially surrendered,

assigned to the replacing insurer or otherwise terminated;

- b. Converted to reduced paid-up insurance, continued as extended term insurance, or otherwise reduced in value by the use of nonforfeiture benefits or other policy values;
  - c. Amended so as to effect either a reduction in force of for which benefits would be paid;
  - d. Reissued with any reduction in cash value; or
  - e. Used in a financed purchase.
2. The regulation excuses variable life and variable annuity contracts from requirements in Sections 5(A)(2) and 6(B) to provide illustrations or policy summaries.
- a. In place of the policy summaries and illustrations requirement, the regulation mandates “premium or contract distribution amounts and identification of the appropriate prospectus or offering circular” instead.
  - b. In all other respects, the regulation fully applies to individual variable contract replacements.

F. *Exceptions* from regulation for group contracts

1. The regulation does not apply to transactions involving:
- a. Policies or contracts used to fund:
    - (1) An employee pension or welfare benefit plan that is covered by the Employee Retirement and Income Security Act (ERISA);
    - (2) A plan described by Sections 401(a), 401(k) or 403(b) of the Internal Revenue Code, where the plan, for purposes of ERISA, is established or maintained by an employer;
    - (3) A governmental or church plan defined in Section 414, a governmental or church welfare benefit plan, or a deferred compensation plan of a state or local government or tax exempt organization under Section 457 of the Internal Revenue Code; or
    - (4) A non-qualified deferred compensation arrangement established or maintained by an employer or plan sponsor.
  - b. Group life insurance or group annuities where there is no

direct solicitation of individuals by an insurance producer.

c. Credit life insurance.

## G. Duties of Producers and Insurers in Replacement Transactions

### 1. Duties of insurers that use producers [Section 4.]

a. Under the regulation, each insurer must:

- (1) *Maintain a system of supervision and control* to insure compliance with the requirements of this regulation that shall *include at least* the following:
  - (a) *Inform its producers of the requirements of the regulation* and incorporate the requirements of the regulation into all relevant *producer training manuals* prepared by the insurer;
  - (b) *Provide to each producer a written statement of the company's position with respect to the acceptability of replacements* providing guidance to its producer as to the appropriateness of these transactions;
  - (c) *A system to review the appropriateness of each replacement transaction that the producer does not indicate is in accord with the regulation's standards;*
  - (d) Procedures to *confirm* that the *requirements* of this regulation have been *met*; and
  - (e) Procedures to *detect transactions that are replacements of existing policies or contracts* by the existing insurer, but that have not been identified as such by the applicant or producer.
- (2) *Have the capacity to produce*, upon request, and make available to the Insurance Department, *records of each producer's*:
  - (a) *Replacements*, including financed purchases, as a percentage of the producer's total annual sales for life insurance and annuity contracts not exempted from this regulation;
  - (b) *Number of lapses* of policies and contracts

by the producer as a percentage of the producer's total annual sales for life insurance and annuity contracts not exempted from this regulation;

- (c) Number of transactions that are *unidentified replacements of existing policies* or contracts by the existing insurer detected by the company's monitoring system as required by Section (4)(A)(5) of the regulation; and
  - (d) *Replacements, indexed by replacing producer and existing insurer.*
- (3) Require with or as a part of each application for life insurance or an annuity a signed statement by both the applicant and the producer as to whether the applicant has existing policies or contracts;
  - (4) Require with each application for life insurance or an annuity that indicates an existing policy or contract a completed notice regarding replacements as contained in Attachment 1 to the regulation;
  - (5) When the applicant has existing policies or contracts, retain completed and signed copies of the notice regarding replacements in its home or regional office for at least five years after the termination or expiration of the proposed policy or contract;
  - (6) When the applicant has existing policies or contracts, obtain and retain copies of any sales material as required by Section 3(E) of the regulation, the basic illustration and any supplemental illustrations used in the sale and the producer's and applicant's signed statements with respect to financing and replacement in its home or regional office for at least five years after the termination or expiration of the proposed policy or contract
  - (7) Records required to be retained by the regulation may be maintained in paper, photograph, microprocess, magnetic, mechanical or electronic media or by any process which accurately reproduces the actual document.

## 2. Duties of Replacing Insurers that Use Producers [Section 6].

- a. Where a replacement is involved in the transaction, the replacing insurer shall:
- (1) Verify that the required forms are received and are in compliance with the regulation;
  - (2) Notify any other existing insurer that may be affected by the proposed replacement within five business days of receipt of a completed application indicating replacement or when the replacement is identified if not indicated on the application, and mail a copy of the available *illustration or policy summary* for the proposed policy or available disclosure document for the proposed contract within five business days of a request from an existing insurer; [*note: this illustration and policy summary requirement does not apply to variable contracts.*]
  - (3) Be able to produce copies of the notification regarding replacement required in Section 4(B), *indexed by producer, in its home or regional office* for at least five years or until the next regular examination by the insurance department of a company's state of domicile, whichever is later; and
  - (4) Provide to the policy or contract owner notice of the right to return the policy or contract within thirty (30) days of the delivery of the contract and receive an unconditional full refund of all premiums or considerations paid on it, including any policy fees or charges or, in the case of a *variable or market value adjustment policy or contract*, a payment of the cash surrender value provided under the policy or contract plus the fees and other charges deducted from the gross premiums or considerations or imposed under such policy or contract.
- b. In transactions where the replacing insurer and the existing insurer are the same or subsidiaries or affiliates under common ownership or control [*internal replacements*] allow credit for the period of time that has elapsed under the replaced policy's or contract's incontestability and suicide period up to the face amount of the existing policy or contract. With regard to *financed purchases* the credit may be limited to the amount the face amount of the existing policy is reduced by the use of existing policy values to fund the new policy or contract.

c. If an insurer *prohibits the use of sales material other than that approved by the company*, as an alternative to the requirements of Section 3(E) the insurer may:

- (1) Require with each application a statement *signed by the producer* that:
  - Represents that the producer used only company approved sales material;
  - *Lists*, by identifying number or other descriptive language, the *sales material that was used*; and
  - States that copies of all sales material were left with the applicant in accordance with Section 3(D); and
- Within ten days of the issuance of the policy or contract:
  - (a) Notify the applicant by sending a letter or by verbal communication with the applicant *by a person whose duties are **separate from the marketing area** of the insurer*, that the producer has represented that copies of all sales material have been left with the applicant in accordance with Section 3(D);
  - (b) Provide the applicant with a *toll free number* to contact *company personnel involved in the compliance function* if such is not the case; and
  - (c) Stress the importance of retaining copies of the sales material for future reference; and
- Keep a copy of the letter or other verification in the policy file at the home or regional office for at least five years after the termination or expiration of the policy or contract.

### 3. Duties of the Existing Insurer [Section 6].

a. Where a replacement is involved in the transaction, the existing insurer shall:

(1) Upon notice that its existing policy or contract may be replaced or a policy may be part of a financed purchase, *retain copies* of the notification in its home or regional office, *indexed by replacing insurer*, notifying it of the

replacement for at least five years or until the conclusion of the next regular examination conducted by the Insurance Department of its state of domicile, whichever is later.

(2) Send a letter to the policy or contract owner of the right to receive information regarding the existing policy or contract values including, if available, an in force illustration or policy summary if an in force illustration cannot be produced within five business days of receipt of a notice that an existing policy or contract is being replaced. The information shall be provided within five business days of receipt of the request from the policy or contract owner.

(3) Upon receipt of a request to borrow, surrender or withdraw any policy or contract values, send to the applicant a notice, advising the policy or contract owner of the effect release of policy or contract values will have on the non-guaranteed elements, face amount or surrender value of the policy or contract from which the values are released. The notice shall be sent separate from the check if the check is sent to anyone other than the policy or contract owner. In the case of *consecutive automatic premium loans or systematic withdrawals* from a contract, the insurer is only required to send the notice at the time of the first loan or withdrawal.

#### 4. Duties of Producers [Section 4].

- a. A producer who initiates an application must submit to the insurer, with or as part of the application, a statement signed by both the applicant and the producer as to whether the applicant has existing policies or contracts. If the answer is "no," the producer's duties with respect to replacement are complete.
- b. If the applicant answered "yes" to the question regarding existing coverage referred to in Subsection (A), the producer shall present and read to the applicant, not later than at the time of taking the application, a notice regarding replacements in the form as described in Attachment 1 to the regulation or other substantially similar form approved by the commissioner. *The notice shall be signed by both the applicant and the producer* attesting that the notice has been read aloud by the producer or that the applicant did not wish the notice to be read aloud (in which case the producer need not have read the notice aloud) and left with the applicant.
- c. The notice shall list all life insurance policies or annuities

proposed to be replaced, properly identified by name of insurer, the insured or annuitant, and policy or contract number if available; and shall include a statement as to whether each policy or contract will be replaced or whether a policy will be used as a source of financing for the new policy or contract. If a policy or contract number has not been issued by the existing insurer, alternative identification, such as an application or receipt number, shall be listed.

- d. In connection with a replacement transaction *the producer shall leave with the applicant* at the time an application for a new policy or contract is completed *the original or a copy of all sales material*. With respect to electronically presented sales material, it shall be provided to the policyholder in printed form no later than at the time of policy or contract delivery.
- e. Except as provided in Section 5(C) of the regulation, in connection with a replacement transaction the producer shall submit to the insurer to which an application for a policy or contract is presented, a copy of each document required by this section, *a statement identifying any preprinted or electronically presented company approved sales materials used, and copies of any individualized sales materials, including any illustrations used in the transaction*

#### H. Selected Definitions

- 1. Section 2(D) defines the term *financed purchase* as “the purchase of a new policy involving the actual or intended use of funds obtained by the withdrawal or surrender of, or by borrowing from values of an existing policy to pay all or part of any premium due on the new policy.”
  - a. If a withdrawal, surrender, or borrowing involving the policy values of an existing policy are used to pay premiums on a new policy owned by the same policyholder *within thirteen months before or after the effective date of the new policy* and is known by the replacing insurer, or if the withdrawal, surrender, or borrowing is shown on any illustration of the existing and new policies made available to the prospective policyowner by the insurer or its producers, it will be *deemed prima facie evidence of a financed purchase*.
- 2. Section 2(I) defines the term registered contract as “a variable annuity contract or variable life insurance policy subject to the prospectus delivery requirements of the Securities Act of 1933.”

I. Several aspects of the amended NAIC model regulation parallel SEC and FINRA positions concerning Section 1035 exchanges and bonus annuity sales.

1. Selected list of parallel regulatory concepts

- a. FINRA Guideline on Variable Life Insurance Distribution: NASD NTM 00-44 (June 2000).
- b. FINRA Guidelines on Supervisory Responsibilities: NASD NTM 99-45 (June 1999).
- c. FINRA Statement on Variable Annuity Distribution: NASD NTM 99-35 (May 1999).
- d. SEC Office of Compliance Inspections and Examinations: Indicators of “Good” Internal Controls in Variable Contract Distribution.

(1) A compilation of the SEC’s indicators drawn from speeches and seminar comments is discussed in Wilkerson, *Variable Product Distribution: A Continuing Study of Compliance Examinations, Inspections Sweeps and Evolving Regulatory Standards*, ACLI Compliance Section Annual Meeting (July 19, 2000) at 20.

e. SEC Examination of Variable Annuity “Bonus” Programs

(1) Several of the items requested in the SEC’s inspection letter requested documents and information that the amended NAIC Model Replacement Regulation also addresses.

(a) Scope of documents requested in the SEC’s examinations was outlined in *Variable Product Distribution: A Continuing Study of Compliance Examinations, Inspections Sweeps and Evolving Regulatory Standards*, ACLI Compliance Section Annual Meeting (July 19, 2000) at 6.

a. FINRA and SEC inspection sweeps focusing on “Section 1035 exchanges” of variable contracts and “life financing” arrangements (1998 and 1996.)

(1) These sweeps and the documentation they elicited were discussed in *Variable Product Distribution: A Continuing Study of Compliance Examinations, Inspections Sweeps and Evolving Regulatory Standards*, ACLI Compliance Section Annual Meeting (July 19, 2000) at 11 and 15.

J. NAIC Model Replacement Regulation: State-by-State Chart

1. A chart listing the status of the NAIC Model Replacement Regulation under state insurance law appears in the pages following Attachment 1 and 2 below.

**[This space left intentionally blank-NAIC Replacement Disclosure Examples  
Follow on Next Page]**

## Attachment 1 to Outline

### IMPORTANT NOTICE: REPLACEMENT OF LIFE INSURANCE OR ANNUITIES

*This document must be signed by the applicant and the producer, if there is one, and a copy left with the applicant.*

You are contemplating the purchase of a life insurance policy or annuity contract. In some cases this purchase may involve discontinuing or changing an existing policy or contract. If so, a replacement is occurring. Financed purchases are also considered replacements.

A replacement occurs when a new policy or contract is purchased and, in connection with the sale, you discontinue making premium payments on the existing policy or contract, or an existing policy or contract is surrendered, forfeited, assigned to the replacing insurer, or otherwise terminated or used in a financed purchase.

A financed purchase occurs when the purchase of a new life insurance policy involves the use of funds obtained by the withdrawal or surrender of or by borrowing some or all of the policy values, including accumulated dividends, of an existing policy, to pay all or part of any premium or payment due on the new policy. A financed purchase is a replacement.

You should carefully consider whether a replacement is in your best interests. You will pay acquisition costs and there may be surrender costs deducted from your policy or contract. You may be able to make changes to your existing policy or contract to meet your insurance needs at less cost. A financed purchase will reduce the value of your existing policy or contract and may reduce the amount paid upon the death of the insured.

We want you to understand the effects of replacements before you make your purchase decision and ask that you answer the following questions and consider the questions on the back of this form.

1. Are you considering discontinuing making premium payments, surrendering, forfeiting, assigning to the insurer, or otherwise terminating your existing policy or contract? \_\_\_  
YES \_\_\_ NO

2. Are you considering using funds from your existing policies or contracts to pay premiums due on the new policy or contract? \_\_\_ YES \_\_\_ NO

If you answered "yes" to either of the above questions, list each existing policy or contract you are contemplating replacing (include the name of the insurer, the insured, and the contract number if available) and whether each policy will be replaced or used as a source of financing:

**INSURER NAME****CONTRACT OR POLICY#****INSURED OR ANNUITANT: REPLACED (R) OR FINANCING (F)**

1.

2.

3.

Make sure you know the facts. Contact your existing company or its agent for information about the old policy or contract. [If you request one, an in force illustration, policy summary or available disclosure documents must be sent to you by the existing insurer.] Ask for and retain all sales material used by the agent in the sales presentation. Be sure that you are making an informed decision.

The existing policy or contract is being replaced because \_\_\_\_\_

\_\_\_\_\_.

I certify that the responses herein are, to the best of my knowledge, accurate:

\_\_\_\_\_

Applicant's Signature and Printed Name

Date

\_\_\_\_\_

\_\_\_\_\_

Producer's Signature and Printed Name

Date

\_\_\_\_\_

\_\_\_\_\_

I do not want this notice read aloud to me. \_\_\_\_\_ (Applicants must initial only if they do not want the notice read aloud.)

A replacement may not be in your best interest, or your decision could be a good one. You should make a careful comparison of the costs and benefits of your existing policy or contract and the proposed policy or contract. One way to do this is to ask the company or agent that sold you your existing policy or contract to provide you with information concerning your existing policy or contract. This may include an illustration of how your existing policy or contract is working now and how it would perform in the future based on certain assumptions. Illustrations should not, however, be used as a sole basis to compare policies or contracts. You should discuss the following with your agent to determine whether replacement or financing your purchase makes sense:

**PREMIUMS:** Are they affordable?  
 Could they change?  
 You're older--are premiums higher for the proposed new policy?  
 How long will you have to pay premiums on the new policy? On the old policy?

**POLICY VALUES:** New policies usually take longer to build cash values and to pay dividends.  
 Acquisition costs for the old policy may have been paid, you will incur costs for the new one.  
 What surrender charges do the policies have?  
 What expense and sales charges will you pay on the new policy?  
 Does the new policy provide more insurance coverage?

**INSURABILITY:** If your health has changed since you bought your old policy, the new one could cost you more, or you could be turned down.  
 You may need a medical exam for a new policy.  
 Claims on most new policies for up to the first two years can be denied based on inaccurate statements.  
 Suicide limitations may begin anew on the new coverage.

**IF YOU ARE KEEPING THE OLD POLICY AS WELL AS THE NEW POLICY:**

How are premiums for both policies being paid?  
 How will the premiums on your existing policy be affected?  
 Will a loan be deducted from death benefits?  
 What values from the old policy are being used to pay premiums?

**IF YOU ARE SURRENDERING AN ANNUITY OR INTEREST SENSITIVE LIFE PRODUCT;**

Will you pay surrender charges on your old contract?  
 What are the interest rate guarantees for the new contract?  
 Have you compared the contract charges or other policy expenses?

**OTHER ISSUES TO CONSIDER FOR ALL TRANSACTIONS:**

What are the tax consequences of buying the new policy?  
 Is this a tax free exchange? (See your tax advisor.)  
 Is there a benefit from favorable "grandfathered" treatment of the old policy under the federal tax code?

Will the existing insurer be willing to modify the old policy?  
How does the quality and financial stability of the new  
company compare with your existing company?

**(Attachment 2 to Replacement Outline)**

**NOTICE REGARDING REPLACEMENT  
REPLACING YOUR LIFE INSURANCE POLICY OR ANNUITY?**

Are you thinking about buying a new life insurance policy or annuity and discontinuing or changing an existing one? If you are, your decision could be a good one--or a mistake. You will not know for sure unless you make a careful comparison of your existing benefits and the proposed policy or contract's benefits.

Make sure you understand the facts. You should ask the company or agent that sold you your existing policy or contract to give you information about it.

Hear both sides before you decide. This way you can be sure you are making a decision that is in your best interest.

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## ACLI LAW SURVEY

# Replacement of Life Insurance and Annuities

### What's New?

Substantive changes in the survey are highlighted in **bold** and may reflect:

- Amendments to existing laws and regulations;
- New laws and regulations; or
- Expansion of the scope of the survey or additional information on the topic.

This multi-state survey identifies the states that have based their life and annuity replacement requirements on the NAIC's Life and Annuities Replacement Model Regulation. The compilation specifically includes a summary of exemptions and notes if states follow the NAIC model with respect to exemptions. The NAIC model was updated in 2006 to include an exemption for a term conversion privilege exercised among corporate affiliates. Over the last few years, many states have amended their provisions to include this exemption and are now noted on the survey as following the NAIC model.

Rather than summarizing other replacement requirements, the compilation provides citations to state law or regulations that correspond with several key elements of the NAIC model: definitions, duties of producers and insurers, and forms. Please refer to ACLI's *Law Survey: [Free Look](#)* for information on free look requirements for replacement policies.

ACLI hopes this compilation is helpful as a quick reference for your questions on life insurance replacement requirements. This survey does not constitute a legal opinion by ACLI staff. The *Law Surveys* are reviewed and updated annually. Users are encouraged to refer to the text of the statutes and regulations cited for the most current and complete information.

Note: No live web links are available in this survey.

**March 2010**  
American Council of Life Insurers  
202-624-2461

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Alabama</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">Ala. Admin. Code 482-1-133-.02</a></p> <p>Follows NAIC model</p>	<p>Definitions:  <a href="#">Ala. Admin. Code 482-1-133-.03</a></p> <p>Duties:</p> <p>Producers:  <a href="#">Ala. Admin. Code 482-1-133-.04</a></p> <p>All insurers using producers:  <a href="#">Ala. Admin. Code 482-1-133-.05</a></p> <p>Replacing insurers that use producers:  <a href="#">Ala. Admin. Code 482-1-133-.06</a></p> <p>Existing insurers:  <a href="#">Ala. Admin. Code 482-1-133-.07</a></p> <p>Direct response:  <a href="#">Ala. Admin. Code 482-1-133-.08</a></p> <p>Forms:                      Ala. Admin. Code 482-1-133-A, Appendix A; Appendix B; and Appendix C</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Alaska</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">Alaska Admin. Code tit. 3 § 26.790</a></p> <p>Follows NAIC model</p>	<p>Definitions:  <a href="#">Alaska Admin. Code tit. 3 § 26.819</a></p> <p>Duties:</p> <p>Producers:  <a href="#">Alaska Admin. Code tit. 3 § 26.795</a></p> <p>All insurers using producers:  <a href="#">Alaska Admin. Code tit. 3 § 26.800</a></p> <p>Replacing insurers that use producers:  <a href="#">Alaska Admin. Code tit. 3 § 26.805</a></p> <p>Existing insurers:  <a href="#">Alaska Admin. Code tit. 3 § 26.810</a></p> <p>Direct response:  <a href="#">Alaska Admin. Code tit. 3 § 26.815</a></p> <p>Forms:  <a href="#">Alaska Admin. Code tit. 3 § 26.795, Appendix A</a>  <a href="#">Alaska Admin. Code tit. 3 § 26.815, Appendix A, Appendix B</a></p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Arizona</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">Ariz. Rev. Stat. Ann. § 20-1241.01</a></p> <p>Follows NAIC model</p>	<p>Definitions:  <a href="#">Ariz. Rev. Stat. Ann. § 20-1241</a></p> <p>Duties:</p> <p>Producers:  <a href="#">Ariz. Rev. Stat. Ann. § 20-1241.03</a></p> <p>All insurers using producers:  <a href="#">Ariz. Rev. Stat. Ann. § 20-1241.04</a></p> <p>Replacing insurers:  <a href="#">Ariz. Rev. Stat. Ann. § 20-1241.05</a></p> <p>Existing insurers:  <a href="#">Ariz. Rev. Stat. Ann. § 20-1241.06</a></p> <p>Direct response:  <a href="#">Ariz. Rev. Stat. Ann. § 20-1241.07</a></p> <p>Forms:  <a href="#">Ariz. Admin. Code R20-6-212</a></p> <p>NAIC Replacement Model Appendix A, Appendix B, Appendix C adopted by reference.</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Arkansas</a></p>	<p><b>Applies to life insurance and annuities.</b></p> <p>Exemptions:</p> <p><a href="#">Arkansas Rule 97</a></p> <p><a href="#">AR Bulletin 14-83</a></p> <p><b>Follows NAIC Model</b></p>	<p>Definitions:</p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">Ark. Code Ann. § 23-66-307</a></p> <p><a href="#">AR Bulletin 6-89.</a></p> <p><b>All insurers using producers:</b></p> <p><a href="#">Arkansas Rule 97</a></p> <p><b>Replacing insurers:</b></p> <p><a href="#">Arkansas Rule 97</a></p> <p><b>Existing insurers:</b></p> <p><a href="#">Arkansas Rule 97</a></p> <p><b>Direct response:</b></p> <p><a href="#">Arkansas Rule 97</a></p> <p>Replacements that do not conform with <a href="#">Ark. Code Ann. § 23-66-307</a> are defined as "churning." <a href="#">Ark. Code Ann. § 23-66-206 (2)A.</a></p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">California</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <ul style="list-style-type: none"> <li>• <a href="#">Cal. Ins. Code § 10509.3</a></li> <li>• Credit life</li> <li>• Group life or group annuities</li> <li>• Application to the existing insurer that issued the existing life insurance when a contractual change or a conversion privilege is being exercised or when a term conversion privilege is exercised among corporate affiliates</li> <li>• Proposed life insurance that is to replace life insurance under a binding or conditional receipt issued by the same insurer</li> <li>• Transactions where the replacing insurer and the existing insurer are the same, with provisos</li> <li>• Registered contracts (exempt from some requirements with provisos)</li> </ul>	<p>Definitions:</p> <ul style="list-style-type: none"> <li>• <a href="#">Cal. Ins. Code § 10509.2</a></li> <li>• <a href="#">Cal. Ins. Code § 10509.3</a></li> </ul> <p>Duties:</p> <p>Producers:</p> <ul style="list-style-type: none"> <li>• <a href="#">Cal. Ins. Code § 10509.4</a></li> </ul> <p>Insurers:</p> <ul style="list-style-type: none"> <li>• <a href="#">Cal. Ins. Code § 10509.5</a></li> </ul> <p>All insurers using producers:</p> <ul style="list-style-type: none"> <li>• <a href="#">Cal. Ins. Code § 10509.6</a></li> </ul> <p>Direct response:</p> <ul style="list-style-type: none"> <li>• <a href="#">Cal. Ins. Code § 10509.7</a></li> </ul> <p>Forms:</p> <ul style="list-style-type: none"> <li>• <a href="#">Cal. Ins. Code § 10509.4 (d)</a></li> </ul>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Colorado</a></p> <p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">3 CO ADC INS 4-1-4</a> Section 3</p> <p><b>Follows NAIC model.</b></p>		<p>Definitions:  <a href="#">3 CO ADC INS 4-1-4</a> Section 4</p> <p>Duties:  <a href="#">3 CO ADC INS 4-1-4</a> Section 5</p> <p>Producers:            All insurers using producers:  <a href="#">3 CO ADC INS 4-1-4</a> Section 6</p> <p>Replacing insurers:  <a href="#">3 CO ADC INS 4-1-4</a> Section 7</p> <p>Existing insurers:  <a href="#">3 CO ADC INS 4-1-4</a> Section 8</p> <p>Direct response:  <a href="#">3 CO ADC INS 4-1-4</a> Section 9</p> <p>Forms:  <a href="#">3 CO ADC INS 4-1-4</a> Appendix A; Appendix B; and Appendix C</p>
<p><a href="#">Connecticut</a></p>		<p><a href="#">Conn. Gen. Stat. s. 38a-435</a> authorizes insurance commissioner to make regulations governing replacement of life insurance and annuities. No regulations to date.</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Delaware</a></p> <p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <ul style="list-style-type: none"> <li>• <a href="#">Del. Admin. Code 18 1200 1204</a>, Section 4.0</li> <li>• Credit life</li> <li>• Group life or group annuities</li> <li>• An application to the existing insurer that issued the existing life insurance and a contractual change or conversion privilege is being exercised</li> <li>• Transactions where the replacing insurer and the existing insurer are the same, or are subsidiaries or affiliates under common ownership or control.</li> <li>• Registered contracts (exempt from some requirements with provisos)</li> <li>• Life insurance or annuity products issued in connection with a pension, profit-sharing or other benefit plan qualifying for tax deductibility of premiums (with provisos)</li> </ul>	<p>Definitions:</p> <p><a href="#">Del. Admin. Code 18 1200 1204</a>, Section 2.0 (replacement);</p> <p><a href="#">Del. Admin. Code 18 1200 1204</a>, Section 3.0 (other)</p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">Del. Admin. Code 18 1200 1204</a>, Section 5.0</p> <p>All insurers:</p> <p><a href="#">Del. Admin. Code 18 1200 1204</a>, Section 6.0</p> <p>All insurers using producers:</p> <p><a href="#">Del. Admin. Code 18 1200 1204</a>, Section 7.0</p> <p>Direct response:</p> <p><a href="#">Del. Admin. Code 18 1200 1204</a>, Section 8.0</p> <p>Forms:</p> <p><a href="#">Del. Admin. Code 18 1200 1204</a>, Exhibit A</p> <p>No applicable provisions.</p>	<p><a href="#">District of Columbia</a></p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Florida</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions (from some requirements):</p> <p><a href="#">69 Fla. Admin. Code Ann. 69B-151.004</a> and <a href="#">69 Fla. Admin. Code Ann. 69O-151.004</a></p> <ul style="list-style-type: none"> <li>• Industrial insurance</li> <li>• Group, franchise, and individual credit life</li> <li>• Group life insurance and life insurance policies issued in connection with a pension, profit sharing or other benefit plan qualifying for tax deductibility of premiums</li> <li>• An application to the existing insurer that issued the existing life insurance where a contractual change or conversion privilege is being exercised</li> <li>• Existing life insurance that is a non-convertible term life insurance policy which will expire in five years or less and cannot be renewed, unless such policy has tabular cash values</li> <li>• Proposed life insurance that is to replace existing life insurance issued under a binding or conditional receipt delivered by the same company</li> <li>• Variable life insurance or annuities under which the death benefits and cash values vary in accordance with unit values of investments held in a separate account</li> </ul>	<p>Definitions:</p> <p><a href="#">69 Fla. Admin. Code Ann. 69B-151.002</a></p> <p><a href="#">69 Fla. Admin. Code Ann. 69O-151.002</a> (replacement);</p> <p><a href="#">69 Fla. Admin. Code Ann. 69B-151.003</a></p> <p><a href="#">69 Fla. Admin. Code Ann. 69O-151.003</a> (other)</p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">69 Fla. Admin. Code Ann. 69B-151.005</a></p> <p><a href="#">69 Fla. Admin. Code Ann. 69O-151.005</a> (agent);</p> <p><a href="#">69 Fla. Admin. Code Ann. 69B-151.006</a></p> <p><a href="#">69 Fla. Admin. Code Ann. 69O-151.006</a> (replacing agent)</p> <p>Replacing insurers:</p> <p><a href="#">69 Fla. Admin. Code Ann. 69O-151.007</a></p> <p>Existing insurers:</p> <p><a href="#">69 Fla. Admin. Code Ann. 69O-151.008</a></p> <p>Forms:</p> <p><a href="#">69 Fla. Admin. Code 69B-151.010</a></p> <p><a href="#">69 Fla. Admin. Code 69O-151.004</a></p> <p><b>OIR-B2-312</b> "Notice to Applicant Regarding Replacement of Life Insurance" given in Exhibit A and <b>OIR-B2-313</b> "Comparative Information Form" given in Exhibit B,</p> <p>Also, for information on churning, see:</p> <p><a href="#">Fla. Stat. Ann. § 626.9541</a> (1)(aa);</p> <p><a href="#">Fla. Stat. Ann. § 627.573</a>;</p> <p><a href="#">69 Fla. Admin. Code Ann. 69B-151.201</a> et seq.; includes Form <b>OIR-DO-1180</b> "Policy Disclosure Form and Instructions."</p>

State	Applicability and Exemptions	Key Elements/Citations
<a href="#">Georgia</a>	<p>Applies to life insurance and annuities replacing existing life insurance.</p> <p>Exemptions:</p> <ul style="list-style-type: none"> <li><a href="#">Ga. Comp. R. &amp; Regs. 120-2-24-.04</a></li> <li>• Replacement of annuity contracts</li> <li>• Credit life</li> <li>• Group life</li> <li>• Life insurance issued in connection with a pension, profit-sharing or other benefit plan qualifying for tax deductibility of premiums, with provisos</li> </ul>	<p>Definitions:  <a href="#">Ga. Comp. R. &amp; Regs. 120-2-24-.03</a></p> <p>Duties:</p> <p>Producers:  <a href="#">Ga. Comp. R. &amp; Regs. 120-2-24-.05</a> (agent)</p> <p>All insurers:  <a href="#">Ga. Comp. R. &amp; Regs. 120-2-24-.06</a></p> <p>All insurers using producers (agents):  <a href="#">Ga. Comp. R. &amp; Regs. 120-2-24-.07</a></p> <p>Direct response:  <a href="#">Ga. Comp. R. &amp; Regs. 120-2-24-.08</a></p> <p>Forms:  <a href="#">Ga. Comp. R. &amp; Regs. 120-2-24-.05</a>, Exhibit A  <a href="#">Ga. Comp. R. &amp; Regs. 120-2-24-.08</a>, Exhibit A</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Hawaii</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">Haw. Rev. Stat. § 431:10D-501</a>  <b>Haw. Admin. Rules § 16-3-3 Repealed. Effective March 9, 2009.</b>                      Follows NAIC model</p>	<p>Definitions:  <a href="#">Haw. Rev. Stat. § 431:10D-502</a>  <b>Haw. Admin. Rules § 16-3-2 Repealed. Effective March 9, 2009.</b></p> <p>Duties:                      Producers:  <a href="#">Haw. Rev. Stat. § 431:10D-503</a>  <b>Haw. Admin. Rules § 16-3-5 Repealed. Effective March 9, 2009.</b></p> <p>All insurers:  <b>Haw. Admin. Rules § 16-3-6 Repealed. Effective March 9, 2009.</b></p> <p>All insurers using producers:  <a href="#">Haw. Rev. Stat. § 431:10D-504</a></p> <p>Replacing insurers:  <a href="#">Haw. Rev. Stat. § 431:10D-505</a></p> <p>Existing insurers:  <a href="#">Haw. Rev. Stat. § 431:10D-506</a></p> <p>Direct response:  <a href="#">Haw. Rev. Stat. § 431:10D-507</a></p> <p>Forms:  <b>Haw. Admin. Rules § 16-3-7 Repealed. Effective March 9, 2009.</b></p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Idaho</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <p><a href="#">Idaho Admin. Code 18.01.41.011</a></p> <ul style="list-style-type: none"> <li>• Credit life</li> <li>• Group life or group annuities</li> <li>• Existing insurer--An application to the insurer that issued the existing life insurance and a contractual change or conversion privilege being exercised</li> <li>• Binding or conditional receipt issued by same company--proposed life insurance that is to replace life insurance under a binding or conditional receipt issued by the same company</li> <li>• Common ownership or control--transactions where the replacing insurer and the existing insurer are the same, or are subsidiaries or affiliates under common ownership or control, with provisos</li> </ul>	<p>Definitions:</p> <p><a href="#">Idaho Admin. Code 18.01.41.004</a> (replacement),  <a href="#">Idaho Admin. Code 18.01.41.005</a> (other)</p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">Idaho Admin. Code 18.01.41.012</a></p> <p>All insurers:</p> <p><a href="#">Idaho Admin. Code 18.01.41.013</a></p> <p>All insurers using producers:</p> <p><a href="#">Idaho Admin. Code 18.01.41.014</a></p> <p>Direct response:</p> <p><a href="#">Idaho Admin. Code 18.01.41.015</a></p> <p>Forms:</p> <p><a href="#">Idaho Admin. Code 18.01.41.016</a>, Exhibit A</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Illinois</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <ul style="list-style-type: none"> <li>• <a href="#">Ill. Admin. Code tit. 50 § 917.50</a></li> <li>• Credit life</li> <li>• Group life and group annuities</li> <li>• Life insurance policies issued in connection with a pension, profit-sharing or other benefit plan qualifying for the tax deductibility of premiums</li> <li>• Registered contracts except that the appropriate prospectus or offering circular shall be given to the applicant</li> <li>• Existing life insurance that is a non-convertible term life insurance policy which will expire in five years or less and cannot be renewed</li> <li>• Transactions where the replacing insurer and the existing insurer are the same or are subsidiaries under common ownership or control, with provisos</li> <li>• The total cash surrender value of all existing policies which would be affected by the replacement is less than \$500 and the sum of their face amounts is less than \$5,000</li> </ul>	<p>Definitions:</p> <p><a href="#">Ill. Admin. Code tit. 50 § 917.30</a> (replacement); <a href="#">Ill. Admin. Code tit. 50 § 917.40</a> (other)</p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">Ill. Admin. Code tit. 50 § 917.60</a></p> <p>Replacing insurers:</p> <p><a href="#">Ill. Admin. Code tit. 50 § 917.70</a></p> <p>Direct response:</p> <p><a href="#">Ill. Admin. Code tit. 50 § 917.80</a></p> <p>Forms:</p> <p>Ill. Admin. Code tit. 50 § 917, Exhibit A; Exhibit B; Exhibit C (direct response); Exhibit D (comparative information)</p>

State	Applicability and Exemptions	Key Elements/Citations
<a href="#">Indiana</a>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <p><a href="#">760 Ind. Admin. Code 1-16.1-4</a></p> <ul style="list-style-type: none"> <li>• Individual and group credit life</li> <li>• Group life and life policies issued in connection with a pension, profit-sharing or other benefit plan qualifying for tax deductibility of premiums, with provisos</li> <li>• An existing life insurance policy in which a contractual change or conversion privilege is being exercised</li> </ul>	<p>Definitions:</p> <p><a href="#">760 Ind. Admin. Code 1-16.1-2</a> (replacement); <a href="#">760 Ind. Admin. Code 1-16.1-3</a> (other)</p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">760 Ind. Admin. Code 1-16.1-5</a></p> <p>Replacing insurers:</p> <p><a href="#">760 Ind. Admin. Code 1-16.1-6</a></p> <p>Existing insurers:</p> <p><a href="#">760 Ind. Admin. Code 1-16.1-8</a></p> <p>Direct response:</p> <p><a href="#">760 Ind. Admin. Code 1-16.1-7</a></p> <p>Forms:</p> <p><a href="#">760 Ind. Admin. Code 1-16.1-12.5</a>, Exhibit A</p> <p><a href="#">760 Ind. Admin. Code 1-16.1-13.5</a>, Exhibit B (direct response)</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Iowa</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">Iowa Admin. Code 191—16.23(507B)</a></p> <p>Follows NAIC model but does not include exemption for term conversion privilege exercised among corporate affiliates.</p>	<p>Definitions:  <a href="#">Iowa Admin. Code 191—16.22(507B)</a></p> <p>Duties:  <a href="#">Iowa Admin. Code 191—16.24(507B)</a></p> <p>Producers:  <a href="#">Iowa Admin. Code 191—16.24(507B)</a>                      All insurers using producers:  <a href="#">Iowa Admin. Code 191—16.25(507B)</a></p> <p>Replacing insurers:  <a href="#">Iowa Admin. Code 191—16.26(507B)</a></p> <p>Existing insurers:  <a href="#">Iowa Admin. Code 191—16.27(507B)</a></p> <p>Direct response:  <a href="#">Iowa Admin. Code 191—16.28(507B)</a></p> <p>Forms:                      Iowa Admin. Code 191—16, Appendix A; Appendix B; Appendix C</p>
<p><a href="#">Kansas</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">Kan. Admin. Regs. 40-2-12 (b)</a></p> <ul style="list-style-type: none"> <li>• Application for the new life insurance is made to the same insurer that issued the existing life insurance, and a contractual policy change or conversion privilege is being exercised</li> <li>• New life insurance is provided under: (A) group life; or (B) mass marketed group life</li> <li>• Existing life insurance is a non-convertible term policy with five years or less to expire and which cannot be renewed</li> <li>• Solicitation is made by direct mail with provisos</li> <li>• Policy is issued in connection with a pension, profit sharing, an individual retirement account, or other benefit plan qualifying for an income tax deduction of premiums</li> </ul>	<p>Definitions:  <a href="#">Kan. Admin. Regs. 40-2-12 (a)</a></p> <p>Duties:  <a href="#">Kan. Admin. Regs. 40-2-12 (c), (d), (h), (i), (j)</a></p> <p>Producers:  <a href="#">Kan. Admin. Regs. 40-2-12 (e)</a></p> <p>All insurers:  <a href="#">Kan. Admin. Regs. 40-2-12 (f)</a></p> <p>Replacing insurers:  <a href="#">Kan. Admin. Regs. 40-2-12 (g)</a></p> <p>Forms:  <a href="#">Kan. Admin. Regs. 40-2-12 (g)</a>, Exhibit A (different insurer); Exhibit B (same insurer); Exhibit C</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Kentucky</a></p>	<p>Applies to life insurance.</p> <p>Exemptions:  <a href="#">Ky. Rev. Stat. Ann. § 304.12-030</a> (3)</p> <p>Follows NAIC model but does not include exemption for term conversion privilege exercised among corporate affiliates.</p>	<p>Definitions:  <a href="#">Ky. Rev. Stat. Ann. § 304.12-030</a> (1)  <a href="#">806 Ky. Admin. Regs. 12:080</a>, Section 1</p> <p>Duties:            Producers:  <a href="#">806 Ky. Admin. Regs. 12:080</a>, Section 3</p> <p>All insurers using producers:  <a href="#">806 Ky. Admin. Regs. 12:080</a>, Section 4</p> <p>Replacing insurers:  <a href="#">806 Ky. Admin. Regs. 12:080</a>, Section 5</p> <p>Existing insurers:  <a href="#">806 Ky. Admin. Regs. 12:080</a>, Section 6</p> <p>Direct response:  <a href="#">806 Ky. Admin. Regs. 12:080</a>, Section 7</p> <p>Forms:  <a href="#">806 Ky. Admin. Regs. 12:080</a>, Section 9, Office Forms A, B, and C (referenced);  <a href="#">KY Bulletin 83-DM-004</a></p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Louisiana</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">La. Admin. Code 37:XIII.8905</a> (Reg. 70)</p> <p>Follows NAIC model but also includes exemption for insurer marketing under the Home Service Marketing Distribution System and does not include exemption for term conversion privilege exercised among corporate affiliates.</p>	<p>Definitions:  <a href="#">La. Admin. Code 37:XIII.8903</a> (Reg. 70)</p> <p>Duties:  <a href="#">La. Admin. Code 37:XIII.8907</a> (Reg. 70)</p> <p>Producers:  <a href="#">La. Admin. Code 37:XIII.8909</a> (Reg. 70)</p> <p>Replacing insurers:  <a href="#">La. Admin. Code 37:XIII.8911</a> (Reg. 70)</p> <p>Existing insurers:  <a href="#">La. Admin. Code 37:XIII.8913</a> (Reg. 70)</p> <p>Direct response:  <a href="#">La. Admin. Code 37:XIII.8915</a> (Reg. 70)</p> <p>Forms:  <a href="#">La. Admin. Code 37:XIII.8921</a> (Reg. 70), Appendix A  <a href="#">La. Admin. Code 37:XIII.8923</a> (Reg. 70), Appendix B  <a href="#">La. Admin. Code 37:XIII.8925</a> (Reg. 70), Appendix C</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Maine</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">Code Me. R. 02-031 Ch. 919 § 1</a></p> <p>Follows NAIC model but does not include exemption for term conversion privilege exercised among corporate affiliates.</p>	<p>Definitions:  <a href="#">Code Me. R. 02-031 Ch. 919 § 2</a></p> <p>Duties:</p> <p>Producers:  <a href="#">Code Me. R. 02-031 Ch. 919 § 3</a></p> <p>Insurers using producers:  <a href="#">Code Me. R. 02-031 Ch. 919 § 4</a></p> <p>Replacing insurers:  <a href="#">Code Me. R. 02-031 Ch. 919 § 5</a></p> <p>Existing insurers:  <a href="#">Code Me. R. 02-031 Ch. 919 § 6</a></p> <p>Direct response:  <a href="#">Code Me. R. 02-031 Ch. 919 § 7</a></p> <p>Forms:  <a href="#">Code Me. R. 02-031 Ch. 919 Appendix A</a>; Appendix B (direct response); Appendix C (direct response)</p>

State	Applicability and Exemptions	Key Elements/ Citations
<a href="#">Maryland</a>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">Md. Regs. Code 31.09.05.02</a></p> <p>Follows NAIC model</p>	<p>Definitions:  <a href="#">Md. Regs. Code 31.09.05.03</a></p> <p>Duties:</p> <p>Producers:  <a href="#">Md. Regs. Code 31.09.05.04</a></p> <p>All insurers using producers:  <a href="#">Md. Regs. Code 31.09.05.05</a></p> <p>Replacing insurers:  <a href="#">Md. Regs. Code 31.09.05.06</a></p> <p>Existing insurers:  <a href="#">Md. Regs. Code 31.09.05.07</a></p> <p>Direct response:  <a href="#">Md. Regs. Code 31.09.05.08</a></p> <p>Forms:  <a href="#">Md. Regs. Code 31.09.05.10</a>, Replacement Form A;  <a href="#">Md. Regs. Code 31.09.05.11</a>, Replacement Form B;  <a href="#">Md. Regs. Code 31.09.05.12</a>, Replacement Form C</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Massachusetts</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <p><a href="#">211 CMR 34.03</a></p> <ul style="list-style-type: none"> <li>• Credit life</li> <li>• Group life and group annuities</li> <li>• Proposed life insurance that is to replace life insurance under a binding or conditional receipt issued by the same company</li> <li>• Internal replacements where the replacing insurer and the existing insurer are the same, or are subsidiaries or affiliates under common ownership or control</li> <li>• Non-contributory group life</li> <li>• Life insurance policies issued in connection with a pension, profit sharing or other benefit plan qualifying for tax deductibility of premiums</li> <li>• Registered contracts (exempt from some requirements with provisos)</li> </ul>	<p>Definitions:</p> <p><a href="#">211 CMR 34.02</a></p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">211 CMR 34.04</a></p> <p>All insurers:</p> <p><a href="#">211 CMR 34.05</a></p> <p>All insurers using producers:</p> <p><a href="#">211 CMR 34.06</a></p> <p>Direct response:</p> <p><a href="#">211 CMR 34.07</a></p> <p>Forms:</p> <p><a href="#">211 CMR 34.04</a></p>
<p><a href="#">Michigan</a></p>	<p>Applies to life insurance, excluding annuities in definition of life insurance.</p> <p>Exemptions:</p> <p><a href="#">Mich. Admin. Code 500.605</a></p> <ul style="list-style-type: none"> <li>• Application for the new life insurance made to the same insurer that issued the existing life insurance or to an affiliate of the existing insurer</li> <li>• New life insurance provided under any of the following plans with provisos: (a) group term life; (b) certain mass marketed policies; (c) life insurance policies issued in connection with a pension, profit sharing, or other benefit plan qualifying for tax-deductibility of premiums</li> <li>• Existing life insurance is a nonconvertible term policy which cannot be renewed and which would expire within five years after the initiation of the transaction</li> </ul>	<p>Definitions:</p> <p><a href="#">Mich. Admin. Code 500.601</a></p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">Mich. Admin. Code 500.602</a></p> <p>All insurers:</p> <p><a href="#">Mich. Admin. Code 500.603</a></p> <p>Replacing insurers:</p> <p><a href="#">Mich. Admin. Code 500.604</a></p> <p>Forms:</p> <p><a href="#">MI Bulletin 84-06</a></p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Minnesota</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <ul style="list-style-type: none"> <li>• <a href="#">Minn. Stat. Ann. § 61A.54</a></li> <li>• Credit life</li> <li>• Group life or group annuities</li> <li>• Application to the existing insurer that issued the existing life insurance or annuity, where a contractual change or a conversion privilege is being exercised</li> <li>• Proposed life insurance that is to replace life insurance under a binding or conditional receipt issued by the same company</li> <li>• Transactions where the replacing insurer and the existing insurer are the same, or are subsidiaries or affiliates under common ownership or control with provisos</li> </ul>	<p>Definitions: <a href="#">Minn. Stat. Ann. § 61A.53</a></p> <p>Duties:</p> <p>Producers: <a href="#">Minn. Stat. Ann. § 61A.55</a></p> <p>All insurers: <a href="#">Minn. Stat. Ann. § 61A.56</a></p> <p>All insurers using producers: <a href="#">Minn. Stat. Ann. § 61A.57</a></p> <p>Direct response: <a href="#">Minn. Stat. Ann. § 61A.58</a></p> <p>Forms: <a href="#">Minn. Stat. Ann. § 61A.60</a>, Subdivisions 1, 2, and 3</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Mississippi</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">MS ADC.INS 99-2</a> Section 1  <a href="#">Mississippi Regulation 99-2, effective January 19, 2010.</a></p> <p><b>Follows NAIC model</b></p>	<p>Definitions:  <a href="#">MS ADC.INS 99-2</a> Section 2</p> <p>Duties:                      Producers:  <a href="#">MS ADC.INS 99-2</a> Section 3</p> <p>All insurers using producers:  <a href="#">MS ADC.INS 99-2</a> Section 4</p> <p>Replacing insurers:  <a href="#">MS ADC.INS 99-2</a> Section 5</p> <p>Existing insurers:  <a href="#">MS ADC.INS 99-2</a> Section 6</p> <p>Direct response:  <a href="#">MS ADC.INS 99-2</a> Section 7</p> <p>Forms:  <a href="#">MS ADC.INS 99-2</a> Appendix A; Appendix B; and Appendix C</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><u>Missouri</u></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <ul style="list-style-type: none"> <li>• <a href="#">20 Mo. Code Regs. 400-5.400 (4)</a></li> <li>• Credit life</li> <li>• Group life or group annuities</li> <li>• Application to the existing insurer that issued the existing life insurance where a contractual change or conversion privilege is being exercised</li> <li>• Proposed life insurance that is to replace life insurance under a binding or conditional receipt issued by the same company</li> <li>• Transactions where the replacing insurer and the existing insurer are the same or are subsidiaries or affiliates under common ownership or control; with provisos</li> <li>• Policies issued in connection with a pension, profit sharing and individual retirement account or other benefit plan qualifying for tax deductibility of premium</li> <li>• Registered contracts (exempt from some requirements with provisos)</li> </ul>	<p>Definitions:  <a href="#">20 Mo. Code Regs. 400-5.400 (2)</a> and (3)</p> <p>Duties:</p> <p>Producers:  <a href="#">20 Mo. Code Regs. 400-5.400 (5)</a></p> <p>All insurers:  <a href="#">20 Mo. Code Regs. 400-5.400 (6)</a></p> <p>All insurers using producers:  <a href="#">20 Mo. Code Regs. 400-5.400 (7)</a></p> <p>Direct response:  <a href="#">20 Mo. Code Regs. 400-5.400 (8)</a></p> <p>Forms:  <a href="#">20 Mo. Code Regs. 400-5.400</a>, Exhibit A and Exhibit B</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Montana</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">Mont. Admin. R. 6.6.304</a></p> <p>Follows NAIC model but does not include exemption for group life insurance and annuities used to fund prearranged funeral contracts and does not include exemption for term conversion privilege exercised among corporate affiliates.</p>	<p>Definitions:  <a href="#">Mont. Admin. R. 6.6.303</a></p> <p>Duties:  <a href="#">Mont. Admin. R. 6.6.305</a></p> <p>Producers:  <a href="#">Mont. Admin. R. 6.6.311</a></p> <p>All insurers using producers:  <a href="#">Mont. Admin. R. 6.6.311</a></p> <p>Replacing insurers:  <a href="#">Mont. Admin. R. 6.6.306</a></p> <p>Existing insurers:  <a href="#">Mont. Admin. R. 6.6.308</a></p> <p>Direct response:  <a href="#">Mont. Admin. R. 6.6.307</a></p> <p>Forms:  <a href="#">Mont. Admin. R. 6.6.313</a>, NAIC model forms Appendix A; Appendix B; and Appendix C incorporated by reference</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Nebraska</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">210 Neb. Admin. Code Ch. 19 § 003</a></p> <p>Follows NAIC model</p>	<p>Definitions:  <a href="#">210 Neb. Admin. Code Ch. 19 § 004</a> (replacement);  <a href="#">210 Neb. Admin. Code Ch. 19 § 005</a> (other)</p> <p>Duties:</p> <p>Producers:  <a href="#">210 Neb. Admin. Code Ch. 19 § 006</a></p> <p>All insurers:  <a href="#">210 Neb. Admin. Code Ch. 19 § 007</a></p> <p>All insurers using producers:  <a href="#">210 Neb. Admin. Code Ch. 19 § 008</a></p> <p>Replacing insurers:  <a href="#">210 Neb. Admin. Code Ch. 19 § 009</a></p> <p>Existing insurers:  <a href="#">210 Neb. Admin. Code Ch. 19 § 010</a></p> <p>Direct response:  <a href="#">210 Neb. Admin. Code Ch. 19 § 011</a></p> <p>Forms:  <a href="#">210 Neb. Admin. Code Ch. 19 Exhibit A</a></p>

State	Applicability and Exemptions	Key Elements/ Citations
<p><a href="#">Nevada</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <p><a href="#">Nev. Admin. Code 686A.540</a></p> <ul style="list-style-type: none"> <li>• Individual credit life</li> <li>• Group life insurance, group credit life insurance or life insurance issued in connection with a pension, profit-sharing or other benefit plan that qualifies for tax deductibility of premiums</li> <li>• Variable life under which the death benefits and cash values vary in accordance with the unit values of investments held in a separate account</li> <li>• Application made to an insurer under an existing policy for a contractual change or the exercise of a privilege of conversion</li> <li>• Existing policy which is a nonconvertible, term policy, will expire in five years or less and cannot be renewed</li> <li>• Proposed life insurance which is to replace life insurance under a binding or conditional receipt issued by the same company</li> <li>• Policy solicited through direct response with a face value of \$5,000 or less</li> </ul>	<p>Definitions:</p> <p><a href="#">Nev. Admin. Code 686A.510</a></p> <p><a href="#">Nev. Admin. Code 686A.530</a></p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">Nev. Admin. Code 686A.550</a></p> <p><a href="#">Nev. Admin. Code 686A.567</a></p> <p>Replacing insurers:</p> <p><a href="#">Nev. Admin. Code 686A.555</a></p> <p><a href="#">Nev. Admin. Code Section 3 of R109-07</a></p> <p>Direct response:</p> <p><a href="#">Nev. Admin. Code 686A.560</a></p> <p>Forms:</p> <p><a href="#">Nev. Admin. Code 686A.563</a></p> <p><a href="#">Nev. Admin. Code Section 2 of R109-07 (annuities)</a></p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">New Hampshire</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">N.H. Code Admin. Ins 302.02</a></p> <p><b>Follows NAIC model</b></p>	<p>Definitions:  <a href="#">N.H. Code Admin. Ins. 302.03</a></p> <p>Duties:  <a href="#">N.H. Code Admin. Ins. 302.04</a></p> <p>Producers:  <a href="#">N.H. Code Admin. Ins. 302.04</a></p> <p>All insurers using producers:  <a href="#">N.H. Code Admin. Ins. 302.05</a></p> <p>Replacing insurers:  <a href="#">N.H. Code Admin. Ins. 302.06</a></p> <p>Existing insurers:  <a href="#">N.H. Code Admin. Ins. 302.07</a></p> <p>Direct response:  <a href="#">N.H. Code Admin. Ins. 302.08</a></p> <p>[In addition to model in New Hampshire, the following is prohibited: Recommending to a prospective purchaser the purchase or replacement of any life insurance policy or annuity contract without reasonable grounds to believe that the recommendation is suitable for the applicant on the basis of information furnished by such person. <a href="#">N.H. Code Admin. Ins. 301.06</a> (k)(3)]</p> <p>Forms:            N.H. Code Admin. Ins 302, Appendix A; Appendix B; and Appendix C</p>

State	Applicability and Exemptions	Key Elements/ Citations
<p><a href="#">New Jersey</a></p>	<p>Applies to life insurance.</p> <p>Exemptions:  <a href="#">N.J. Admin. Code § 11:4-2.1</a></p> <p>Follows NAIC model but does not specifically apply to policies or contracts used to fund any plan or arrangement that is funded solely by contributions an employee elects to make, whether on a pre-tax or after-tax basis, and where the insurer has been notified that plan participants may choose from among two or more insurers and there is a direct solicitation of an individual employee by an insurance producer for the purchase of a contract or policy.</p>	<p>Definitions:  <a href="#">N.J. Admin. Code § 11:4-2.2</a></p> <p>Duties:</p> <p>Producers:  <a href="#">N.J. Admin. Code § 11:4-2.3</a></p> <p>Insurers that use producers:  <a href="#">N.J. Admin. Code § 11:4-2.5</a></p> <p>Replacing insurers:  <a href="#">N.J. Admin. Code § 11:4-2.4</a></p> <p>Existing insurers:  <a href="#">N.J. Admin. Code § 11:4-2.6</a></p> <p>Direct response:  <a href="#">N.J. Admin. Code § 11:4-2.7</a></p> <p>Forms:            N.J. Admin. Code § 11:4-2 Appendix A; Appendix B; and Appendix C            (Also see <a href="#">NJ Bulletin 2005-02.</a>)</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">New Mexico</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <p><a href="#">N.M. Admin Code 13.9.6.2</a></p> <p>Follows NAIC model but does not include exemption for term conversion privilege exercised among corporate affiliates.</p>	<p>Definitions:</p> <p><a href="#">N.M. Admin Code 13.9.6.7</a></p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">N.M. Admin Code 13.9.6.8</a></p> <p>All insurers using producers:</p> <p><a href="#">N.M. Admin Code 13.9.6.9</a></p> <p>Replacing insurers using producers:</p> <p><a href="#">N.M. Admin Code 13.9.6.10</a></p> <p>Existing insurers:</p> <p><a href="#">N.M. Admin Code 13.9.6.11</a></p> <p>Direct response:</p> <p><a href="#">N.M. Admin Code 13.9.6.12</a></p> <p>Forms:</p> <p><a href="#">N.M. Admin Code 13.9.6.14</a>, Appendix A;</p> <p><a href="#">N.M. Admin Code 13.9.6.15</a>, Appendix B;</p> <p><a href="#">N.M. Admin Code 13.9.6.16</a>, Appendix C</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">New York</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <p><a href="#">11 NYCRR 51.3</a></p> <ul style="list-style-type: none"> <li>• The application for the new life insurance policy or new annuity contract is made to the same insurer that issued the existing life insurance policy or annuity contract and a contractual conversion privilege is being exercised</li> <li>• A policy change customarily granted by the insurer is being exercised, provided such change results in no additional surrender or expense charge or suicide or contestable restrictions, and only to the extent such change is approved by the Superintendent of Insurance</li> <li>• New coverage under certain group life policies or group annuities</li> <li>• Individual life or individual annuity whose cost is borne wholly by the applicant's employer or by an association of which the applicant is a member</li> <li>• Certain mass marketed individual life policies or individual annuity contracts</li> <li>• The existing life insurance is a nonrenewable, nonconvertible term policy with five years or less to its expiration date</li> </ul>	<p>Definitions: <a href="#">11 NYCRR 51.2</a></p> <p>Duties:</p> <p>Producers: <a href="#">11 NYCRR 51.5</a></p> <p>All insurers: <a href="#">11 NYCRR 51.6</a></p> <p>Replacing insurers: <a href="#">11 NYCRR 51.6</a></p> <p>Existing insurers: <a href="#">11 NYCRR 51.6</a></p> <p>Forms: <a href="#">11 NYCRR 51.8</a>, Appendix 10A (disclosure statement); Appendix 10B (annuity to annuity); Appendix 10C (notice); Appendix 11 (definition of replacement)</p>

State	Applicability and Exemptions	Key Elements/ Citations
<a href="#">North Carolina</a>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">11 NCAC 12.0604</a></p> <p>Follows NAIC model</p>	<p>Definitions:  <a href="#">11 NCAC 12.0602</a>  <a href="#">11 NCAC 12.0603</a></p> <p>Duties:</p> <p>Producers:  <a href="#">11 NCAC 12.0605</a></p> <p>Existing insurer:  <a href="#">11 NCAC 12.0606</a></p> <p>Insurers using producers:  <a href="#">11 NCAC 12.0607</a></p> <p>Replacing insurers using producers:  <a href="#">11 NCAC 12.0612</a></p> <p>Direct response:  <a href="#">11 NCAC 12.0608</a></p> <p>Forms:  <a href="#">11 NCAC 12.0611</a> (NAIC replacement notice by reference)</p>
<a href="#">North Dakota</a>		<p>No applicable provisions.</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Ohio</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">Ohio Admin. Code § 3901-6-05 (B)(2)</a></p> <p>Follows NAIC model</p>	<p>Definitions:  <a href="#">Ohio Admin. Code § 3901-6-05 (C)</a></p> <p>Duties:</p> <p>Producers:  <a href="#">Ohio Admin. Code § 3901-6-05 (D)</a></p> <p>Insurers using producers:  <a href="#">Ohio Admin. Code § 3901-6-05 (E)</a></p> <p>Replacing insurers using producers:  <a href="#">Ohio Admin. Code § 3901-6-05 (F)</a></p> <p>Existing insurer:  <a href="#">Ohio Admin. Code § 3901-6-05 (G)</a></p> <p>Direct response:  <a href="#">Ohio Admin. Code § 3901-6-05 (H)</a></p> <p>Forms:  <a href="#">Ohio Admin. Code § 3901-6-05 Appendix A</a>;  <a href="#">Appendix B</a>; <a href="#">Appendix C</a></p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Oklahoma</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <ul style="list-style-type: none"> <li>• <a href="#">36 Okla. Stat. Ann. § 4032</a></li> <li>• Credit life</li> <li>• Group life or group annuities</li> <li>• Contracts issued in connection with employee benefits or welfare plans as defined by ERISA</li> <li>• The exercise by an insured of an existing contractual right with the same insurer for the purchase of additional insurance under a guaranteed insurability provision or conversion option or any other contractual policy change privilege</li> <li>• Short-term nonrenewable life insurance policies written to cover periods of 31 days or less</li> <li>• An existing nonconvertible term life insurance policy which will expire in five years or less and which cannot be renewed</li> <li>• Proposed life insurance policy that is to replace life insurance under a binding or conditional receipt issued by the same company issuing the policy which is to be replaced</li> </ul>	<p>Definitions:</p> <p><a href="#">36 Okla. Stat. Ann. § 4033</a></p> <p><a href="#">36 Okla. Stat. Ann. § 4037</a></p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">36 Okla. Stat. Ann. § 4034</a></p> <p>All insurers:</p> <p><a href="#">36 Okla. Stat. Ann. § 4034</a></p> <p>Existing insurers:</p> <p><a href="#">36 Okla. Stat. Ann. § 4034</a></p> <p>Forms:</p> <p><a href="#">36 Okla. Stat. Ann. § 4035</a> (notice)</p> <p><a href="#">36 Okla. Stat. Ann. § 4036</a> (applicant's statement)</p> <p><a href="#">36 Okla. Stat. Ann. § 4037</a> (definitions)</p>

State	Applicability and Exemptions	Key Elements/ Citations
<p><a href="#">Oregon</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">Or. Admin. R. 836-080-0001</a> (4) and (5)</p> <p>Follows NAIC model</p> <ul style="list-style-type: none"> <li>Does not include exemption for group life insurance and annuities used to fund prearranged funeral contracts.</li> </ul>	<p>Definitions:  <a href="#">Or. Admin. R. 836-080-0005</a></p> <p>Duties:</p> <p>Producers:  <a href="#">Or. Admin. R. 836-080-0014</a></p> <p>All insurers using producers:  <a href="#">Or. Admin. R. 836-080-0022</a></p> <p>Replacing insurers:  <a href="#">Or. Admin. R. 836-080-0029</a></p> <p>Existing insurers:  <a href="#">Or. Admin. R. 836-080-0034</a></p> <p>Direct response:  <a href="#">Or. Admin. R. 836-080-0039</a></p> <p>Forms:  Or. Admin. R. 836-080, Appendix A; Appendix B; and Appendix C (available through insurance agency)</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Pennsylvania</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <ul style="list-style-type: none"> <li>• <a href="#">31 Pa. Code § 81.3</a></li> <li>• Group life policies issued to creditors</li> <li>• Credit life</li> <li>• Group life or group annuities</li> <li>• Application to the existing insurer that issued the existing life insurance and a contractual change or a conversion privilege is being exercised</li> <li>• Proposed life insurance that is to replace life insurance under a binding or conditional receipt issued by the same company</li> <li>• Transactions where the replacing insurer and the existing insurer are the same, or are subsidiaries or affiliates under common ownership or control with provisos</li> <li>• Registered contracts (exempt from some requirements with provisos)</li> </ul>	<p>Definitions:</p> <p><a href="#">31 Pa. Code § 81.2</a></p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">31 Pa. Code § 81.4</a></p> <p>All insurers:</p> <p><a href="#">40 Pa. Cons. Stat. Ann. § 625-9</a>;</p> <p><a href="#">31 Pa. Code § 81.5</a></p> <p>All insurers using producers:</p> <p><a href="#">31 Pa. Code § 81.6</a></p> <p>Direct response:</p> <p><a href="#">31 Pa. Code § 81.7</a></p> <p>Forms:</p> <p>31 Pa. Code Chapter 81, Appendix A and Appendix B</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Rhode Island</a></p>	<p>Applies to life insurance.</p> <p>Exemptions:  <a href="#">R. I. Code R. 02 030 029</a> Section 2</p> <p>Follows NAIC model</p>	<p>Definitions:  <a href="#">R. I. Code R. 02 030 029</a> Section 3</p> <p>Duties:</p> <p>Producers:  <a href="#">R. I. Code R. 02 030 029</a> Section 4</p> <p>All insurers using producers:  <a href="#">R. I. Code R. 02 030 029</a> Section 5</p> <p>Replacing insurers:  <a href="#">R. I. Code R. 02 030 029</a> Section 6</p> <p>Existing insurers:  <a href="#">R. I. Code R. 02 030 029</a> Section 7</p> <p>Direct response:  <a href="#">R. I. Code R. 02 030 029</a> Section 8</p> <p>Forms:  <a href="#">R. I. Code R. 02 030 029</a> Appendix A; Appendix B; and Appendix C</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">South Carolina</a></p> <p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">S. C. Code of Regulations R. 69-12.1, Section 1</a></p> <p><b>Follows NAIC Model</b></p>	<p>Definitions:  <a href="#">S. C. Code of Regulations R. 69-12.1, Section 2</a></p> <p>Duties:  <a href="#">S. C. Code of Regulations R. 69-12.1, Section 3</a></p> <p>Producers:  <a href="#">S. C. Code of Regulations R. 69-12.1, Section 4</a></p> <p>All insurers:  <a href="#">S. C. Code of Regulations R. 69-12.1, Section 4</a></p> <p>All insurers using producers:  <a href="#">S. C. Code of Regulations R. 69-12.1, Section 4</a></p> <p><b>Replacing insurers:</b>  <a href="#">S. C. Code of Regulations R. 69-12.1, Section 5</a></p> <p><b>Existing insurers:</b>  <a href="#">S. C. Code of Regulations R. 69-12.1, Section 6</a></p> <p>Direct response:  <a href="#">S. C. Code of Regulations R. 69-12.1, Section 7</a></p> <p>Forms:  <a href="#">S. C. Code of Regulations R. 69-12.1, Appendix A</a>; Appendix B; and Appendix C</p>	
<p><a href="#">South Dakota</a></p> <p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">S. D. Admin. 20:06:08:40</a></p> <ul style="list-style-type: none"> <li>• Credit life</li> <li>• Group life or group annuities</li> <li>• Application to the insurer that issued the existing life insurance or annuity exercising a contractual change or conversion privilege</li> <li>• Proposed life insurance that is to replace life insurance or annuity under a binding or conditional receipt issued by the same company</li> <li>• A term conversion privilege when exercised among corporate affiliates</li> </ul>	<p>Definitions:  <a href="#">S. D. Admin. 20:06:08:38</a></p> <p>Duties:  <a href="#">S. D. Admin. 20:06:08:39</a></p> <p>Producers:  <a href="#">S. D. Admin. 20:06:08:39</a></p> <p>Replacing insurers:  <a href="#">S. D. Admin. 20:06:08:39</a></p> <p>Forms:  <a href="#">S. D. Admin. 20:06:08:41</a> (describes contents of notice)</p>	

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Tennessee</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <ul style="list-style-type: none"> <li>• <a href="#">Tenn. Comp. R. &amp; Regs. 0780-01-24-02</a></li> <li>• Credit life</li> <li>• Group life insurance</li> <li>• Application to the existing insurer that issued the existing life insurance and a contractual change or a conversion privilege is being exercised</li> <li>• Proposed life insurance that is to replace life insurance under a binding or conditional receipt issued by the same company</li> <li>• Transactions where the replacing insurer and the existing insurer are the same, or are subsidiaries or affiliates under common ownership or control with provisos</li> <li>• Registered contracts (exempt from some requirements with provisos)</li> </ul>	<p>Definitions:</p> <p><a href="#">Tenn. Comp. R. &amp; Regs. 0780-01-24-.02</a> (replacement);</p> <p><a href="#">Tenn. Comp. R. &amp; Regs. 0780-01-24-.03</a> (other)</p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">Tenn. Comp. R. &amp; Regs. 0780-01-24-.05</a></p> <p>All insurers:</p> <p><a href="#">Tenn. Comp. R. &amp; Regs. 0780-01-24-.06</a></p> <p>All insurers using producers:</p> <p><a href="#">Tenn. Comp. R. &amp; Regs. 0780-01-24-.07</a></p> <p>Direct response:</p> <p><a href="#">Tenn. Comp. R. &amp; Regs. 0780-01-24-.08</a></p> <p>Forms:</p> <p><a href="#">Tenn. Comp. R. &amp; Regs. 0780-01-24, Exhibit A</a></p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Texas</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">Tex. Ins. Code Ann. § 1114.004</a></p> <p>Follows NAIC model</p>	<p>Definitions:  <a href="#">Tex. Ins. Code Ann. § 1114.002</a> (general)  <a href="#">Tex. Ins. Code Ann. § 1114.003</a> (policy summary)  <a href="#">28 Tex. Admin. Code § 3.9502</a> (agent and producer)</p> <p>Duties:            Producers:  <a href="#">Tex. Ins. Code Ann. § 1114.051</a></p> <p>All insurers using producers:  <a href="#">Tex. Ins. Code Ann. § 1114.052</a></p> <p>Replacing insurers that use producers:  <a href="#">Tex. Ins. Code Ann. § 1114.053</a>  <a href="#">28 Tex. Admin. Code § 3.9504</a></p> <p>Existing insurers:  <a href="#">Tex. Ins. Code Ann. § 1114.054</a></p> <p>Direct response:  <a href="#">Tex. Ins. Code Ann. § 1114.055</a></p> <p>Forms:  <a href="#">Tex. Ins. Code Ann. § 1114.006</a>  <a href="#">28 Tex. Admin. Code § 3.9503</a> (format)  <a href="#">28 Tex. Admin. Code § 3.9504</a> (replacement)  <a href="#">28 Tex. Admin. Code § 3.9505</a> (direct response)  <a href="#">28 Tex. Admin. Code § 3.9506</a> (substantially similar notices)</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Utah</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">Utah Admin. Code R590-93</a> section 2</p> <p>Follows NAIC model</p>	<p>Definitions:  <a href="#">Utah Admin. Code R590-93</a> section 3</p> <p>Duties:  <a href="#">Utah Admin. Code R590-93</a> section 4</p> <p>Producers:            All insurers using producers:  <a href="#">Utah Admin. Code R590-93</a> section 5</p> <p>Replacing insurers that use producers:  <a href="#">Utah Admin. Code R590-93</a> section 6</p> <p>Existing insurers:  <a href="#">Utah Admin. Code R590-93</a> section 7</p> <p>Direct response:  <a href="#">Utah Admin. Code R590-93</a> section 8</p> <p>Forms:  <a href="#">Utah Admin. Code R590-93</a> section 3, Appendix A; Appendix B; and Appendix C adopted by reference.</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Vermont</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">Vt. Code R. 21.020.010</a>, Sec. 1.B.</p> <p>Follows NAIC model but does not include exemption for term conversion privilege exercised among corporate affiliates.</p>	<p>Definitions:  <a href="#">Vt. Code R. 21.020.010</a>, Sec. 2</p> <p>Duties:</p> <p>Producers:  <a href="#">Vt. Code R. 21.020.010</a>, Sec. 3</p> <p>All insurers using producers:  <a href="#">Vt. Code R. 21.020.010</a>, Sec. 4</p> <p>Replacing insurers:  <a href="#">Vt. Code R. 21.020.010</a>, Sec. 5</p> <p>Existing insurers:  <a href="#">Vt. Code R. 21.020.010</a>, Sec. 6</p> <p>Direct response:  <a href="#">Vt. Code R. 21.020.010</a>, Sec. 7</p> <p>Forms:  <a href="#">Vt. Code R. 21.020.010</a>, Appendix A and Appendix C</p>

State	Applicability and Exemptions	Key Elements/ Citations
<a href="#">Virginia</a>	<p>Applies to life insurance and annuities used to replace existing life insurance.</p> <p>Exemptions:  <a href="#">14 Va. Admin. Code 5-30-30</a></p> <p>Follows NAIC model</p>	<p>Definitions:  <a href="#">14 Va. Admin. Code 5-30-20</a></p> <p>Duties:                      Producers:  <a href="#">14 Va. Admin. Code 5-30-40</a></p> <p>All insurers using producers:  <a href="#">14 Va. Admin. Code 5-30-60</a></p> <p>Replacing insurers:  <a href="#">14 Va. Admin. Code 5-30-51</a></p> <p>Existing insurers:  <a href="#">14 Va. Admin. Code 5-30-55</a></p> <p>Direct response:  <a href="#">14 Va. Admin. Code 5-30-70</a></p> <p>Forms:                      14 Va. Admin. Code 5-30, Form 30-A; Form 30-B, Notice Regarding Replacement; and Form 30-C, Important Notice: Replacement of Life Insurance or Annuities (direct response)</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Washington</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <ul style="list-style-type: none"> <li>• <a href="#">Wash. Admin. Code § 284-23-430</a></li> <li>• Credit life</li> <li>• Certain group life or group annuities</li> <li>• Application to the existing insurer that issued the existing life insurance when a contractual change or conversion privilege is being exercised</li> <li>• Proposed life insurance that is to replace life insurance under a binding or conditional receipt issued by the same company</li> <li>• Transactions where the replacing insurer and the existing insurer are the same, or are subsidiaries or affiliates under common ownership or control with provisos</li> <li>• Registered contracts (exempt from some requirements with provisos)</li> </ul>	<p>Definitions:</p> <p><a href="#">Wash. Admin. Code § 284-23-410</a> (replacement);</p> <p><a href="#">Wash. Admin. Code § 284-23-420</a> (other)</p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">Wash. Admin. Code § 284-23-440</a></p> <p>All insurers:</p> <p><a href="#">Wash. Admin. Code § 284-23-450</a></p> <p>All insurers using producers:</p> <p><a href="#">Wash. Admin. Code § 284-23-455</a></p> <p>Direct response:</p> <p><a href="#">Wash. Admin. Code § 284-23-460</a></p> <p>Forms:</p> <p><a href="#">Wash. Admin. Code § 284-23-485</a></p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">West Virginia</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">W. Va. Code 33-11-5a (c)</a>  <a href="#">W. Va. Code St. R. 114-8-3</a></p> <p>Follows NAIC model</p>	<p>Definitions:  <a href="#">W. Va. Code 33-11-5a (a)</a>;  <a href="#">W. Va. Code St. R. 114-8-2</a></p> <p>Duties:                      Producers:  <a href="#">W. Va. Code St. R. 114-8-4</a></p> <p>All insurers using producers:  <a href="#">W. Va. Code St. R. 114-8-5</a></p> <p>Replacing insurers:  <a href="#">W. Va. Code 33-11-5a (b)</a>;  <a href="#">W. Va. Code St. R. 114-8-6</a></p> <p>Existing insurers:  <a href="#">W. Va. Code St. R. 114-8-7</a></p> <p>Direct response:  <a href="#">W. Va. Code St. R. 114-8-8</a></p> <p>Forms:  <a href="#">W. Va. Code St. R. 114-8, Appendix A; Appendix B; and Appendix C</a></p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Wisconsin</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:  <a href="#">WI ADC Ins 2.0Z (2)</a></p> <p><b>Follows NAIC model</b></p>	<p>Definitions:  <a href="#">WI ADC Ins 2.0Z (3)</a></p> <p>Duties:</p> <p>Producers:  <a href="#">WI ADC Ins 2.0Z (4)</a></p> <p>All insurers using producers:  <a href="#">WI ADC Ins 2.0Z (5)</a></p> <p><b>Replacing insurers:</b>  <a href="#">WI ADC Ins 2.0Z (6)</a></p> <p><b>Existing insurers:</b>  <a href="#">WI ADC Ins 2.0Z (7)</a></p> <p>Direct response:  <a href="#">WI ADC Ins 2.0Z (5)(b)</a></p> <p>Forms:  <a href="#">WI ADC Ins 2.0Z (6)</a>, Appendix I; Appendix II (direct response); and Appendix III (definitions)</p>

State	Applicability and Exemptions	Key Elements/Citations
<p><a href="#">Wyoming</a></p>	<p>Applies to life insurance and annuities.</p> <p>Exemptions:</p> <ul style="list-style-type: none"> <li>• <a href="#">Wy. Admin. Code Ins Gen Ch 12 s 4</a></li> <li>• Credit life</li> <li>• Group life or group annuities</li> <li>• Application to the existing insurer that issued the existing life insurance and a contractual change or a conversion privilege is being exercised</li> <li>• Proposed life insurance that is to replace life insurance under a binding or conditional receipt issued by the same company</li> <li>• Transactions where the replacing insurer and the existing insurer are the same, or are subsidiaries or affiliates under common ownership or control with provisos</li> </ul>	<p>Definitions:</p> <p><a href="#">Wy. Admin. Code Ins Gen Ch 12 s 3</a></p> <p>Duties:</p> <p>Producers:</p> <p><a href="#">Wy. Admin. Code Ins Gen Ch 12 s 5</a></p> <p>All insurers:</p> <p><a href="#">Wy. Admin. Code Ins Gen Ch 12 s 6</a></p> <p>All insurers using producers:</p> <p><a href="#">Wy. Admin. Code Ins Gen Ch 12 s 7</a></p> <p>Direct response:</p> <p><a href="#">Wy. Admin. Code Ins Gen Ch 12 s 8</a></p> <p>Forms:</p> <p><a href="#">Wy. Admin. Code Ins Gen Ch 12 s 11</a>, Replacement Form</p>

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## **ACLI Disclosure Initiative for Fixed, Index and Variable Annuities: Constructive Change on the Horizon**

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### **I. Background and Summary**

A. Over the past several years, regulators, the press, and consumers have regularly observed that useful information about different annuities and sales practices needed improvement to facilitate informed decision-making and suitable matches of customer needs with products.

B. In January 2005, ACLI's Board of Directors took steps to enhance annuity disclosure and improve fixed, index, and variable annuity sales practices.

1. ACLI formed a CEO-level task force to develop recommendations addressing criticism that annuities are misunderstood by consumers. The Task Force emphasized increased attention to suitability, and prioritized enhanced consumer decision-making through improved disclosure with short, plain-English information.
2. To elevate consistently suitable annuity sales practices, ACLI strongly recommended expanding the Senior Protection in Annuity Transactions Model Regulation to all ages, rather than limiting it to age 65 and over.
  - a) The NAIC adopted ACLI's recommended enlargement to all ages in June 2006, renaming it the Suitability in Annuity Transactions Model Regulation. ACLI has actively advocated uniform adoption of this model suitability regulation in the states.
  - b) A chart accompanying this outline compiles the status of the NAIC Suitability in Annuity Transactions Model Regulation together with the status of the NAIC Annuity Disclosure Model Regulation in the states.
3. To constructively improve disclosure, ACLI actively advocated adoption of the NAIC Annuity Disclosure Model Regulation throughout the states. Although developed in 1995, it had not been widely adopted.
  - a) The disclosure model establishes an informational core of improved understanding about annuities.
  - b) Life insurers in the fixed, index and variable annuity markets emphasized design of short, simple, and comparable disclosure as an essential priority to meaningfully help consumers in purchase decisions.

C. The industry group developed a set of “templates” for presenting required disclosure information in a simplified plain-English presentation of information essential to an informed purchase decision.

1. The disclosure templates for fixed and index annuities implement standards mandated by the NAIC Annuity Disclosure Model Regulation.
2. The template for variable annuities parallels the approach of the mutual fund Profile Plus and would be followed by a full prospectus.

D. The industry group produced sample documents under the three templates based on actual fixed, variable and index annuities.

1. The samples were tested in a series of focus groups with retirees, consumers in the baby boomer age group, and annuity salespersons.
2. The various focus groups expressed constructive and positive reactions. The sample documents were revised to reflect focus group feedback and then retested again with the groups.

E. ACLI regularly shared the templates with the SEC, FINRA, and state insurance regulators as the designs evolved.

## **II. Ingredients of the Disclosure Template Project**

- A. General guidelines on how to write readable disclosure materials;
- B. Instructions on how to complete a disclosure template;
- C. Templates for fixed, index, and variable annuity disclosures;
- D. Instructions and a template for depicting indexed interest crediting strategies; and,
- E. A sample of what an actual disclosure might look like for each product.
- F. The ACLI Disclosure Templates and Guides are attached at the back of this outline

## **III. The Guidelines to Readable Disclosure in ACLI’s Disclosure Initiative**

A. The purpose and scope of ACLI’s readable disclosure guidelines directly parallel the SEC’s goals and structure in plain-English Rule 421(d) under the Securities Act of 1933.

1. Under the SEC’s plain-English rule, issuers must use plain-English principles in the organization, language, and design of the front and back cover pages, the summary, and the risk factors section in filings with the SEC’s Division of Corporation Finance under the 1933 Act. When drafting the language for selected parts of the prospectus, issuers must comply with a series of specified plain-English principles.

- a) See “Plain-English Disclosure,” the updated SEC Staff Bulletin No 7 at <http://www.sec.gov/interps/legal/cfslb7a.htm>.
- b) See also the SEC’s “Plain-English Handbook” at <http://www.sec.gov/news/extra/handbook.htm> .
- c) The rule and handbook extol clear, simplified narrative in disclosure, using basic rules of grammar and composition.

## B. ACLI’s Guideline to Readable Disclosure

1. The guideline outlines rules for writing more readable disclosures, and relied on parallel government endeavors as an important resource which is found at <http://www.plainlanguage.gov>.

- a) Like the SEC Handbook, the ACLI guidelines emphasize clear, simplified disclosure, using basic rules of grammar and composition.
- b) The guide instructs and encourages drafters to, among other things:
  - (1) Write for the average reader;
  - (2) Organize to meet the needs of the reader;
  - (3) Include only the information your reader needs;
  - (4) Use headings and make the headings useful
  - (5) Use short sentences and short sections; and,
  - (6) Use lists and tables to simplify information.

2. The structure of the guideline’s follows the organization of the online presentation, “Writing in Plain Language on the TriCare Site” at <http://www.tricare.osd.mil/webmaster/Plain-Language-Rules-Web-Toolkit-2005-07-27.ppt>.

3. Brenda J. Cude, Ph.D., Professor of Housing and Consumer Economics, at the University of Georgia developed the guidelines for ACLI. In her work, Dr. Cude focuses specifically on consumer protection and behavior, including how consumers acquire and use information before making buying decisions.

- a) She represents the consumer perspective in policy discussions at national meetings of insurance regulators.

## IV. Reactions from Regulators to the Summary Disclosure Initiative

### A. SEC

1. On March 23, 2007, ACLI staff met with Representatives of the SEC's Division of Investment Management to discuss the Annuity Disclosure Guidelines developed by the ACLI CEO Task Force on Annuities.
2. The SEC staff evaluated the Guidelines, and commended the industry's proactive approach.
  - a) The SEC staff indicated that the Annuity Disclosure Guidelines could be voluntarily used immediately with variable annuities as "supplemental sales literature" or as a Rule 482 filing under the Securities Act of 1933 without further rulemaking.
  - b) ACLI staff explained that the industry preferred a mandatory, rather than a permissive, approach to the Annuity Disclosure Guidelines. The SEC staff appreciated the industry's preference, and clarified that the guidelines could be used voluntarily until mandatory standards were promulgated.
  - c) The SEC staff also encouraged the industry to consider the summary information in the annuity disclosure guidelines as a form of prospectus simplification that could be used to replace current variable annuity prospectus disclosure.
    - (1) This news may accelerate the timetable originally envisioned by the SEC Task Force for an industry initiated variable annuity prospectus simplification.
    - (2) The SEC staff encouraged the industry group to initiate "data tagging" together with the annuity guidelines to make the information even more useful for consumers.
    - (3) Data tagging provides a method for searching, retrieving, and analyzing information through automated means.
    - (4) In other initiatives, the SEC has explained that [d]ata tagging uses standard definitions to translate text-based information, such as information contained in SEC filings, into files that can be retrieved, searched and analyzed through automated means.
      - (a) Data tags may enable investors and other market participants to more efficiently and effectively analyze data from different sources and automatically exchange financial information across various software platforms, including web services.
      - (b) See SEC Concept Release No. 33-8497 (Oct. 2004) which invited comments on the benefits of tagged data and its potential for improving the timeliness, accuracy, and analysis of financial and other filed information. The

SEC's release explains that the essential elements of tagged data must include:

- (i) the technology to administer the tags — a technology specification that provides the system's core concepts and language;
- (ii) standard definitions to describe the tags — a set of tags agreed upon by users and preparers of information that give data an identity and context by providing an unique label to each specific data element; and a means of presenting and analyzing the tagged data — software programs that process the tagged data for presentation and analytical purposes.

(5) According to the SEC staff, the mutual fund industry has initiated a data tagging process for SEC review.

(a) SEC leadership has assigned a high priority to streamlined, simplified disclosure coupled with data tagging.

(b) Industry initiated development of data tagging in variable annuity disclosure would greatly expedite the approval process, according to the staff. The SEC staff felt that variable annuity disclosure project would have to wait until the pending mutual fund project was completed.

(c) Data tags can be applied through fixed field technology or through actively pairing data and tags.

(i) Fixed field technology requires preparers of information to provide data in a specialized form or template.

(ii) Using fixed field technology, preparers fill out a form and each cell within the form is assigned a tag by the filing system. In this way neither preparers nor users actively participate in tagging the data.

(6) The SEC supports the notion of electronic delivery, but also is committed to making paper copies of disclosure available upon request for those wishing non-electronic disclosure.

(a) ACLI noted in response that ACLI's CEO Task Force considered and supported this approach, which appears in the Annuity Disclosure Guidelines.

(7) As a matter of procedure, ACLI indicated its intention to file a rulemaking petition to expedite the administrative approval process.

(a) The SEC staff was receptive to a rulemaking petition, and will consider whether the petition would be appropriately filed under the Investment Company Act of 1940 or the Securities Exchange Act of 1934.

(b) The Investment Company Act governs disclosure developed by registered separate accounts funding variable annuities. The Securities Exchange Act establishes responsibilities of broker-dealers in distributing securities.

(c) ACLI indicated its expectation that life insurers would be best positioned to develop and update the summary variable annuity disclosure because much of the information exists within the company's domain.

d) ACLI also met with the SEC's Division of Market Regulation [now renamed the Division of Trading and Markets] in the spring of 2007 to provide updates on the summary disclosure initiative and to explain how it could supplant or replace the pending point-of-sale proposal for variable annuities under the 1934 Act.

(1) The Division staff was receptive to the value of simplified plain-English disclosure in a short, user-friendly format.

(2) The Division received ACLI's report on its discussions with the SEC's Division of Investment Management, and the status of discussions.

e) ACLI has developed several refinements to the variable annuity disclosure templates in response to two stages of feedback from the SEC staff. The revised formats are reflected in the variable annuity template following this outline, and is current as of June 2010.

## B. FINRA

1. ACLI met with representatives of FINRA in 2007-2009 to highlight the status of the annuity disclosure projects under development by ACLI.

a) The industry group emphasized that the consensus recommendations at FINRA's Annuity Roundtable in May 2006 have been fulfilled through:

(1) Summary annuity disclosure for fixed, variable, and index annuities;

(2) Implementation of and amendment to the NAIC Suitability in Annuity Transactions Regulation, which fully incorporates FINRA's suitability and supervision standards, and further includes a monitoring role for life insurers issuing these products; and,

(3) Implementation of the NAIC Annuity Disclosure Regulation.

- (4) The ACLI group emphasized that with multiple moving parts dealing with annuity suitability, supervision and disclosure, it is critical that FINRA be fully aware and carefully coordinated on state and federal developments to avoid conflicts and redundancies.
- b) ACLI met with Representatives of FINRA to discuss the Annuity Disclosure Guidelines developed by the ACLI CEO Task Force on Annuities, and summarized the status of several aspects of the CEO Task Force Initiative.
- c) ACLI staff updated FINRA staff with the status and purpose of the annuity disclosure project. The ACLI staff summarized a March 23, 2007 visit with the SEC staff in the Division of Investment Management. The group explained that the SEC Staff:
- (1) Evaluated the Guidelines, and commended the industry's proactive approach;
  - (2) Indicated that the Annuity Disclosure Guidelines could be voluntarily used immediately with variable annuities as "supplemental sales literature" or as a Rule 482 filing under the Securities Act of 1933 without further rulemaking;
  - (3) Appreciated the industry's preference for a mandatory, rather than a permissive approach to the Annuity Disclosure Guidelines, and clarified that the guidelines could be used voluntarily until mandatory standards were promulgated; and,
  - (4) Encouraged the industry group to initiate "data tagging" together with the annuity guidelines to make the information even more useful for consumers. Data tagging provides a method for searching, retrieving, and analyzing information through automated means.

- d) FINRA staff reacted favorably to the ACLI's report, and offered a variety of constructive suggestions.
- e) FINRA staff also suggested a tiered approach to implementing the regulation on a state by state basis, together with SEC and NAIC level implementation.
- f) FINRA is receptive to issuing guidance encouraging broker-dealers to distribute ACLI's summary disclosure materials, and as a means to fulfill disclosure requirements in FINRA Rule 2330.

## C. State Regulators

### 1. Individual States

- a) Several states, such as Iowa and Minnesota have encourage life insurers to voluntarily use the disclosure templates as a means of fulfilling the state's Annuity Disclosure Regulation.
- b) Under these arrangements, use of the template in the pilot program would be in lieu of, and not in addition to, disclosure otherwise required in the Annuity Disclosure Regulation.

# **IMPROVING ANNUITY DISCLOSURE**

## A LIFE INSURANCE INDUSTRY INITIATIVE

*Templates, guidelines, and instructions  
for life insurers to prepare disclosure  
documents for fixed, index, and variable  
annuities*

The American Council of Life Insurers is a Washington, D.C.-based trade association, whose 340 members account for 93 percent of the life insurance industry's total assets in the United States. ACLI member companies offer life insurance; annuities; pensions, including 401(k) plans; long-term care insurance; disability income insurance; reinsurance; and other retirement products.

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Permission granted to legal reserve life insurance companies to use the information, language, and styles in this booklet to develop their own product-specific disclosure documents.

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## INTRODUCTION

Everyone agrees that retirement today requires more planning than in previous generations. Americans are living longer, fewer workers are covered by traditional pension plans that guarantee an income for life, and Social Security likely won't provide the same level of benefits in the future as it does today.

Americans need ways to create and guarantee lifetime income so their standard of living does not decline with age. For many Americans, an annuity can help them achieve that goal. However, most consumers don't understand how an annuity works, its benefits and risks, and what their commitments are under an annuity contract.

In January 2005, ACLI's Board of Directors took steps to bridge this information gap for fixed, index, and variable annuities. A CEO-level task force was formed to develop recommendations to address the widespread criticism that annuities are misunderstood by consumers. Their first recommendations were to give increased attention to suitability and initiate an industry-wide emphasis on consumer empowerment through improved disclosure.

In the area of suitability, ACLI fully supported the NAIC recommendation to expand the Senior Protection in Annuity Transactions Model Regulation to apply to all ages. The NAIC adopted this change in June 2006, and ACLI has been actively pursuing uniform adoption of the expanded model (Suitability in Annuity Transactions) in the states.

With regard to improved disclosure, ACLI has been pursuing state adoption of the NAIC Annuity Disclosure Model Regulation. The model—developed nearly a decade ago, but not widely adopted—provides the necessary base for improved understanding of annuities. However, the companies that comprise ACLI agreed that the development of short, simple, and standardized disclosure documents that are company and product specific was an essential next step to further assist consumers in their purchasing decisions.

ACLI—working closely with member companies and other industry groups—developed a set of “templates” for presenting required disclosure information in a consumer-friendly manner. Disclosure templates for fixed and index annuities are based on the requirements set forth in NAIC's disclosure model regulation. The template for variable annuity products follows disclosure requirements under federal securities laws.

These templates were used to produce sample documents based on actual annuity products. The samples were tested in a series of focus groups and one-on-one interviews with retirees, baby boomers, and producers. The responses from all three groups was overwhelmingly positive. After each set of groups and interviews, recommendations were incorporated into the samples and retested.

As directed by its Board of Directors, ACLI has been meeting with federal and state regulators to have the templates become part of the regulatory regime. The templates have been well received by regulators.

The Iowa Division of Insurance launched a pilot program, beginning January 31, 2008, to introduce the templates to the marketplace. The Ohio Department of Insurance launched a similar program in April 2009. ACLI is hopeful other states will follow suit and embrace the templates as the preferred method of satisfying annuity disclosure requirements.

ACLI continues to work with the Securities and Exchange Commission and the Financial Industry Regulatory Authority to achieve regulatory acceptance of the variable annuity template in connection with federal disclosure and sales practice standards.

# **GENERAL GUIDELINES FOR WRITING READABLE DISCLOSURES**

*Measures of Readability*

*Writing More Readable Disclosures*

*Web Pages*

## GENERAL GUIDELINES FOR WRITING READABLE DISCLOSURES

The following guidelines were developed by Brenda J. Cude, Ph.D., Professor of Housing and Consumer Economics, at the University of Georgia. Dr. Cude is an expert on consumer protection and behavior whose interests focus on how consumers acquire and use information before making buying decisions. She represents the consumer perspective in policy discussions at national meetings of insurance regulators.

Effective writing for a general audience means writing in plain language. Adult literacy levels are relatively low; Adkins and Ozanne report that more than one-fifth of the U.S. adult population is functionally illiterate (lacks reading and writing skills needed to meet daily demands) and another 34 percent is marginally literate.<sup>1</sup> In addition, even literate people may read information too quickly to understand it or may not read it at all if it appears too complex.

### Measures of Readability

There are two widely-used measures of readability: the Flesch Reading Ease Score and the Flesch-Kincaid Grade Level. Each is calculated based on a formula that uses average sentence length and average number of words per sentence. The Flesch Reading Ease Score ranges from 0 to 100, with a higher score indicating easier reading. The Flesch-Kincaid Grade Level formula converts the Flesch Reading Ease score to a U.S. grade school level.<sup>2</sup> Over one-half of the adult population has reading skills below sixth grade.<sup>3</sup> Recent versions of Microsoft Word calculate both the Flesch Reading Ease Score and the Flesch-Kincaid Grade Level.

Alternate measures of readability recognize other elements that affect readability. The FOG (Frequency of Gobbledygook) Index is based on average sentence length and the percentage of words with three or more syllables.<sup>4</sup> There's also a SMOG (Simple Measure of Gobbledygook) Index.<sup>5</sup>

The Cloze Test is a measure of how well "average" consumers understand written material. To use the Cloze Test delete every fifth word and ask one or more persons to fill in the blanks. If the information is well written, the reader should be able to fill in at least 60 percent of the blanks based on the rest of the sentence. If the reader can't complete at least 40 percent of the blanks, the information probably needs to be rewritten.<sup>6</sup>

### Writing More Readable Disclosures

This section outlines a number of rules for writing more readable disclosures. An important resource used in writing this section was <http://www.plainlanguage.gov>.<sup>7</sup>

- Write for the average reader.
  - Know the expertise and interest of your average reader and write to that person. Pretest information with the average reader before releasing it publicly.
  - Don't write to the experts, the lawyers, or management, unless they are the intended audience.
  - Use common, everyday words.
- Organize to meet the needs of the reader.
  - Create a plan for organizing your document (most general to most specific, chronological, etc.) and explain to the reader how you've organized the document and how to use it.
  - Use descriptive headings to help your reader find specific information more easily.
  - Summarize complicated topics before you describe all the details.
  - Put items of most interest to your reader at the beginning.

- 
- Include only the information your reader needs. Too much information and too much detail make it hard for consumers to find the important information.
  - Use headings and make the headings useful.
    - Headings help the reader find their way through the material. Adults read to solve problems and answer questions. Headings help them find the information they need. A question format for headings is often a good way to help the reader find information.
    - Headings should describe all of the material under the heading. If they don't, you need more headings.
    - Every page should have at least one heading and most should have more than one. Don't use more than two or three subordinate levels of headings.
    - Headings should be visually different from the rest of the text and easy to identify. That's most likely to happen if the headings are relatively short—just a few words.
  - Use “you” and other pronouns to help the reader understand the information.
    - Use pronouns to pull readers into the disclosure and make it more meaningful to them.
    - In a question, refer to the reader as I (“how do I,” “how is my annuity”). In the answer, refer to the reader as you (“your annuity”). Refer to the company as “we” or use the name of the insurance company. Don't use the generic “insurer” or “company.”
  - Use active voice.
    - Writing in active voice is the single most powerful change to improve readability.
    - Use active voice to clarify who is doing what. If you use passive voice, who is doing what is often unclear.
    - Active voice is generally shorter, as well as clearer.
    - Active sentences are structured with the actor first (as the subject), then the verb, then the object of the action. (For example: You can't take any of the money out of your annuity after the payout begins, NOT A full surrender of your contract can be made at any time before payouts begin.)
  - Use short sentences and short sections.
    - Use short sentences, paragraphs, and sections to help your reader get through the material. Long dense text with few headings increases the odds the reader will get lost.
    - If you “chunk” the information using columns, headings, and/or bullets, your document will have more white space. White space opens your document visually and makes it more appealing
    - Sentences should average 15 to 20 words and never be longer than 40 words.
    - Use the simplest tense possible. Use base verbs, not nominalizations (hidden verbs).
    - The simplest verb tense is the clearest and strongest; use simple present tense whenever possible. For example, say, “We credit interest every quarter,” not “We will be crediting interest every quarter.”
    - A nominalization is a verb that has been turned into a noun. For example, say, “We manage your investment portfolio” and “We analyze data,” not “We are responsible for management of your investment portfolio” or “We conduct an analysis of the data.”

- 
- Eliminate all excess words.
    - Challenge every word—do you need it?
    - Use pronouns, active voice, and base verbs to eliminate excess words.
    - Eliminate all unnecessary modifiers. For example, in “The two groups issued a joint report,” “joint” isn’t necessary. In “this information is really critical,” “really” isn’t necessary.
  - Use concrete familiar words.
    - Big words and unfamiliar words don’t impress people; they confuse them.<sup>8</sup>
    - If your contract uses a unique term to refer to a contract feature, use that term but include a definition in parentheses after.
    - Use the term premium to refer to money the consumer pays you. Use the term payout to refer to money you pay the consumer.
    - If the contract uses another term for payout, the first time it appears put the other term in the disclosure followed by payout in parentheses. After the first time, use the generic term payout.
    - If the contract uses another term for surrender charge, the first time it appears in the disclosure, put the other term followed by surrender charge in parentheses. After the first time, use the generic term surrender charge. (Example: XYZ Life Insurance Company takes a contingent deferred sales charge (also known as a surrender charge).)
    - Put important terms in bold font the first time you use them. Be selective about what terms you consider important and thus put in bold font; if too many words are in bold, the technique loses its effectiveness.
    - Define (and limit) abbreviations.
    - Avoid jargon, foreign terms, Latin terms, and legal terms.
    - Don’t use “and/or” or multiple negatives.
  - Use “must” to state requirements. Avoid using the more ambiguous “shall.”
    - “Shall” is ambiguous and a word we rarely use in everyday conversation.
    - “Must” (not “shall”) is the clearest way to express a requirement or obligation.<sup>9</sup>
  - Place words carefully.
    - Placing words carefully within a sentence is as important as organizing your document effectively.
    - Keep subject, verb, and object close together; put exceptions at the end.
  - Use lists and tables to simplify information.
    - Lists and tables are one way to explain complex material in less space.
    - Lists and tables give the document more white space and make it more appealing to the reader.
    - If you use a table, explain the table. An example using information from the table is a good way to explain the table.

- Pay attention to format.
  - Make notes to text and tables less visually important than the text. One way to do that is to use a smaller font for notes.
  - Avoid “mice type” (small print) for important information.
  - Serif fonts such as Times and Times New Roman are generally considered most readable but there are ways to make any font more or less readable.<sup>10</sup> For example, each of the fonts below is 12 point but there’s an obvious difference in readability.
    - For example (Arial)
    - For example (Bookman Old Style)
    - For example (Arial Narrow)
    - For example (Gil Sans MT Condensed)
- Don’t overuse **BOLD** and all **CAPITAL** letters for **EMPHASIS**.
- Every page should have at least one heading—and most should have more.
- “Chunk” the information using columns, headings, and/or bullets in your document to create more white space.
- Use lists and tables to explain complex information.

## Web Pages

Most of the preceding information applies to Web pages as well. Online, most people are looking for information to answer immediate questions. They scroll and scan pages looking for information and don’t want to read much. These preferences suggest:<sup>11</sup>

- Break documents into separate topics.
- Use even shorter paragraphs than on paper.
- Use even more lists than on paper.
- Use even more headings with less under each heading.
- Keep the information on each page to no more than two levels; the Web has little room for indenting or showing levels of headings.
- Questions often make great headings because users come to the Web with questions in mind.

And, some thoughts on fonts online:<sup>12</sup>

- Use real text rather than text within graphics.
- Select basic, simple, easily-readable fonts.
- Use a limited number of fonts.
- Ensure sufficient contrast between the text and the background.
- Avoid small font sizes.
- Use relative units for font size.
- Limit the use of font variations such as bold, italics, and ALL CAPITAL LETTERS.
- Don’t rely only on the appearance of the font (color, shape, font variation, placement, etc.) to convey meaning.
- Avoid blinking or moving text.

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## Notes

<sup>1</sup>Adkins, N.R., & Ozanne, J.L. (2005, June). The low literate consumer. *Journal of Consumer Research*, 12, 93-105.

<sup>2</sup>See Coh-Metrix, University of Memphis Department of Psychology at <http://csep.psyc.memphis.edu/cohmetrix/readabilityresearch.htm> or Readability Info at <http://www.readability.info/> for more information.

<sup>3</sup>National Adult Literacy Survey 1992 at <http://nces.ed.gov/naal/>.

<sup>4</sup>See "Writing Tips" at [http://process.umn.edu/groups/ppd/documents/information/Writing\\_Tips.cfm](http://process.umn.edu/groups/ppd/documents/information/Writing_Tips.cfm).

<sup>5</sup>See SMOG Index at [http://en.wikipedia.org/wiki/SMOG\\_Index](http://en.wikipedia.org/wiki/SMOG_Index) and a link to an online calculator to create a SMOG Index.

<sup>6</sup>Hochhauser, M. (2001-2005). Take the Cloze Test: Readability of a Financial Privacy Policy. Privacy Rights Clearinghouse. Available at <http://www.privacyrights.org/fs/fs24b-ClozeFinancial.htm>.

<sup>7</sup>The organization of this section follows the organization of the online Power Point presentation, "Writing in Plain Language on the TriCare Site" at <http://www.tricare.osd.mil/webmaster/Plain-Language-Rules-Web-Toolkit-2005-07-27.ppt>.

<sup>8</sup>For a list of complex words and simpler alternatives, visit [http://employees.faa.gov/worktools/correspondence\\_writing/writing\\_resources/simple\\_words/index.cfm](http://employees.faa.gov/worktools/correspondence_writing/writing_resources/simple_words/index.cfm).

<sup>9</sup>For information about plain language in the legal sector, visit <http://www.plainlanguage.gov/examples/legal/index.cfm>.

<sup>10</sup>See <http://www.webaim.org/techniques/fonts/> for more information about fonts.

<sup>11</sup>From "Writing in Plain Language on the TriCare Site" at <http://www.tricare.osd.mil/webmaster/Plain-Language-Rules-Web-Toolkit-2005-07-27.ppt>.

<sup>12</sup>From [WebAIM.org](http://www.webaim.org) at <http://www.webaim.org/techniques/fonts/>.

# **FIXED ANNUITY DISCLOSURE MATERIALS**

*How to Complete the Template  
for a Fixed Annuity Disclosure*

*Example 1A: Template for a  
Fixed Annuity Disclosure*

*Example 1B: Sample of a  
Fixed Annuity Disclosure*

## HOW TO COMPLETE THE TEMPLATE FOR A FIXED ANNUITY DISCLOSURE

The following is a guide to writing a disclosure for a fixed annuity. It includes general suggestions for writing statements; the types of information that should be covered under each required section, the headings to be used and questions to be answered; and in some cases, provides suggested language that can be used.

Example 1A on page 11 shows a graphic of a fixed annuity disclosure template; Example 1B on pages 12–13 is a sample of what an actual product disclosure may look like. Addendum X shows the disclosure document to scale. Companies are encouraged to follow the language used in the sample where possible. Disclosure documents should be kept short (preferably two pages).

### Guide to Writing Disclosure Statements

- Make a clear distinction about whether a statement is true of all annuities (“an annuity”) or all annuities of this type (“a deferred annuity”) or this product (“this annuity,” “this deferred annuity”).
- In a question, refer to the reader as I (my annuity). In the answer, refer to the reader as you (your annuity). Refer to the company as “we” or use the name of the insurance company. Don’t use the generic “insurer” or “company.”
- Avoid statements that don’t give specific information or don’t give the reader information to find specific information. For example, “Interest is credited to your account” is a general statement that isn’t very useful. “Interest is credited to your account daily” is a specific statement of information as is “Page 23 of your contract explains the different ways that interest may be credited to your account.”
- Use specific terms (i.e. surrender) from your contract in the disclosure but include a definition in parentheses after.
- Put important terms in bold font the first time you use them. Be selective about what terms you consider important. If too many words are in bold, the technique loses its effectiveness.
- If you refer the reader to the contract for more information, be specific about what information is there and exactly where to find it (e.g. use page numbers or section titles).
- The phrasing “includes” (i.e. “Your options include”) suggest there are other options not stated here. If you’ve stated all of the options, say “Your options are.” If you plan to add options later, say, “Your options now are.”
- The term “annuity” is easier for consumers to understand than “contract.” Use “annuity contract” when you’re referring the consumer to the written contract. Don’t use the word policy to describe an annuity.
- When possible, present information in a bulleted list with a brief description and refer to a specific page number or heading in the contract for more information.

## SECTION 1: INTRODUCTION

- Include your company name and name of the product at the top of the page. A company logo also may be inserted.
- Specify if the annuity is single-premium or flexible premium. (Suggested language: This annuity is single-premium which means you buy it with one premium (payment) **or** flexible premium, which means you can purchase it with multiple payments).
- Include statements that briefly explain each of the major features of the annuity. (Suggested language: This annuity is fixed, which means it earns a specified interest rate during the guaranteed period. This annuity is deferred, which means payouts begin at a future date. You don't pay taxes on the interest it earns until the money is paid to you.)
- Include a statement that the buyer can use an annuity for lifetime income but it is not meant for short-term goals. (Suggested language: You can use an annuity to save money for retirement and to receive retirement income for life. It is not meant to be used to meet short-term financial goals. You may pay a fee if you take out money before the end of a time period specified by the contract. You also may pay a tax penalty in addition to taxes due on earnings if you withdraw money before 59 1/2.)

## SECTION 2: THE ANNUITY CONTRACT

### How will the value of my annuity grow?

- Explain how the annuity earns interest, clearly distinguishing between guaranteed, nonguaranteed, and determinable elements, including their limitations.
- Explain any guarantees and the factors that affect the guarantees.
- Explain how and when interest is credited to the account.

Suggestions for writing statements in this section:

- When you use a table, explain the table. An example using information from the table is a good way to explain the table.

## SECTION 3: BENEFITS

### How do I get income (payouts) from my annuity?

- Outline choices in payout options, including whether there is a specified maturity date.
- Describe options and restrictions on withdrawing money from the annuity.
- Explain what happens if the annuitant doesn't choose a payout option.

Suggestions for writing statements in this section:

- Use the terms that are in the contract for payout options, but include a clear explanation of each.
- If the contract uses another term for payout, the first time it appears put the other term in the disclosure followed by payout in parenthesis. After the first time, use the generic term payout.
- Use the term premium to refer to money the consumer pays you. Use the term payout to refer to money you pay the consumer.

### What happens after I die?

- Describe what happens if the owner (and annuitant if different) dies before and after the company starts to pay income from the annuity and any choices the owner will be asked to make.

## SECTION 4: OPTIONAL BENEFIT RIDERS AND THEIR FEES

### What other benefits can I choose?

- List all optional riders, briefly describe each, and include either the range or maximum fee charged for each option.
- If no optional benefit riders are offered, include a statement that none are available.

## SECTION 5: FEES, EXPENSES & OTHER CHARGES

### What happens if I take out some or all of the money from my annuity?

This section should outline:

- The amount of surrender charges and when they are paid.
- Any other charges or adjustments in the amount received when taking money from an annuity.

Suggestions for writing statements in this section:

- If the contract uses another term for surrender charge, the first time it appears in the disclosure, put the other term followed by surrender charge in parentheses. After the first time, use the generic term surrender charge. (Example: ABC Life Insurance Company takes a contingent deferred sales charge (also known as a surrender charge).)
- State surrender charges in a table format and include an example to explain the table.
- Include an explanation of the market value adjustment, if applicable. (Suggested language: When you make a withdrawal, we also may increase or decrease the amount you receive based on a market value adjustment (MVA). If interest rates went up after you bought your annuity, the MVA likely will decrease the amount you receive. If interest rates went down, the MVA likely will increase the amount you receive.)

### Do I pay any other fees or charges?

- Outline any other fees or charges that apply to the annuity, including contract fees and annual service fees, the amounts, and when and how they are collected.

Suggestions for writing statements in this section:

- When you use a table, include an example to explain the table.

## SECTION 6: TAXES

### How will payouts and withdrawals from my annuity be taxed?

This section should outline:

- The meaning of tax-deferred (Suggested language: This annuity is tax-deferred, which means you don't pay taxes on the interest it earns until the money is paid to you. When you take payouts or make a withdrawal, you pay ordinary income taxes on the earned interest. You also pay a 10% federal income tax penalty on earnings you withdraw before age 59 1/2.)
- If your company takes premium taxes from withdrawals or payouts, include a statement describing the deduction. (Suggested language: If your state imposes a premium tax, it will be deducted from the money you receive.)
- That one tax-deferred annuity can be exchanged for another without paying taxes on earnings. (Suggested language: You can exchange one tax-deferred annuity for another without paying taxes on the earnings when you make the exchange. Before you do, compare the benefits, features, and costs of the two annuities.)

---

**SECTION 6: TAXES (continued)****Does buying an annuity in a retirement plan provide extra tax benefits?**

- Explain that there are no tax advantages to buying an annuity as part of a retirement plan. (Suggested language: Buying an annuity within an IRA, 401(k), or other tax-deferred retirement plan doesn't give you any extra tax benefits. Choose your annuity based on its other features and benefits as well as its risks and costs, not its tax benefits.)

**SECTION 7: OTHER INFORMATION****What else do I need to know?**

All disclosures should include the following statements, modified as needed to match your situation.

**Changes to your contract**

We may change your annuity contract from time to time to follow federal or state laws and regulations. If this happens, we'll tell you about the changes in writing.

**Compensation**

We pay the agent, broker, or firm for selling the annuity to you. They may receive additional compensation for selling this annuity contract than for selling other annuity contracts.

**Free Look**

Many states have laws that give you a set number of days to look at an annuity after you buy it. If you decide during that time that you don't want it, you can return the annuity and get all your money back. Read your contract (page x) to learn about your free look period. (Or replace suggested language with state and company specific information about free look.)

Include in this section other important information that doesn't appear elsewhere.

**What should I know about the insurance company?**

Provide a general description of the company as well as all contact information, including an address, phone number, website, and e-mail address (as applicable). You also may consider including financial strength ratings.

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**All disclosures should include the statement:** *This is a summary document and not part of your contract with the insurer.*

EXAMPLE 1A

**Template for a Fixed Annuity Disclosure**

Example 1A shows how to group disclosure material into sections and in two-column format. Disclosure documents should be short (preferably two pages). The template also includes the section headings that are to be used, the questions that need to be answered, and provides direction. Refer to the accompanying instructions for more information about how to complete the template and for suggested language.

SECTION 1

**[COMPANY NAME]****[PRODUCT NAME] Disclosure**

[STATE COMPANY NAME AND NAME OF PRODUCT. SPECIFY IF THE ANNUITY IS A SINGLE- OR FLEXIBLE- PREMIUM ANNUITY. INCLUDE STATEMENTS THAT BRIEFLY EXPLAIN MAJOR FEATURES AND HOW IT ACCUMULATES VALUE. DISCLOSE THAT THE ANNUITY IS NOT MEANT TO BE USED TO MEET SHORT-TERM GOALS. SUGGESTED LANGUAGE PROVIDED IN ACCOMPANYING INSTRUCTIONS.]

SECTION 2

**THE ANNUITY CONTRACT****How will the value of my annuity grow?**

[EXPLAIN HOW THE ANNUITY EARNS INTEREST AND HOW AND WHEN INTEREST IS CREDITED TO THE ACCOUNT. DISTINGUISH BETWEEN GUARANTEED, NON-GUARANTEED, AND DETERMINABLE ELEMENTS.]

**BENEFITS****How do I get income (payouts) from my annuity?**

[OUTLINE VARIOUS PAYOUT OPTIONS AND INCLUDE IF THERE IS A SPECIFIED MATURITY DATE. DESCRIBE OPTIONS AND RESTRICTIONS ON WITHDRAWING MONEY, AS WELL AS WHAT HAPPENS WHEN A PAYOUT OPTION IS NOT SELECTED.]

**What happens after I die?**

[DESCRIBE WHAT HAPPENS IF DEATH OCCURS BEFORE AND AFTER INCOME PAYMENTS START AND ANY CHOICES THE ANNUITY OWNER WILL BE ASKED TO MAKE.]

**OPTIONAL BENEFIT RIDERS AND THEIR FEES****What other benefits can I choose?**

[LIST AND DESCRIBE ALL OPTIONAL RIDERS. INCLUDE EITHER THE RANGE OF FEES OR MAXIMUM FEE CHARGED FOR EACH.]

**FEES, EXPENSES AND OTHER CHARGES****What happens if I take out some or all of the money from my annuity?**

[STATE SURRENDER CHARGES AND PROVIDE EXAMPLE. INCLUDE EXPLANATION OF MARKET VALUE ADJUSTMENT, IF APPLICABLE. SUGGESTED LANGUAGE PROVIDED IN ACCOMPANYING INSTRUCTIONS.]

**Do I pay any other fees or charges?**

[OUTLINE OTHER FEES THAT APPLY.]

SECTION 3

SECTION 4

SECTION 5

**TAXES****How will payouts and withdrawals from my annuity be taxed?**

[DESCRIBE MEANING OF TAX-DEFERRED. INCLUDE STATEMENT DESCRIBING ANY DEDUCTION TAKEN FOR PREMIUM TAXES. EXPLAIN TAX TREATMENT OF EXCHANGES. SUGGESTED LANGUAGE PROVIDED IN ACCOMPANYING INSTRUCTIONS.]

**Does buying an annuity in a retirement plan provide extra tax benefits?**

[EXPLAIN THAT THERE ARE NO ADDITIONAL TAX BENEFITS. SUGGESTED LANGUAGE PROVIDED IN ACCOMPANYING INSTRUCTIONS.]

**OTHER INFORMATION****What else do I need to know?****Changes to your contract**

[INCLUDE A STATEMENT EXPLAINING THAT THE CONTRACT OWNER WILL BE NOTIFIED IN WRITING OF ANY CHANGES TO THE CONTRACT. SUGGESTED LANGUAGE PROVIDED IN ACCOMPANYING INSTRUCTIONS.]

**Compensation**

[INCLUDE A STATEMENT EXPLAINING THAT THE SELLER MAY RECEIVE ADDITIONAL COMPENSATION FOR SELLING THIS ANNUITY. SUGGESTED LANGUAGE PROVIDED IN ACCOMPANYING INSTRUCTIONS.]

**Free Look**

[INCLUDE STATE AND COMPANY SPECIFIC INFORMATION ABOUT FREE LOOK. SUGGESTED LANGUAGE PROVIDED IN ACCOMPANYING INSTRUCTIONS.]

**What should I know about the insurance company?**

[PROVIDE OTHER RELEVANT COMPANY INFORMATION, INCLUDING ADDRESS, PHONE NUMBER, WEBSITE. INCLUDE THE STATEMENT: *THIS IS A SUMMARY DOCUMENT AND NOT PART OF YOUR CONTRACT WITH THE INSURER.*]

SECTION 6

SECTION 7

## EXAMPLE 1B

**Sample of a Fixed Annuity Disclosure**

Example 1B is a sample of how a final disclosure document might look. This is only a sample and is not intended to serve as a model disclosure for all types of annuities. Disclosure documents for each company and product will vary. Disclosure documents should be kept short (preferably two pages).

**Fixed Single-Premium Deferred Annuity Disclosure**

This document reviews important points to think about before you buy this XYZ Insurance Company annuity. This annuity is single-premium which means you buy it with one premium (payment). It is a fixed annuity which means it earns a specified interest rate during the guaranteed period. This annuity is **deferred**, which means payouts begin at a future date. You don't pay taxes on the interest it earns until the money is paid to you.

You can use an annuity to save money for retirement and to receive retirement income for life. It is **not** meant to be used to meet short-term financial goals.

**If you have questions about this annuity, please ask your agent, broker, or advisor, or contact a company representative at 800-123-4567.**

**THE ANNUITY CONTRACT****How will the value of my annuity grow?**

Your annuity earns **tax-deferred** interest at a **guaranteed minimum rate** for a **guaranteed period**. When you buy your annuity, you choose a guaranteed period of 5, 6, 7, 8, 9, or 10 years. The guaranteed rate depends on the guaranteed period you choose and current interest rates in the market. Interest compounds daily and is credited to your annuity account on the last day of each month.

Within 30 days after the end of each guaranteed period, you choose a new guaranteed period or surrender (cancel and withdraw the money from) your annuity. If you do nothing, a new guaranteed period begins that is the same length as the one before. The new guaranteed rate depends on the length of the new guaranteed period and current market rates. Interest compounds daily at the new rate in the new period.

**The account value of your annuity cannot go down.**

**BENEFITS****How do I get income (payouts) from my annuity?**

When you apply for your annuity, you choose a payout commencement date—when you start to get income from your annuity. You also choose how to get the income—the payout option. Your choices now are:

- **Life:** Guarantees income for as long as you live.
- **Joint and survivor life:** Guarantees income for as long as you or your joint annuitant (usually a spouse) live.
- **Life income with period certain:** Guarantees income for as long as you live. If you die within the "period certain" (usually 10 or 20 years), it pays income to your beneficiary for the rest of the period.
- **Designated period of time:** Pays income for that period.
- **Lump sum:** One payout.

You may change both the start date and the payout option up until payout begins.

If you don't choose an annuity payout option, we start payouts on [FILL IN DATE] and continue them for [FILL IN DURATION].

Once payouts begin, you can't surrender (cancel) your annuity.

**What happens after I die?**

If you die before we start to pay you income from your annuity, we pay the value of your annuity to your beneficiary. If you die after the payouts start, depending on the type of payout you chose, we pay the remaining value in the annuity, if any, to your beneficiary.

**OPTIONAL BENEFIT RIDERS AND THEIR FEES****What other benefits can I choose?**

This contract also offers other benefits for an extra cost. Your choices and the fees charged are described below. You will pay a fee for each option you choose every year you own the annuity. The annual cost will be reflected in a lower rate credited to your account balance than you would have received without the riders.

**Annual Fees for Available Optional Benefit Riders**

	<b>Maximum</b>
<u>Principal Guarantee Rider</u>	.10%
If you surrender your contract before the end of the guarantee period, this rider guarantees the amount you receive will never be less than your initial premium payment.	
<u>Additional Liquidity Benefit</u>	.10%
Allows you to withdraw up to 10% annually without charge.	

**FEES, EXPENSES & OTHER CHARGES****What happens if I take out some or all of the money from my annuity?**

You can't take any of the money out of your annuity after the payout begins. Before it begins, you can take out all of your annuity's value (**full surrender**) or part of it (**partial surrender**). You can take a partial surrender as long as the amount you take is at least \$1,000 and you leave at least \$5,000 in the account.

## EXAMPLE 1B—CONTINUED

We take a **contingent deferred sales charge (also known as a surrender charge)** from amounts you withdraw before the end of the seventh contract year. Here's how the charge is calculated:

<b>Contract year</b>	1	2	3	4	5	6	7	8+
<b>Surrender charge</b>	7%	6%	5%	4%	3%	2%	1%	0

*Example:* If you withdraw \$5,000 from your annuity in the third year contract year, your surrender charge is  $\$5,000 \times 0.05 = \$250$ . If you take out any amount after the end of the seventh contract year, there's no charge.

When you make a withdrawal, we also may increase or decrease the amount you receive based on a **market value adjustment (MVA)**. If interest rates went up after you bought your annuity, the MVA likely will decrease the amount you receive. If interest rates went down, the MVA likely will increase the amount you receive.

*Exceptions:* In some cases, we may waive the surrender charge or the market value adjustment. For example, there's no surrender charge if we pay the remaining value of your annuity to a beneficiary after your death.

#### Do I pay any other fees or charges?

No. There aren't any other fees or charges on this annuity. Also, you pay only one premium for your annuity.

### TAXES

#### How will payouts and withdrawals from my annuity be taxed?

This annuity is tax-deferred, which means you don't pay taxes on the interest it earns until the money is paid to you. When you take payouts or make a withdrawal, you pay ordinary income taxes on the earned interest. You also pay a 10% federal income tax penalty on earnings you withdraw before age 59 1/2. If your state imposes a premium tax, it will be deducted from the money you receive.

You can exchange one tax-deferred annuity for another without paying taxes on the earnings when you make the exchange. Before you do, compare the benefits, features, and costs of the two annuities. You may pay a surrender charge if you make the exchange during the first seven years you own the annuity. Also, you may pay a surrender charge if you make withdrawals from the new annuity during the first years you own it.

#### Does buying an annuity in a retirement plan provide extra tax benefits?

Buying an annuity within an IRA, 401(k), or other tax-deferred retirement plan doesn't give you any extra tax benefits. Choose your annuity based on its other features and benefits as well as its risks and costs, not its tax benefits.

### OTHER INFORMATION

#### What else do I need to know?

##### Changes to your contract

We may change your annuity contract from time to time to follow federal or state laws and regulations. If we do, we'll tell you about the changes in writing.

##### Compensation

We pay the agent, broker, or firm for selling the annuity to you. They may receive additional compensation for selling this annuity contract than for selling other annuity contracts.

##### Free look

Many states have laws that give you a set number of days to look at an annuity after you buy it. If you decide during that time that you don't want it, you can return the annuity and get all your money back. Read your contract (page x) to learn about your **free look** period.

#### What should I know about the insurance company?

XYZ Life Insurance Company offers a wide variety of retirement and financial security products, including life insurance, annuities, long-term care, and disability income insurance. We also are a leading provider of products and services to workplace-based pension plans—both defined contribution and defined benefit plans. Our financial strength ratings are: A+ (A.M. Best); AA (S&P); Aa3 (Moody's); and AA+ (Fitch).

XYZ Life Insurance Company  
123 Main Street  
Your Town USA  
Telephone: 800-123-4567  
<http://www.xyzlife.com>

This is a summary document and not part of your contract with the insurer.



# **INDEX ANNUITY DISCLOSURE MATERIALS**

*How to Complete the Template  
for an Index Annuity Disclosure*

*Example 2A: Template for an  
Index Annuity Disclosure*

*Example 2B: Sample of an  
Index Annuity Disclosure*

*How to Complete the Template  
for Depicting Indexed Interest*

*Example 2C: Template for Depiction  
of Indexed Interest*

*Example 2D: Sample of Depiction  
of Indexed Interest*

## HOW TO COMPLETE THE TEMPLATE FOR AN INDEX ANNUITY DISCLOSURE

The following is a guide to writing a disclosure for an index annuity. It includes general suggestions for writing statements; the types of information that should be covered under each required section, the headings to be used and questions to be answered; and in some cases, provides suggested language that can be used.

Example 2A on page 19 shows a graphic of an index annuity disclosure template; Example 2B on pages 20–21 is an example of what an actual product disclosure may look like. Addendum X shows the disclosure document to scale. Companies are encouraged to follow the language used in the sample where possible. Disclosure documents should be kept short (preferably two pages). The font in the documents should be a minimum size of 11 point.

### Guide to Writing Disclosure Statements

- Make a clear distinction about whether a statement is true of all annuities (“an annuity”) or all annuities of this type (“a deferred annuity”) or this product (“this annuity,” “this deferred annuity”).
- In a question, refer to the reader as I (my annuity). In the answer, refer to the reader as you (your annuity). Refer to the company as “we” or use the name of the insurance company. Don’t use the generic “insurer” or “company.”
- Avoid statements that don’t give specific information or don’t give the reader information to find specific information. For example, “Interest is credited to your account” is a general statement that isn’t very useful. “Interest is credited to your account daily” is a specific statement of information as is “Page 23 of your contract explains the different ways that interest may be credited to your account.”
- Use specific terms (i.e. surrender) from your contract in the disclosure but include a definition in parentheses after.
- Put important terms in bold font the first time you use them. Be selective about what terms you consider important. If too many words are in bold, the technique loses its effectiveness.
- If you refer the reader to the contract for more information, be specific about what information is there and exactly where to find it (e.g. use page numbers or section titles).
- The phrasing “includes” (“Your options include”) suggest there are other options not stated here. If you’ve stated all of the options, say “Your options are.” If you plan to add options later, say, “Your options now are.”
- The term “annuity” is easier for consumers to understand than “contract.” Use “annuity contract” when you’re referring the consumer to the written contract. Don’t use the word policy to describe an annuity.
- When possible, present information in a bulleted list with a brief description and refer to a specific page number or heading in the contract for more information.
- Disclosure documents should be kept short (preferably two pages). The font in the documents should be a minimum size of 11 point.

## SECTION 1: INTRODUCTION

- Include your company name and name of the product at the top of the page. A company logo also may be inserted.
- Specify if the annuity is single premium or flexible premium. (Suggested language: This annuity is single-premium which means you buy it with one premium (payment) **or** flexible premium which means you can purchase it with multiple payments.)
- Include statements that briefly explain each of the major features of the annuity. (Suggested language: This annuity is deferred, which means payouts begin at a later date. You don't pay taxes on the interest it earns until the money is paid to you. This annuity can earn interest in two ways: 1) interest that is guaranteed in the first year and can't go below [Insert Rate/Percentage] after that, and 2) interest that depends on how one or more market indexes perform. This annuity doesn't participate directly in any stock or equity investments. You aren't buying shares of stock or an index. Dividends paid on the stocks on which the indexes are based don't increase your annuity earnings.)
- Include a statement that the buyer can use an annuity for lifetime income but it is not meant for short-term goals. (Suggested language: You can use an annuity to save money for retirement and to receive retirement income for life. It is not meant to be used to meet short-term financial goals. You may pay a fee if you take out money before the end of a time period specified by the contract. You also may pay a tax penalty in addition to taxes due on earnings if you withdraw money before 59 1/2.)

## SECTION 2: THE ANNUITY CONTRACT

### How will the value of my annuity grow?

- Explain how the annuity earns interest, clearly distinguishing between guaranteed, nonguaranteed, and determinable elements, including their limitations.
- Explain any guarantees and the factors that affect the guarantees.
- Explain how and when interest is credited to the account, including a depiction explaining the interest crediting strategy. (The depiction should be attached to the two-page disclosure document as supplemental material. A guide and template for developing the depiction are on pages 22–23.)
- Explain any caps or floors on interest and how they work.

Suggestions for writing statements in this section:

- When you use a table, explain the table. An example using information from the table is a good way to explain the table.

## SECTION 3: BENEFITS

### How do I get income (payouts) from my annuity?

- Outline choices in payout options, including whether there is a specified maturity date.
- Describe options and restrictions on withdrawing money from the annuity.
- Explain what happens if the annuitant doesn't choose a payout option.

Suggestions for writing statements in this section:

- Use the terms that are in the contract for payout options, but include a clear explanation of each.
- If the contract uses another term for payout, the first time it appears put the other term in the disclosure followed by payout in parenthesis. After the first time, use the generic term payout.
- Use the term premium to refer to money the consumer pays you. Use the term payout to refer to money you pay the consumer.

**What happens after I die?**

- Describe what happens if the owner (and annuitant if different) dies before and after the company starts to pay income from the annuity and any choices the owner will be asked to make.

**SECTION 4: OTHER BENEFITS AND THEIR FEES****What other benefits can I choose?**

- List all optional riders, briefly describe each, and include either the range of fees or maximum fee charged for each option.
- If no optional benefit riders are offered, include a statement that none are available.

**SECTION 5: FEES, EXPENSES & OTHER CHARGES****What happens if I take out some or all of the money from my annuity?**

This section should outline:

- The amount of surrender charges and when they are paid.
- Any other charges or adjustments in the amount received when taking money from an annuity.

Suggestions for writing statements in this section:

- If the contract uses another term for surrender charge, the first time it appears in the disclosure, put the other term followed by surrender charge in parentheses. After the first time, use the generic term surrender charge. (Example: XYZ Life Insurance Company takes a contingent deferred sales charge (also known as a surrender charge)...).
- State surrender charges in a table format and include an example to explain the table.
- Include an explanation of the market value adjustment, if applicable. (Suggested language: When you make a withdrawal, we also may increase or decrease the amount you receive based on a market value adjustment (MVA). If interest rates went up after you bought your annuity, the MVA likely will decrease the amount you receive. If interest rates went down, the MVA likely will increase the amount you receive.)

**Do I pay any other fees or charges?**

- Outline any other fees or charges that apply to the annuity, including contract fees and annual service fees, the amounts, and when and how they are collected.

Suggestions for writing statements in this section:

- When you use a table, include an example to explain the table.

## SECTION 6: TAXES

### How will payouts and withdrawals from my annuity be taxed?

This section should outline:

- The meaning of tax-deferred (Suggested language: This annuity is tax-deferred, which means you don't pay taxes on the interest it earns until the money is paid to you. When you take payouts or make a withdrawal, you pay ordinary income taxes on the earned interest. You also pay a 10% federal income tax penalty on earnings you withdraw before age 59 1/2.)
- If your company takes premium taxes from withdrawals or payouts, include a statement describing the deduction. (Suggested language: If your state imposes a premium tax, it will be deducted from the money you receive.)
- That one tax-deferred annuity can be exchanged for another without paying taxes on earnings. (Suggested language: You can exchange one tax-deferred annuity for another without paying taxes on the earnings when you make the exchange. Before you do, compare the benefits, features, and costs of the two annuities.)

### Does buying an annuity in a retirement plan provide extra tax benefits?

- Explain that there are no tax advantages to buying an annuity as part of a retirement plan. (Suggested language: Buying an annuity within an IRA, 401(k), or other tax-deferred retirement plan doesn't give you any extra tax benefits. In that case, choose your annuity based on its other features and benefits as well as its risks and costs, not its tax benefits.)

## SECTION 7: OTHER INFORMATION

### What else do I need to know?

All disclosures should include the following statements, modified as needed to match your situation:

#### Changes to your contract

We may change your annuity contract from time to time to follow federal or state laws and regulations. If this happens, we'll tell you about the changes in writing.

#### Compensation

We pay the agent, broker, or firm for selling the annuity to you. They may receive additional compensation for selling this annuity contract than for selling other annuity contracts.

#### Free Look

Many states have laws that give you a set number of days to look at an annuity after you buy it. If you decide during that time that you don't want it, you can return the annuity and get all your money back. Read your contract [Insert page number] to learn about your free look period. (Or replace suggested language with state and company specific information about free look.)

Include in this section other important information that doesn't appear elsewhere, such as what happens if the annuitant doesn't choose a payout option and information about the impact of riders.

### What should I know about the insurance company?

Provide a general description of the company as well as all contact information, including an address, phone number, website, and e-mail address (as applicable). You also may consider including financial strength ratings.

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**All disclosures should include the statement:** *This is a summary document and not part of your contract with the insurer.*

## EXAMPLE 2A

**Template for an Index Annuity Disclosure**

Example 2A shows how to group disclosure material into sections and in two-column format. Disclosure documents should be short (preferably two pages). The template also includes the section headings that are to be used, the questions that need to be answered, and provides suggested language that can be used. If there is additional information that you need to include, including a depiction of how indexed interest is calculated, it should be attached to the disclosure.

SECTION 1

**[COMPANY NAME]****[PRODUCT NAME] Disclosure**

[STATE COMPANY NAME AND NAME OF PRODUCT. SPECIFY IF THE ANNUITY IS A SINGLE- OR FLEXIBLE- PREMIUM ANNUITY. INCLUDE STATEMENTS THAT BRIEFLY EXPLAIN MAJOR FEATURES AND HOW IT ACCUMULATES VALUE. DISCLOSE THAT THE ANNUITY IS NOT MEANT TO BE USED TO MEET SHORT-TERM GOALS. SUGGESTED LANGUAGE PROVIDED IN ACCOMPANYING INSTRUCTIONS.]

SECTION 2

**THE ANNUITY CONTRACT****How will the value of my annuity grow?**

[EXPLAIN HOW THE ANNUITY EARNS INTEREST AND HOW AND WHEN INTEREST IS CREDITED TO THE ACCOUNT. DISTINGUISH BETWEEN GUARANTEED, NONGUARANTEED, AND DETERMINABLE ELEMENTS AND EXPLAIN ANY CAPS OR FLOORS ON INTEREST. ATTACH TO THE DISCLOSURE A DEPICTION OF HOW INDEXED INTEREST IS CALCULATED.]

**BENEFITS****How do I get income (payouts) from my annuity?**

[OUTLINE VARIOUS PAYOUT OPTIONS AND INCLUDE IF THERE IS A SPECIFIED MATURITY DATE. DESCRIBE OPTIONS AND RESTRICTIONS ON WITHDRAWING MONEY, AS WELL AS WHAT HAPPENS WHEN A PAYOUT OPTION IS NOT SELECTED.]

**What happens after I die?**

[DESCRIBE WHAT HAPPENS IF DEATH OCCURS BEFORE AND AFTER INCOME PAYMENTS START AND ANY CHOICES ANNUITY OWNER WILL BE ASKED TO MAKE.]

**OPTIONAL BENEFIT RIDERS AND THEIR FEES****What other benefits can I choose?**

[LIST AND DESCRIBE ALL OPTIONAL RIDERS. INCLUDE EITHER THE RANGE OF FEES OR MAXIMUM FEE CHARGED FOR EACH.]

**FEES, EXPENSES AND OTHER CHARGES****What happens if I take out some or all of the money from my annuity?**

[STATE SURRENDER CHARGES AND PROVIDE EXAMPLE. INCLUDE EXPLANATION OF MARKET VALUE ADJUSTMENT, IF APPLICABLE. SUGGESTED LANGUAGE PROVIDED IN ACCOMPANYING INSTRUCTIONS.]

**Do I pay any other fees or charges?**

[OUTLINE OTHER FEES THAT APPLY.]

SECTION 3

SECTION 4

SECTION 5

**TAXES****How will payouts and withdrawals from my annuity be taxed?**

[DESCRIBE MEANING OF TAX-DEFERRED. INCLUDE STATEMENT DESCRIBING ANY DEDUCTION TAKEN FOR PREMIUM TAXES. EXPLAIN TAX TREATMENT OF EXCHANGES. SUGGESTED LANGUAGE PROVIDED IN ACCOMPANYING INSTRUCTIONS.]

**Does buying an annuity in a retirement plan provide extra tax benefits?**

[EXPLAIN THAT THERE ARE NO ADDITIONAL TAX BENEFITS. SUGGESTED LANGUAGE PROVIDED IN THE ACCOMPANYING INSTRUCTIONS.]

**OTHER INFORMATION****What else do I need to know?****Changes to your contract**

[INCLUDE A STATEMENT EXPLAINING THAT THE CONTRACT OWNER WILL BE NOTIFIED IN WRITING OF ANY CHANGES TO THE CONTRACT. SUGGESTED LANGUAGE PROVIDED IN THE ACCOMPANYING INSTRUCTIONS.]

**Compensation**

[INCLUDE A STATEMENT EXPLAINING THAT THE SELLER MAY RECEIVE ADDITIONAL COMPENSATION FOR SELLING THIS ANNUITY. SUGGESTED LANGUAGE PROVIDED IN ACCOMPANYING INSTRUCTIONS.]

**Free Look**

[INCLUDE STATE AND COMPANY SPECIFIC INFORMATION ABOUT FREE LOOK. SUGGESTED LANGUAGE PROVIDED IN THE ACCOMPANYING INSTRUCTIONS.]

**What should I know about the insurance company?**

[PROVIDE OTHER RELEVANT COMPANY INFORMATION, INCLUDING ADDRESS, PHONE NUMBER, WEBSITE. INCLUDE THE STATEMENT: *THIS IS A SUMMARY DOCUMENT AND NOT PART OF YOUR CONTRACT WITH THE INSURER.*]

SECTION 6

SECTION 7

## EXAMPLE 2B

**Sample of an Index Annuity Disclosure**

Example 2B is a sample of how a final disclosure document might look. This is only a sample and is not intended to serve as a model disclosure for all types of annuities. Disclosure documents for each company and product will vary. Disclosure documents should be kept short (preferably two pages).

**Index Annuity Disclosure**

This document reviews important points to think about before you buy this XYZ Life Insurance Company annuity. It is a single-premium annuity which means you buy it with one premium (payment).

This annuity is **deferred**, which means payouts begin at a future date. You don't pay taxes on the interest it earns until the money is paid to you.

This annuity can earn interest in two ways: 1) interest that is guaranteed in the first year and can't go below 1.5% after that, and 2) interest that depends on how one or more market indexes perform. This annuity does not participate directly in any stock or equity investments. You aren't buying shares of stock or an index. Dividends paid on the stocks on which the indexes are based don't increase your annuity earnings.

You can use this annuity to save for retirement and to receive retirement income for life. It is not meant to be used to meet short-term financial goals.

**If you have questions about this annuity, please ask your agent, broker, advisor, or contact a company representative at 800-123-4567.**

**THE ANNUITY CONTRACT****How will the value of my annuity grow?**

The XXX Annuity earns interest in two ways. One is a fixed rate that is guaranteed at x% for the first year. After the first year, the **fixed** rate is guaranteed to be at least 1.5%.

The value of this annuity also may grow through **indexed** returns. The amount of the index-linked interest depends on how the Dow Jones Industrial Average, a nationally recognized market index, performs. Your annuity contract (see page x or Section x) spells out how index-linked interest is credited to your annuity account at the end of each contract year.

How much index-linked interest is credited to your account annually depends on the sum of the **capped monthly returns**. These are the caps (or limits) we set on the effect on your account value of the positive change in the market index from one month to the next. We set the cap on the positive returns at the beginning of each contract year. That cap can change each year. **We guarantee the monthly cap will never be lower than 1%.**

However, interest earnings credited can never be less than zero, even if the sum of the monthly returns is negative.

Here's how the caps work. If the market index increases more than the cap, the monthly change increases by the amount of the cap. If the market index increases less than the cap, the monthly change increases by the amount of the increase. If the market index goes down, the monthly change goes down by the full amount of the decrease. The monthly changes are then added up at the end of the contract year and any interest earned is credited to your account. Each of the following could happen:

- A large decrease in index-linked interest in one month could wipe out some or all of the monthly increases from earlier months.
- Even if the index is up overall for the year, the annual index-linked interest credited could be lower (or zero).

- If the total of the capped monthly returns is negative, the index-linked interest for that year would be zero.

**Attached is a depiction explaining how indexed interest is calculated.**

**BENEFITS****How do I get income (payouts) from my annuity?**

Your annuity's account (the value while you're paying into your annuity) depends on your premium and any annual index-linked interest and guaranteed interest credited to your account. After five contract years, you can ask the company to pay the accumulation value of your contract to you as income. You can choose how to get the income. Your annuity contract describes your options in detail (see page x or Section x). Your current choices are:

- **Life:** Guarantees income for as long as you live.
- **Joint and survivor life:** Guarantees income for as long as you or your joint annuitant (usually a spouse) live.
- **Life income with period certain:** Guarantees income for as long as you live. If you die within the "period certain" (usually 10 or 20 years), it pays income to your beneficiary for the rest of the period.
- **Designated period of time:** Pays income for that period.
- **Lump sum:** One payout.

If you don't choose an annuity payout option, we start payouts on [FILL IN DATE] and continue them for [FILL IN DURATION].

Once you start to get income from your annuity, the account value stops earning index-linked interest. It will continue to earn guaranteed interest.

In the first 10 contract years, you can withdraw money from your annuity once a contract year without paying a fee. The most you can withdraw each year without paying a fee is 10% of the total premiums you've paid.

## EXAMPLE 2B—CONTINUED

If you withdraw 50% or more of the premiums paid, you lose the right to make a withdrawal without paying a fee.

Once payouts begin, you can't surrender (cancel) your annuity.

#### What happens after I die?

If you die before we start to pay you income from your annuity, your beneficiary can choose to get the accumulation value of your annuity as one payment or as a series of payouts over time. If you die after payouts start, depending on the type of payout you chose, we pay the remaining value in the annuity, if any, to your beneficiary.

#### OPTIONAL BENEFITS AND THEIR FEES

##### What other benefits can I choose?

There are no optional benefits available with this annuity contract.

#### FEES, EXPENSES AND OTHER CHARGES

##### What happens if I take out some or all of the money from my annuity?

When you take money from your annuity, you may lose some or all of your credited interest. If you take out all (**full surrender**) or part (**partial surrender**) of the money, you also may have to pay a **surrender charge**. The amount of the charge depends on how long you've had the annuity and how much you withdraw. Here's how the charge is calculated:

Contract year	1	2	3	4	5	6	7	8+
Surrender charge	10%	9%	8%	7%	6%	5%	4%	0

*Example:* After two years, you've paid \$10,000 in premium. You want to withdraw \$1,100 from your annuity in the third year. Since \$1,100 is more than 10% of the premium you've paid ( $\$10,000 \times 0.10 = \$1,000$ ), your surrender charge is  $\$1,100 \times 0.08 = \$88$ . There's no surrender charge after the end of the seventh contract year.

When you make a withdrawal, we also may increase or decrease the amount you receive based on a **market value adjustment (MVA)**. If interest rates went up after you bought your annuity, the MVA likely will decrease the amount you receive. If interest rates went down, the MVA likely will increase the amount you receive.

##### Do I pay any other fees or charges?

No. There aren't any other fees or charges on this annuity. Also, you pay only one premium for your annuity.

#### TAXES

##### How will payouts and withdrawals from my annuity be taxed?

This annuity is tax-deferred, which means you don't pay taxes on the interest it earns until the money is paid to you. When you take payouts or make a withdrawal, you pay ordinary income taxes on the earned interest. You also pay a 10% federal income tax penalty on earnings

you withdraw before age 59 1/2. If your state imposes a premium tax, it will be deducted from the money you receive.

You can exchange one tax-deferred annuity for another without paying taxes on the earnings when you make the exchange. Before you do, compare the benefits, features, and costs of the two annuities. You may pay a surrender charge if you make the exchange during the first seven years you own the annuity. Also, you may pay a surrender charge if you make withdrawals from the new annuity during the first years you own it.

##### Does buying an annuity in a retirement plan provide extra tax benefits?

Buying an annuity within an IRA, 401(k), or other tax-deferred retirement plan doesn't give you any extra tax benefits. Choose your annuity based on its other features and benefits as well as its risks and costs, not its tax benefits.

#### OTHER INFORMATION

##### What else do I need to know?

###### Changes to your contract

We may change your annuity contract from time to time to follow federal or state laws and regulations. If we do, we'll tell you about the changes in writing.

###### Compensation

We pay the agent, broker, or firm for selling the annuity to you. They may receive additional compensation for selling this annuity contract than for selling other annuity contracts.

###### Free Look

Many states have laws that give you a set number of days to look at an annuity after you buy it. If you decide during that time that you don't want it, you can return the annuity and get all your money back. Read your contract (page x) to learn about your **free look** period.

##### What should I know about the insurance company?

XYZ Life Insurance Company offers a wide variety of retirement and financial security products, including life insurance, annuities, long-term care, and disability income insurance. We also are a leading provider of products and services to workplace-based pension plans—both defined contribution and defined benefit plans. Our financial strength ratings are: A+ (A.M. Best); AA (S&P); Aa3 (Moody's); and AA+ (Fitch).

XYZ Life Insurance Company  
123 Main Street  
Your Town USA  
Telephone: 800-123-4567  
<http://www.xyzlife.com>

This is a summary document and not part of your contract with the insurer.



## HOW TO COMPLETE THE TEMPLATE FOR DEPICTING INDEXED INTEREST

The following is a guide for developing a depiction of how credited interest is calculated for an index annuity. A separate depiction for each indexed account offered under the annuity contract should be attached to the disclosure document as a supplement. Each depiction must include a written explanation of how interest is calculated. A graphic example supporting the explanation enhances consumer understanding.

### Guidelines for developing a depiction

- Explain how indexed interest is calculated for a single index term. For example, if an indexed interest credit covers a 12-month period, then the examples should show how indexed interest is calculated for a 12-month period. If the indexed interest credit covers more than a 12-month period, such as a 5-year point-to-point account, then the examples should show how indexed interest is calculated for a 5-year period.
- If a non-guaranteed element such as a cap is involved in the interest calculation, the value used in the explanation should never be greater than the then-current value in effect for new policies. The minimum guaranteed value for such guaranteed element must be stated.
- If an annuity contract tracks different account values for different benefit streams such that there is more than one indexed interest credit for a given period, then the explanation must depict the calculation of indexed interest for each benefit stream.
- To assure that the explanation is balanced, it should provide examples explaining how interest is calculated under two index scenarios: one with positive indexed interest and one with zero indexed interest. A graphic example will enhance consumer understanding.
  - The positive example should portray a reasonably favorable change in the index constructed to produce an illustrative indexed interest credit equivalent to an annual effective rate of [6%], subject to any lower cap that may apply to the indexed account. If the indexed interest credit covers a time period other than 12 months, the resulting interest credit must also be expressed in terms of an equivalent annual effective rate.
  - The zero example should portray an equally negative index scenario that results in zero indexed interest.

## EXAMPLE 2C

**Template for Depiction of Indexed Interest**

*Example 2C is a template for developing a depiction of how credited interest is calculated for an index annuity. A separate depiction for each indexed account offered under the annuity contract should be attached to the disclosure document as a supplement. Each depiction must include a written explanation of how interest is calculated. A graphic example supporting the explanation enhances consumer understanding.*

**[COMPANY NAME] Depiction of Indexed Interest for the [NAME OF INDEXED ACCOUNT] Offered in the [ANNUITY CONTRACT NAME]**

or

**[COMPANY NAME] Depiction of Indexed Interest for the [ANNUITY CONTRACT NAME]**

This document provides an explanation of how indexed interest is calculated for the [NAME OF INDEXED ACCOUNT].

**Graphic Examples of How Indexed Interest is Calculated**

■ Positive Indexed Interest Result

[INSERT: LINE OR BAR CHART CONTRASTING PERFORMANCE OF INDEX OVER THE CREDITING PERIOD WITH THE INDEXED INTEREST RESULT.] Graphic should be accompanied by a written explanation that explains what index is used, how interest is linked to the index, and what elements of the account are subject to change.

■ Zero Indexed Interest Result

[INSERT: LINE OR BAR CHART CONTRASTING PERFORMANCE OF INDEX OVER THE CREDITING PERIOD WITH THE INDEXED INTEREST RESULT.] Graphic should be accompanied by a written explanation that explains what index is used, how interest is linked to the index, and what elements of the account are subject to change.

EXAMPLE 2D

**Sample of Depiction of Indexed Interest**

The sample shows how indexed interest is credited for an XYZ Life Insurance Company annuity. See page 22 for instructions on how to complete the template for depicting indexed interest.

**Index Annuity Disclosure: Indexed Interest Depiction for the XYZ Index Annuity**

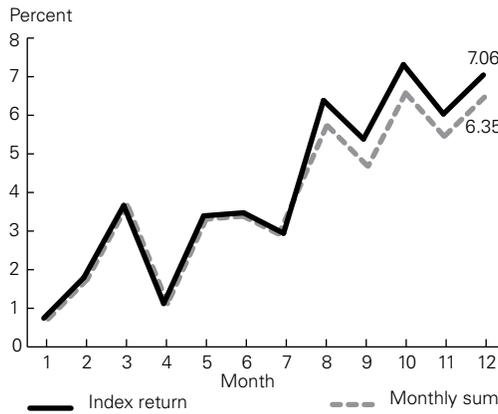


Scenario 1 shows hypothetical index changes for a 12-month period in which the index performed favorably. The index return (solid line) shows the cumulative return that investing directly in the index would have achieved. The dotted monthly sum line represents the cumulative capped monthly sum, compounded, and assuming a 2.8% monthly cap. The cap may vary from year to year, but is guaranteed never to be less than 1.0%. **In scenario 1, the ending monthly sum is 6.35%—the interest rate that would be credited to the index annuity.**

**Example: Favorable index performance**

Month	Monthly index return (percent)	Monthly capped index return (percent)
1	0.70	0.70
2	1.05	1.05
3	1.87	1.87
4	-2.54	-2.54
5	2.27	2.27
6	0.08	0.08
7	-0.53	-0.53
8	3.44	2.80
9	-1.00	-1.00
10	1.94	1.94
11	-1.29	-1.29
12	1.01	1.01
Total (compounded)	7.06	6.35

**Scenario 1: Positive indexed interest**

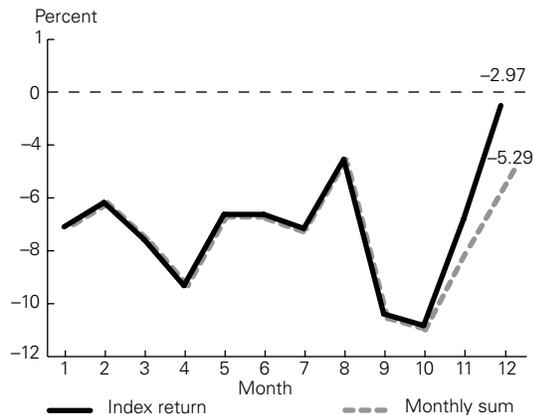


Scenario 2 shows hypothetical index changes for a 12-month period in which the index performed poorly. The solid black index return line represents the cumulative return that investing directly in the index would have achieved. The dotted monthly sum line represents the cumulative capped monthly sum, compounded, and assuming a 2.8% monthly cap. The cap may vary from year to year, but is guaranteed never to be less than 1.0%. **In scenario 2, since the ending monthly sum is negative (-5.29%) at the end of the year, 0 % interest would be credited to the index annuity.**

**Example: Unfavorable index performance**

Month	Monthly index return (percent)	Monthly capped index return (percent)
1	-7.15	-7.15
2	0.92	0.92
3	-1.39	-1.39
4	-1.75	-1.75
5	2.69	2.69
6	1.95	1.95
7	-2.48	-2.48
8	2.61	2.61
9	-6.04	-6.04
10	-0.24	-0.24
11	4.03	2.80
12	4.63	2.80
Total (compounded)	-2.97	-5.29

**Scenario 2: Zero indexed interest**



# **VARIABLE ANNUITY DISCLOSURE MATERIALS**

*How to Complete the Template  
for a Variable Annuity Disclosure*

*Example 3A: Template for a  
Variable Annuity Disclosure*

*Example 3B: Sample of a  
Variable Annuity Disclosure*

## HOW TO COMPLETE THE TEMPLATE FOR A VARIABLE ANNUITY DISCLOSURE

The following is a guide to writing a disclosure for an variable annuity. It includes guidance for writing statements; the types of information that should be covered under each required section, the headings to be used and questions to be answered; and in some cases, provides suggested language that can be used. **Disclosure documents must be prepared consistently with FINRA conduct rule 2210 (Communications to the Public).**

Example 3A on page 29 shows a graphic of a variable annuity disclosure template; Example 3B on pages 30–31 is an example of what an actual product disclosure may look like; Addendum X shows the disclosure document to scale. Companies are encouraged to follow the language used in the sample.

**Note: The variable annuity disclosure document may be presented in two forms: print or electronic. If distributed electronically, in addition to providing direct links to the annuity prospectus or supplement material for more information, companies also should keep references to specific pages (and, if appropriate, headings on that page) in the event consumers prefer to print hard copies.**

### Guide to Writing Disclosure Statements

- Make a clear distinction about whether a statement is true of all annuities (“an annuity”) or all annuities of this type (“a deferred annuity”) or this product (“this annuity,” “this deferred annuity”).
- In a question, refer to the reader as I (my annuity). In the answer, refer to the reader as you (your annuity). Refer to the company as “we” or use the name of the insurance company. Don’t use the generic “insurer” or “company.”
- Avoid statements that don’t give specific information or don’t give the reader information to find specific information. For example, “Interest is credited to your account” is a general statement that isn’t very useful. “Interest is credited to your account daily” is a specific statement of information as is “Page 23 of your annuity prospectus explains the different ways that interest may be credited to your account.”
- Use specific terms (i.e. surrender) from your annuity prospectus in the disclosure but include a definition in parentheses after.
- Put important terms in bold font the first time you use them. Be selective about what terms you consider important. If too many words are in bold, the technique loses its effectiveness.
- If you refer the reader to the annuity prospectus for more information be specific about what information is there and exactly where to find it (e.g. use page numbers or section titles).
- The phrasing “includes” (“Your options include”) suggest there are other options not stated here. If you’ve stated all of the options, say “Your options are.” If you plan to add options later, say, “Your options now are.”
- Use “annuity prospectus” when you’re referring the consumer to the written prospectus.
- Don’t use the word policy to refer to an annuity.
- When possible, present information in a bulleted list with a brief description and refer to a specific page number in the annuity prospectus for more information.

## SECTION 1: INTRODUCTION

- Include your company name and name of the product at the top of the page. A company logo also may be inserted.
- Include statements that briefly explain each of the major features of the annuity. (Suggested language: This annuity is deferred, which means payouts begin at a future date.)
- Specify that this is a variable annuity and include a definition. (Suggested language: This is a variable annuity: the return on your investments will vary with changes in the market OR its value depends on the performance of the investments you chose.)
- Include a statement that the buyer can use an annuity for lifetime income but it is not meant for short-term goals. (Suggested language: You can use an annuity to save money for retirement and to receive retirement income for life. It is not meant to be used to meet short-term financial goals.)
- Specify if the annuity is single-premium or flexible premium. (Suggested language: This annuity is single-premium which means you buy it with one payment (premium) **or** flexible premium which means you can purchase it with multiple payments (premiums)).
- Include information about how the annuity accumulates earnings. For example: This annuity can accumulate earnings in two ways: 1) from various investment choices we offer and 2) from a fixed interest account of XYZ Life Insurance Company.

## SECTION 2: THE ANNUITY CONTRACT

### What are my investment options?

- Explain how the annuity accumulates earnings, clearly distinguishing between guaranteed, non-guaranteed, and determinable elements, including their limitations.
- List how many investment choices are currently available, explain the choices the consumer must make, and refer to the specific pages of the annuity prospectus where detailed information is available. (If the disclosure is online, this section may provide a link to more information about investment choices.)

## SECTION 3: BENEFITS

### What are the benefits of my annuity?

- List and describe the benefits of the annuity and include links, page numbers, or section headings for more information.

Guide to writing statements in this section:

- Use the term premium to refer to money the consumer pays you. Use the term payout to refer to money you pay the consumer.
- Use the same terms that are used in the annuity prospectus for payout options, but include a clear explanation of each.
- If the annuity prospectus uses another term for payout, the first time it appears put the other term in the disclosure followed by payout in parenthesis. After the first time, use the generic term payout.
- When you use a table, explain the table. An example using information from the table is a good way to explain the table.
- Be specific when you refer to the annuity prospectus; include links, page numbers and, if appropriate, headings on that page.

### How do I get income (payouts) from my annuity?

- Mention the various payout options and provide a link to the annuity prospectus, page numbers, or section headings where more information is available.
- Explain what happens if the annuitant doesn't choose a payout option.

## SECTION 4: OPTIONAL BENEFIT RIDERS AND THEIR FEES

### What other benefits can I choose?

- List **all** optional riders, briefly describe each, and include either the range of fees or the maximum fee charged for each option. Include links, page numbers, or section headings and refer to specific

page numbers or section headings in the annuity prospectus and supplement material for more information.

Guide to writing statements in this section:

- Present information in a chart or table.
- Be specific when you refer to the annuity prospectus; include links, page numbers and, if appropriate, section headings on that page.
- Use the same terms used in the annuity prospectus for riders, but include a brief explanation of what the rider offers.

## **SECTION 5: RISKS**

### **What are the risks?**

In this section, describe the types of risks in a bulleted list with a brief description of each. If online, include a link to the relevant information. Also include specific page numbers in the annuity prospectus for more detailed information. This section should describe:

- Risks to guaranteed elements.
- Risks associated with underlying investments.
- Options and restrictions on withdrawing money from the annuity.
- Tax consequences for early withdrawals.

Guide to writing statements in this section:

- Use the terms used in the annuity prospectus for risks, but include a brief explanation of what each risk is.
- Be specific when you refer to the annuity prospectus; include links, page numbers and, if appropriate, headings on that page.

## **SECTION 6: FEES, EXPENSES AND OTHER CHARGES**

### **What happens if I take out some or all of the money from my annuity?**

This section should outline:

- The amount of surrender charges and when they are paid.
- If the variable annuity contract is designed without surrender charges, the question should be answered to indicate that no surrender charges apply under the contract provisions for surrenders.
- Any other charges or adjustments in the amount received when taking money from an annuity.

Guide to writing statements in this section:

- If the annuity prospectus uses another term for surrender charge, the first time it appears in the disclosure, put the other term followed by surrender charge in parentheses. After the first time, use the generic term surrender charge. (Example: XYZ Life Insurance Company takes a contingent deferred sales charge (also known as a surrender charge) ...).
- State surrender charges in a table format and include an example to explain the table.
- Be specific when you refer to the annuity prospectus; include links, page numbers and, if appropriate, headings on that page.

### **What fees or charges do you take from my annuity account value?**

- List and describe contract fees, such as annual contract fees and annual portfolio expenses. You may list the range of each fee or the maximum fee charged for each.

### **Do I pay any other fees or charges?**

- List and describe any other fees or charges that apply, such as maintenance charges or transfer fees. Include links, page numbers, or section headings in the annuity prospectus for more information.

Guide to writing statements in this section:

- A table may be useful to explain fees and charges. If you use a table, include an example to explain the table.

## SECTION 7: TAXES

### How will payouts and withdrawals from my annuity be taxed?

This section should outline:

- The meaning of tax-deferred (Suggested language: Variable annuities are tax-deferred which means you don't pay taxes on accumulated earnings until the money is paid to you. When you take payouts or make a withdrawal, you pay ordinary income taxes on the accumulated earnings. You also defer paying taxes on earnings if you move money from one investment option in your annuity to another. You may pay a 10% federal income tax penalty on earnings you withdraw before age 59 1/2.)
- If your company takes premium taxes from withdrawals or payouts, include a statement describing the deduction. (Suggested language: If your state imposes a premium tax, it will be deducted from the money you receive.)
- That one tax-deferred annuity can be exchanged for another without paying taxes on accumulated earnings. (Suggested language: You can exchange one tax-deferred annuity for another without paying taxes on the accumulated earnings when you make the exchange. Before you do, compare the benefits, features, and costs of the two annuities.)

### Does buying an annuity in a retirement plan provide extra tax benefits?

- Explain that there are no additional tax advantages to buying an annuity in an IRA, 401 (k) plan or other tax deferred retirement product. (Suggested language: Buying an annuity within an IRA, 401(k), or other tax-deferred retirement plan doesn't give you any extra tax benefits. Choose your annuity based on its other features and benefits as well as its risks and costs, not its tax benefits.)

## SECTION 8: OTHER INFORMATION

### What else do I need to know?

All disclosures should include the following statements, modified as needed to match your situation.

#### Changes to your contract

We may change your annuity contract from time to time to follow federal or state laws and regulations. If this happens, we'll tell you about the changes in writing.

#### Compensation

Ask your sales representative how he or she is paid. We pay the sales representative and the firm he or she is associated with for selling this annuity to you. The compensation they receive could create an incentive for recommending one product over another.

#### Free look

Many states have laws that give you a set number of days to look at an annuity after you buy it. If you decide during that time that you don't want it, you can return the annuity and get all your money back. Read your contract [Insert link, page number or section title] or the annuity prospectus [Insert link, page number or section title] to learn about your free look period. (Or replace suggested language with state and company specific information about free look.)

Include in this section other important information that doesn't appear elsewhere.

### What should I know about the insurance company?

Include in this section a general description of the company as well as all contact information, including an address, phone number, Web site, and e-mail address (as applicable). You also may consider including financial strength ratings.

All disclosures should include the following statement, modified as needed to match your situation:

- Note: The about information is current as of the annuity prospectus dated\_\_\_\_. This is a summary document. The prospectus contains important information required under the federal securities laws. If you wish to receive a paper copy of the prospectus and supplement material, click here or call 800-123-4567. There is no charge for paper copies.

## EXAMPLE 3A

**Template for a Variable Annuity Disclosure**

Example 3A shows how to group disclosure material into sections and in two-column format. Disclosure documents should be kept short. The template also includes the section headings that are to be used, the questions that need to be answered, and provides direction. Refer to the accompanying instructions for more information about how to complete the template and for suggested language. Disclosure documents must be prepared consistently with FINRA conduct rule 2210 (Communications to the Public).

**Note:** The variable annuity disclosure document may be presented in two forms: print or electronic. If distributed electronically, in addition to providing links to the prospectus, keep references to specific pages in case consumers choose to print hard copies.

SECTION 1

**[COMPANY NAME]****[PRODUCT NAME] Disclosure**

[STATE COMPANY NAME AND NAME OF PRODUCT. SPECIFY IF THE ANNUITY IS A SINGLE- OR FLEXIBLE- PREMIUM. INCLUDE STATEMENTS THAT BRIEFLY EXPLAIN MAJOR FEATURES AND HOW THE ANNUITY ACCUMULATES EARNINGS. DISCLOSE THAT THE ANNUITY IS NOT MEANT TO BE USED TO MEET SHORT-TERM GOALS. SUGGESTED LANGUAGE PROVIDED IN THE ACCOMPANYING INSTRUCTIONS.]

SECTION 2

**THE ANNUITY CONTRACT****What are my investment options?**

[EXPLAIN THE CHOICES THE CONTRACT OWNER MUST MAKE, INCLUDING HOW MANY INVESTMENT OPTIONS ARE AVAILABLE AND THEIR VARYING DEGREES OF RISK AND THE CURRENT RATE OF THE FIXED ACCOUNT.]

**BENEFITS****What are the benefits of my annuity?**

[LIST AND DESCRIBE THE ANNUITY'S BENEFITS.]

**How do I get income (payouts) from my annuity?**

[DESCRIBE VARIOUS PAYOUT OPTIONS.]

SECTION 3

**OPTIONAL BENEFIT RIDERS****What other benefits can I choose?**

[LIST AND DESCRIBE ALL OPTIONAL RIDERS. INCLUDE EITHER THE RANGE OR MAXIMUM FEE CHARGED FOR EACH.]

SECTION 4

**RISKS****What are the risks?**

[LIST AND DESCRIBE RISKS TO GUARANTEED ELEMENTS, RISKS ASSOCIATED WITH THE UNDERLYING INVESTMENTS, RESTRICTIONS ON WITHDRAWING MONEY, AND TAX LIABILITIES FOR EARLY WITHDRAWALS.]

SECTION 5

**FEES, EXPENSES AND OTHER CHARGES****What happens if I take out some or all of the money from my annuity?**

[STATE SURRENDER CHARGES AND PROVIDE AN EXAMPLE.]

SECTION 6

**What fees or charges do you take from my annuity account value?**

[LIST AND DESCRIBE CONTRACT FEES AND PROVIDE AN EXAMPLE.]

**Do I pay any other fees or charges?**

[LIST AND DESCRIBE ANY OTHER FEES OR CHARGES THAT APPLY.]

**TAXES****How will payouts and withdrawals from my annuity be taxed?**

[DESCRIBE THE MEANING OF TAX-DEFERRED. INCLUDE A STATEMENT DESCRIBING ANY DEDUCTION TAKEN FOR PREMIUM TAXES. EXPLAIN TAX TREATMENT OF EXCHANGES. SUGGESTED LANGUAGE PROVIDED IN THE ACCOMPANYING INSTRUCTIONS.]

**Does buying an annuity in a retirement plan provide extra tax benefits?**

[EXPLAIN THAT THERE ARE NO ADDITIONAL TAX BENEFITS. SUGGESTED LANGUAGE PROVIDED IN THE ACCOMPANYING INSTRUCTIONS.]

SECTION 7

**OTHER INFORMATION****What else do I need to know?****Changes to your contract**

[INCLUDE A STATEMENT EXPLAINING THAT THE CONTRACT OWNER WILL BE NOTIFIED IN WRITING OF ANY CHANGES TO THE CONTRACT. SUGGESTED LANGUAGE PROVIDED IN THE ACCOMPANYING INSTRUCTIONS.]

**Compensation**

[INCLUDE A STATEMENT EXPLAINING THAT THE COMPENSATION RECEIVED BY THE SALES REPRESENTATIVE COULD CREATE AN INCENTIVE FOR RECOMMENDING ONE PRODUCT OVER ANOTHER. SUGGESTED LANGUAGE PROVIDED IN THE ACCOMPANYING INSTRUCTIONS.]

**Free Look**

[INCLUDE STATE AND COMPANY SPECIFIC INFORMATION ABOUT FREE LOOK. SUGGESTED LANGUAGE PROVIDED IN THE ACCOMPANYING INSTRUCTIONS.]

SECTION 8

**What should I know about the insurance company?**

[PROVIDE RELEVANT COMPANY INFORMATION, INCLUDING ADDRESS, PHONE NUMBER, WEBSITE. ALSO INCLUDE THE FOLLOWING STATEMENT, MODIFIED TO MEET SPECIFIC COMPANY SITUATION: *Note: the above information is current as of the annuity prospectus dated \_\_\_\_\_. This is a summary document. The annuity prospectus contains important information required under the federal securities laws. If you wish to receive a paper copy of the prospectus and supplement material, [click here](#) or call 800-123-4567. There is no charge for paper copies.*]

## EXAMPLE 3B

**Sample of a Variable Annuity Disclosure**

Example 3B is a sample of how a final disclosure document might look. Addendum X shows document to scale. This is a only a sample and is not intended to serve as a model disclosure for all types of annuities. Disclosure documents for each company and product will vary. Disclosure documents must be prepared consistently with FINRA conduct rule 2210 (Communications to the Public).

**Note: The variable annuity disclosure document may be presented in two forms: print or electronic. If distributed electronically, in addition to providing links to the prospectus, keep references to specific pages in case consumers choose to print hard copies.**

**Variable Annuity Disclosure**

This document reviews important points to think about before you buy this XYZ Life Insurance Company annuity. This variable annuity is a contract between you and our company. It is a single-premium annuity which means you buy it with one payment (premium).

This annuity is deferred, which means payouts begin at a future date. You can use an annuity to save money for retirement and to receive retirement income for life. It is not meant to be used to meet short-term financial goals. You may pay a fee if you take out money before the end of a time period specified by the contract.

This annuity is variable, which means its value depends on the performance of the investments you chose. This annuity can accumulate earnings in two ways: 1) from various investment choices we offer and 2) from a fixed interest account of XYZ Life Insurance Company.

**If you have questions about this annuity, please ask your agent, broker, advisor, or contact a company representative at 800-123-4567.**

**THE ANNUITY CONTRACT****What are my investment options?**

You can invest your money in our fixed interest account and in any or all of the investment choices we offer. Click on the links below or refer to pages of the annuity prospectus for more information about your choices.

- **Investment choices:** You may choose from 41 fund portfolios that have different investment objectives and levels of risk (see page 13).
- **Fixed account:** This choice offers a guaranteed rate of return, which currently is 3% (see page 12).

**BENEFITS****What are the benefits of my annuity?**

The benefits of your annuity are described below. Click on the links provided or read the section of the annuity prospectus for more information.

- **Death benefits:** This annuity includes a death benefit that will be paid to your beneficiary if you die before your income payouts begin. This benefit equals either your premium minus any withdrawals or the contract value, whichever is greater (see page 28).
- **Nursing care and terminal condition withdrawal:** If you or your spouse are in a hospital or nursing facility for 30 consecutive days or diagnosed with a terminal condition after the annuity was issued, you can take money from your annuity without paying a fee (see page 37).
- **Unemployment waiver:** If you (or your spouse) become unemployed, you won't pay fees when you take out money if certain conditions defined in the contract are met (see page 37).
- **Systematic payout option:** You can get monthly, quarterly, or annual payouts from your annuity in set amounts at any time without paying certain fees (see page 34).

**What types of income (payouts) can I get from my annuity?**

You can choose to get payouts for you and a joint annuitant for life or for a specific period of time or you can choose a lump sum payout. (Pages\_\_ explain your payout options.)

**OPTIONAL BENEFIT RIDERS AND FEES****What other benefits can I choose?**

The contract also offers other benefits for an extra cost. Your choices and the fees charged are described below. You will pay a fee for each option you choose every year you own the annuity. The fee is calculated as a percentage of the value of your investments. Click on the links or refer to pages in the annuity prospectus and supplement material for more information, [including how fees are calculated.](#)

**Annual Fees for Optional Benefit Riders**

<b>Additional Death Benefit Riders</b>	<b>CURRENT</b>	<b>MAXIMUM</b>
<a href="#">Additional Death Distribution Option</a> Pays your beneficiary an extra death benefit in specific situations (description of benefit: supplement pages 35-36; explanation of fee: supplement page 23).	.20%	20%
<b>Living Benefit Riders</b>	<b>CURRENT</b>	<b>MAXIMUM</b>
<a href="#">Guaranteed Minimum Accumulation Benefit:</a> Guarantees a future value of your annuity no matter how the investment options you choose perform (description of benefit: supplement pages 4-5; explanation of fee; supplement pages 7-8).	.40%	.50%
<a href="#">Guaranteed Minimum Withdrawal Benefit:</a> Guarantees an annual amount you can take out of your annuity regardless of its value (description of benefit: supplement pages 5-7; explanation of fee; supplement pages 7-8).	.50% (single) .85% (joint)	1.00%

**RISKS**

This annuity has several risks. Click on the links below or read the annuity prospectus for more information about:

- **Risks of your annuity contract:** There's a risk that we won't be able to pay claims on guaranteed annuity contract benefits, such as the guaranteed minimum accumulation value (see page 12).
- **Risks based on the investment portfolio you choose:** The investments you choose may decrease in value; if any of them do, the value of your annuity will go down. You may lose money if you take money out in whole or in part when the value is down (see pages 15–16).
- **Access to your money:** You may pay a fee (surrender charge) if you take out money before the end of the fifth contract year (see the next section of this disclosure or pages 24–25).
- **Your tax liability:** You may pay a 10% federal income tax penalty on earnings in addition to taxes due on earnings if you withdraw money before age 59 1/2 (see section on "Taxes" or pages 29–34).

**CONTRACT FEES, EXPENSES AND OTHER CHARGES**

**What happens if I take out some or all of the money from my annuity?**

You may pay a surrender charge if you take out money before the end of the fifth contract year. Here's how the charge is calculated.

Contract Year	1	2	3	4	5	6+
<b>Surrender Charge</b>	5%	4%	3%	2%	1%	0

Example: If you withdraw \$5,000 from your annuity in the third contract year, your surrender charge is \$5,000 x .03 = \$150. If you take out any amount after the end of the fifth contract year, there's no charge.

You may not have to pay a surrender charge if you take out part of your money (a partial surrender). [Click here](#) or see pages 20–21 of the annuity prospectus for more information about surrender charges.

**What fees or charges do you take from my annuity account value?**

You will pay fees every year you own the annuity. The fees are calculated as a percentage of the contract's value.

**Annual Contract Fees**

(not including fees for optional riders)

	Current	Maximum
Mortality and expense risk	.95%	1.35%
Administrative	.10%	.15%
<b>Total annual contract fees</b>	<b>1.50%</b>	<b>2.27%</b>

**Example: Cost Based on Annual Contract Fees**

Investment value	Current (1.50%)	Maximum (2.27%)
\$1,000	\$15.00	\$22.70
\$50,000	\$759.00	\$1,135.00
\$100,000	\$1,500.00	\$2,270.00

**Total Annual Portfolio Operating Fees**

Minimum	.85%	Maximum	1.42%
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**Example: Cost Based on Annual Portfolio Operating Fees**

Investment value	Minimum	Maximum
\$1,000	\$8.50	\$14.50
\$50,000	\$425.00	\$710.00
\$100,000	\$850.00	\$1,420.00

**Do I pay any other fees or charges?**

There's also an annual service charge. We will tell you the amount of the service charge (between \$0 and \$35 per annuity) each year. There may be other charges in some cases. You may pay a contract maintenance or transfer fee. The maintenance fee is waived if the contract value is more than \$50,000 on the contract anniversary or at the time of surrender. You also pay a fee for each optional rider you choose (see section on optional benefit riders and fees). [Click here](#) or see page 10 of the annuity prospectus for more information about fees and charges.

**TAXES**

**How will payouts and withdrawals from my annuity be taxed?**

Variable annuities are tax-deferred, which means you don't pay taxes on the annuity's accumulated earnings until the money is paid to you. When you take payouts or make a withdrawal, you pay ordinary income taxes on the accumulated earnings. You also defer paying taxes on earnings if you move money from one investment option in your annuity to another. You may pay a 10% federal income tax penalty on earnings you withdraw before age 59 1/2. If your state imposes a premium tax, it will be deducted from the money you receive.

You can exchange one tax-deferred annuity for another without paying taxes on the accumulated earnings when you make the exchange. Before you do, compare the benefits, features, and costs of the two annuities.

**Does buying an annuity in a retirement plan provide extra tax benefits?**

Buying an annuity within an IRA, 401(k), or other tax-deferred retirement plan doesn't give you any extra tax benefits. Choose your annuity based on its other features and benefits as well as its risks and costs, not its tax benefits.

**OTHER INFORMATION****What else do I need to know?**

**Changes to your contract:** We may change your annuity contract from time to time to follow federal or state laws and regulations. If we do, we'll tell you about the changes in writing.

**Compensation:** Ask your sales representative how he or she is paid. We pay the sales representative and firm he or she is associated with for selling this annuity to you. The compensation they receive could create an incentive for recommending one product over another.

**Free Look:** Many states have laws that give you a set number of days to look at an annuity after you buy it. If you decide during that time that you don't want it, you can return the annuity and get all your money back. Read your contract (page \_\_\_) **or see page \_\_\_ of the annuity prospectus** to learn about your free look period.

**What should I know about the insurance company?**

XYZ Life Insurance Company offers a wide variety of retirement and financial security products, including life insurance, annuities, long-term care, and disability income insurance. We also are a leading provider of products and services to workplace-based pension plans—both defined contribution and defined benefit plans. Our financial strength is as follows: A+ (A.M. Best); AA (S&P); Aa3 (Moody's); and AA+ (Fitch).

XYZ Life Insurance Company  
123 Main Street  
Your Town USA  
Telephone: 800-123-4567  
www.XYZlife.com

Note: The above information is current as the annuity prospectus dated May 1, 2006. This is a summary document. The prospectus contains important information required under the federal securities laws. If you wish to receive a paper copy of the prospectus and supplement material, click here or call 800-123-4567. There is no charge for paper copies.



**AMERICAN COUNCIL OF LIFE INSURERS**  
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## **A Comprehensive System of State Regulation Governs the Distribution of Insurance and Annuity Contracts**

Carl B. Wilkerson, Vice President & Chief Counsel-Securities & Litigation  
American Council of Life Insurers © 2010 All Rights Reserved.

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### **A. STATE INSURANCE REGULATION**

Through a network of statutes and regulations, state insurance departments heavily regulate the operations, products, and sales of life insurance companies. Life insurers and their salespersons must satisfy this regulatory structure in their state of domicile and every jurisdiction in which they distribute life insurance and annuities. Uniformity of regulation is accomplished throughout the states by means of model statutes and regulations promulgated by the National Association of Insurance Commissioners (the "NAIC"). Many of the insurance statutes and regulations promulgated and enforced by state insurance departments fulfill regulatory goals quite similar to those of the state securities administrators. The summary below highlights the broad scope and comprehensiveness of certain state insurance statutes and regulations. While only a small portion of the larger universe of state insurance regulation, these regulations are directly relevant in evaluating the market conduct structure governing insurance salespersons engaged in the delivery of financial planning and broker-dealer services. This discussion is intended to fill in other areas not covered in the preceding outline materials to this submission.

#### **UNFAIR TRADE PRACTICES**

Virtually every state has enacted a version of the NAIC Model Unfair Trade Fair Practices Act which was developed to regulate trade practices in the insurance business by defining and prohibiting practices that constitute unfair methods of competition or unfair deceptive acts or practices.<sup>1</sup>

A variety of the activities defined to be unfair trade practices directly parallel the purpose and scope of state securities codes. Section 4(A) involves misrepresentations and false advertising of insurance policies, and identifies unfair trade practices to include any estimate, illustration, circular or statement, sales misrepresentation, omission or comparison that misrepresents the benefits, advantages, conditions or terms of any policy, among other things.

Section 4(B) involves false information and advertising generally. This provision defines an unfair trade practice to include making, publishing or disseminating in a newspaper, magazine or other publication, on any radio/television station any assertion, representation or statement about an insurer or its business, which is untrue, deceptive or misleading.

Knowingly making any false statement of any material fact to insurance regulators, or in documents that will be publicly disseminated, is defined to be an unfair trade practice in Section 4(B) of the Model Unfair Trade Practices Act. This proscription is consistent with the

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<sup>1</sup>This model statute governs items previously subject to Section 5 of The Federal Trade Commission Act. Congress observed that continued regulation of insurance by the states was in the public interest. See, legislative history of NAIC Unfair Trade Practices Act, NAIC Model Regulation Service at 880-20(1993).

truthfulness and accuracy of reports, records and representations required of Broker/Dealers by the NASD and the SEC under the federal securities laws.

Section 4(J) involves the failure to maintain marketing and performance records, and defines as an unfair trade practice the failure of an insurer to maintain its books, records, documents, and other business records in such an order that data regarding complaints, claims, reading, underwriting and marketing are accessible and retrievable for examination by the insurance commissioner. Data for at least the current calendar year in the two preceding years must be maintained under this standard. This provision directly parallels the scope and purpose of NASD Conduct Rule 3110 regarding books and records.

Section 4(K) defines the failure of any insurer to maintain a complete record of all the complaints it received since the date of its last market conduct examination to be an unfair trade practice. The records of complaints must indicate the total number of complaints, their classification by line of insurance, the nature of each complaint, the disposition of each complaint and the time it took to process each.<sup>2</sup> For purposes of this subsection, the term “complaint” means any written communication primarily expressing a grievance.

Like state securities administrators, insurance commissioners have the power to examine and investigate the affairs of every insurer operating in the insurance department’s state “in order to determine whether such insurer has been or is engaged in any unfair trade practice prohibited by [the Unfair Trade Practices Act].”<sup>3</sup> Several provisions embellish this important authority.

For example, Section 7 of the Unfair Trade Practices Act gives insurance commissioners extensive authority to initiate hearings concerning unfair trade practices, to compel witnesses, appearances, production of books, and service of process. Section 7 sets forth detailed administrative and procedural practices, in order to assure due process and quasi-judicial formality.

Section 8 of the Unfair Trade Practices statute authorizes insurance commissioners finding insurers guilty of unfair trade practices to issue written findings and enforcement orders requiring the insurer to cease and desist from engaging in the act or practice. The insurance commissioner also has the discretionary authority to suspend and revoke the insurer’s license if the insurer knew or reasonably should have known that its conduct violated the Unfair Trade Practices Act, and to order penalties of \$1,000 for each violation up to an aggregate penalty of \$100,000, unless the violation was committed flagrantly in conscious disregard of the act, in which case the penalty may be up to \$25,000 for each violation to an aggregate total penalty of \$250,000. A similar monetary violation may be imposed under Section 11 for violations of cease and desist orders. The act also provides for judicial review of insurance commissioner orders and authorizes immunity from prosecution for witnesses who attend, testify or produce books, records or other paper correspondence.<sup>4</sup>

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<sup>2</sup>The NAIC has also promulgated a Model Regulation for Complete Records to be maintained pursuant to Section 4(K) of the NAIC Unfair Trade Practices Act. See, NAIC Model Regulation Service at 844-1(1992). This regulation sets forth a complaint record form, content requirements, maintenance requirements, and standards concerning the format of complaint records.

<sup>3</sup> See Section 6, Power of Commissioner, Model Unfair Trade Practices Act, NAIC Model Regulation Service at 880-9(1993).

<sup>4</sup> See Sections 8, 9, 10, 11 and 14 of the Model Unfair Trade Practices Act, NAIC Model Regulation Service at 880-10 through 13(1994).

These significant powers that may be used by insurance commissioners to enforce violations of unfair trade practice proscriptions, together with the recordkeeping, reporting and inspection powers of the Act, provide a package of regulatory tools directly analogous to state securities codes, the NASD Rules of Conduct and SEC regulations governing market conduct practices and the prosecution of violations. In a sum, the unfair trade practice laws provide meaningful proscriptions that eliminate the need for duplicative regulation of variable contracts.

### **NAIC MODEL FRAUD LAWS AND FRAUD LEGISLATION**

Enactment of state fraud statutes represents another significant insurance regulatory development. Recent market conduct issues have resulted in some insurance departments requiring insurer management to assume increased responsibility for supervision of sales activities. Other states have taken an approach similar to that of New York and Pennsylvania by requiring insurer review of market conduct compliance, thus placing direct responsibility at the corporate officer level. This widespread action dovetails with the objectives of the Federal Crime Control Statute and the Federal Sentencing guidelines, discussed below.

While states have taken different approaches to the issue, the majority of states addressing the fraud issue enacted legislation similar to the NAIC Model Fraud Laws.<sup>5</sup>

### **MARKET CONDUCT EXAMINATIONS**

Nearly every jurisdiction has enacted a version of the NAIC Model Law on Examinations.<sup>6</sup> This Act is designed to provide an effective and efficient system for examining the activities, operations, financial condition and affairs of all persons transacting the business of insurance in each state and concerning individuals otherwise subject to the insurance commissioner's jurisdiction. The Act is intended to enable commissioners to adopt a flexible system of examinations and allocate resources deemed appropriate and necessary for the administration of the insurance laws of each state. The Model Law on Examinations sets forth standards for the conduct of examinations, commissioner authority, scope, and scheduling of examinations. It also details the scope of examination reports which shall be comprised of only facts appearing on books, records or other documents of the company, its agents or other persons examined or as ascertained from the testimony of its officers or agents or other persons examined.<sup>7</sup>

Significantly, this Model Act dovetails with the NAIC Market Conduct Examiner's Handbook, an extremely detailed manual for examiners to assure that examiners follow comprehensive, uniform practices and procedures. The Examiner's Handbook is divided into seven different sections and contains 58 different standards. Among other things, the Examiner's Handbook addresses complaint handling, marketing and sales, producer licensing, and company operations/management.<sup>8</sup>

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<sup>5</sup> See NAIC Insurance Fraud Prevention Model Act, NAIC Model Reporting Service at 680-1(1995).

<sup>6</sup> See NAIC Model Regulation Service at 390-1(1991).

<sup>7</sup> See Sections 3, 4, and 5 of the Model Law on Examinations, NAIC Model Regulation Service at 390-5 (1991). Section 5 also sets forth detailed provisions for orders and administrative procedures in the conduct of hearing and adoption of a report on examination.

<sup>8</sup> Certain standards under the complaint handling section illuminate the depth and scope of the market conduct examination. Several standards are set forth below in this note as representative examples.

Throughout most of 1995 and 1996, the NAIC significantly revised the Market Conduct Examiner's Handbook. The NAIC, together with industry input, sought to expand and enhance tools fostering the detection and prevention of marketplace abuse in the life insurance industry. Market conduct examinations are extremely comprehensive and serve as a means of positive reinforcement, by discouraging deficient practices that will be detected on examination, resulting in remedial action, and insurance department intervention.

## **AGENTS LICENSING AND TESTING**

The NAIC Agents and Brokers Licensing Model Act,<sup>9</sup> which appears virtually in every state, governs the qualifications and procedures for licensing insurance and annuity agents and brokers. This model law sets forth examination and licensing standards in great detail, and has a specific category for variable annuities and variable life insurance contracts. Licensed salespeople must be deemed by the insurance commissioner to be competent, trustworthy,

### **Complaint Handling-Standard 2**

The company has adequate complaint handling procedures in place and communicates such procedures to policyholders.

#### **Review Procedures and Criteria**

Review manuals to verify complaint procedures exist. Procedures in place should be sufficient to require satisfactory handling of complaints received as well as internal procedures for analysis in areas developing complaints. There should be a method for distribution of and obtaining and recording response to complaints. This method should be sufficient to allow response within the time frame required by state law.

Company should provide a telephone number and address for consumer inquiries.

### **Complaint Handling-Standard 3**

The company should take adequate steps to finalize and dispose of the complaint in accordance with applicable statutes, rules and regulations and contract language.

#### **Review Procedures and Criteria**

Review complaints documentation to determine if the company response fully addresses the issues raised. If the company did not properly address/resolve the complaint, the examiner should ask company what corrective action it intends to take.

#### **Commentary:**

Reference to the examiner's general instructions on Handbook page VIII-14 (November 1995) reveals that an inquiry broader in scope than the mere resolution of a given complaint is expected. For example, the Handbook contains the following instructions: "The examiner should review the frequency of similar complaints and be aware of any pattern of specific type of complaints....Should the types of complaints generated be cause for unusual concern, specific measures should be instituted to investigate other areas of the company's operation."

### **Complaint Handling-Standard 4**

The time frame within which the company responds is in accordance with applicable statutes, rules, and regulations.

#### **Review Procedures and Criteria**

Review complaints to ensure company is maintaining adequate documentation. Determine if the company response is timely. The examiner should refer to state laws for the required time frame.

<sup>9</sup>See NAIC Model Regulation Service at 210-1 (2008).

financially responsible, and of good personal and business reputation. Insurance brokers must also fulfill experience requirements. Section 8 of this regulation governs license denial, non-renewal and termination, giving the insurance commissioner broad discretion to suspend, revoke or refuse to issue or renew a license upon finding any of a variety of conditions including materially untrue statements, violation or noncompliance with insurance laws, withholding, misappropriating or converting customer moneys, conviction of a felony or misdemeanor involving moral turpitude, forgery, or cheating on licensing examinations, among other things.

### **CONTINUING EDUCATION**

In granting insurance agents and brokers licenses, most states also impose significant continuing education standards that parallel in objective and scope the continuing education standards recently developed by the securities industry together with the NASD. As in other areas seeking uniformity, the NAIC has promulgated the Agents and Brokers Licensing Model Act.<sup>10</sup> Under Section 5 of this model regulation, licensed agents must annually satisfy courses or programs of instruction approved by insurance commissioners in each state according to a minimum number of classroom hours, which typically is in the range of 25 class room hours per year for life and annuity salespersons. The courses include those presented by the Life Underwriter Training Council Life Course Curriculum, the American College's Chartered Life Underwriter and Chartered Financial Planner curriculum, and the Insurance Institute of America's programs in general insurance, for example. Like the NASD, state insurance regulators understand that testing, licensing and demonstration of continued competence through continuing education is critically important in the distribution of insurance and annuity products.

### **VARIABLE CONTRACT STATUTES**

Life insurance companies are authorized to issue separate accounts funding variable life insurance and annuity contracts upon fulfilling a variable contract statute in their domestic state, which typically follows the NAIC Model Variable Contract Law.<sup>11</sup> This NAIC model statute gives the insurance commissioner exclusive authority to regulate the issuance and sale of variable contracts and to issue rules and regulations appropriate to carry out the act's purpose. This model act and associated regulations that appear under state insurance law gives an additional, important measure of regulatory scrutiny and purchaser protection.

Collectively, the NAIC statutes and regulations provide a significant network of comprehensive regulation over many important aspects affecting the marketing and sale of variable contracts that closely reflect the purpose and scope of analogous concepts of securities regulation.

### **INSURANCE PRODUCER DATABASE**

From a market conduct perspective, life insurers have committed to a single, industry-accessible national producer database to facilitate their ability to track pertinent information regarding licensed producers. Access to information having a bearing on the producer's background, qualifications and competency is a valuable tool to insurers in the employment/appointment screening process. Moreover, widespread availability of such information makes it more difficult for a producer with significant disciplinary history to continue illegal or unethical practices by "company jumping."

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<sup>10</sup> See NAIC Model Regulation Service at 215-1 (1990).

<sup>11</sup> See NAIC Model Regulation Service at 260-1 (1984).

NIPR ([National Insurance Producer Registry](#)) is a non-profit affiliate of the National Association of Insurance Commissioners (NAIC). It was created in October 1996 to develop and operate a national repository for producer license information (PDB) and to establish a network to facilitate the electronic exchange of producer information.

The Producer Database (PDB) is an electronic database consisting of information relating to insurance agents and brokers (producers) accessible through the NIPR Gateway on a subscription basis through the Internet. Internet PDB links participating state regulatory licensing systems into one common system establishing a repository of producer information. Internet PDB also contains or references producer information from sources such as the Regulatory Information Retrieval System (RIRS) of the NAIC. Its development is based, in part, on the belief that the widespread availability of such information will make it more difficult for a producer with significant disciplinary history to continue illegal or unethical practices.

The NIPR Gateway is an electronic communication network that links state insurance regulators with the entities they regulate to facilitate the electronic exchange of producer information; including license applications, appointments, and terminations. To date, data standards have been developed for the exchange of appointment and not-for-cause termination information. All data flowing through the NIPR Gateway will conform to these standards.

Through Internet PDB, industry is able to access all public information related to a producer provided by participating states, including licensing, demographics and final regulatory actions. The product is designed to assist insurers in exercising due diligence in the monitoring of agents and brokers to reduce the incidence of fraud. Currently, Internet PDB contains information on over 2.9 million producers. Information available includes:

- Demographics-name, date of birth, addresses
- License Summary-state of license, license number, issue date, expiration date, license type/class, residency, lines of authority, status, status reason, status/reason effective date.
- Continuing Education-CE compliance indicator, CE renewal date, CE credits needed.
- Certificates and Clearance-date issued, issuing state, receiving state, certification or clearance indicator.
- Regulatory Actions-State of action, entity role, origin of action, reason for action, enter date penalty/fine/forfeiture, effective date, file reference, time/length of dates.
- Appointment Information-Effective date, termination date, reasons for termination.

Currently all 50 states, DC and PR participate in the PDB.

In many respects, this new producer data base parallels the purpose and scope of FINRA's Central Records Depository or CRD. Through the NIPR data base, problem producers can be tracked and deterred from the insurance business.

### C. FEDERAL STATUTE ENHANCING COMPLIANCE PROCEDURES AND MARKET CONDUCT

The *Federal Violent Crime Control Act of 1994* ("The Act"), and the *Federal Sentencing Guidelines for Organizations* have an important impact on the prevention of abusive sales practices. Together, these statutes provide material protections for qualified plans and their participants.

Several provisions in the *Federal Violent Crime Control Act of 1994*<sup>12</sup> relate to sales practices within the insurance industry. The law punishes with fines and a jail term up to five years anyone who *participates* in the business of insurance and has been convicted of a felony involving dishonestly or a breach of trust. Likewise anyone convicted of violating the Act itself cannot participate in the business of insurance and is punished with fines and jail. There are fines and jail terms for anyone who willfully allows a person to participate in the business of insurance who has been convicted of a felony involving dishonesty or a breach of trust. Consequently, anyone who willfully *allows* a person who has been convicted of a felony involving dishonesty or a breach of trust to participate in the business of insurance will be prohibited from participating in the business of insurance themselves.

The law applies to all insurance companies, regardless of the lines of business sold or the state of domicile. Persons who "*participate*" in the business of insurance include officers, directors, agents, employees, or persons authorized to act on behalf of such persons. The "*willfully permits*" language means that even if the felony was before the effective date, that person cannot be allowed to continue to participate in the business.

The Federal Crime Control Statute imposes an important prophylactic parallel to the NASD's barrier to statutorily disqualified individuals in the broker/dealer industry. This protection applies to all life and annuity sales, including variable annuities marketed to qualified plans.

Importantly, the *Sentencing Reform Act of 1984* has made a dramatic change in the federal court sentencing system since its enactment.<sup>13</sup> Essentially, the law provides that evidence of effective compliance programs will be regarded favorably as mitigating factors in the imposition of sentence upon a conviction for criminal behavior. The guidelines as provided in the *United States Sentencing Commission Guidelines Manual: Sentencing of Organizations*, are:

"An effective program to prevent and detect violations of law means a program that been reasonably designed, implemented, and enforced so that it generally will be effective in preventing and detecting criminal conduct. Failure to prevent or detect the instant offense, by itself, does not mean that the program was not effective. The hallmark of an effective program to prevent and detect violations of law is that the organization exercised due diligence in seeking to prevent and detect criminal conduct by its employees and other agents. Due diligence requires at a

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<sup>12</sup>Ch. 47, Title 18, U.S.C. at subsection 1033 (1996).

<sup>13</sup>The particular provisions noted above are from the *Organizational Sentencing Guidelines*, and took effect on November 1, 1991.

minimum that the organization must have taken the following types of steps:

- (1) The organization must have established compliance standards and procedures to be followed by its employees and other agents that are reasonably capable of reducing the prospect of criminal conduct.
- (2) Specific individual(s) within high-level personnel of the organization must have been assigned overall responsibility to oversee compliance with such standards and procedures.
- (3) The organization must have used due care not to delegate substantial discretionary authority to individuals whom the organization knew, or should have known through the exercise of due diligence, had a propensity to engage in illegal activities.
- (4) The organization must have taken steps to communicate effectively its standards and procedures to all employees and other agents, *e.g.*, by requiring participation in training programs or by disseminating publications that explain in a practical manner what is required.
- (5) The organization must have taken reasonable steps to achieve compliance with its standards, *e.g.*, by utilizing monitoring and auditing systems reasonably designed to detect criminal conduct by its employees and other agents and by having in place and publicizing a reporting system whereby employees and other agents could report criminal conduct by others within the organization without fear of retribution.
- (6) The standards must have been consistently enforced through appropriate disciplinary mechanisms, including, as appropriate, discipline of individuals responsible for the failure to detect an offense. Adequate discipline of individuals responsible for an offense is a necessary component of enforcement; however, the form of discipline that will be appropriate will be case specific.
- (7) After an offense has been detected, the organization must have taken all reasonable steps to respond appropriately to the offense and to prevent further similar offenses -- including any necessary modifications to its program to prevent and detect violations of law."

Significantly, organizations are now strongly motivated to establish compliance standards and procedures and to monitor those procedures through a self evaluative process. Through this process, corporations can reduce exposure to liability, both criminally and civilly. Insurance and annuity consumers benefit from these initiatives.

## **NAIC Model Regulation on the Use of Senior-Specific Certifications and Professional Designations in the Sale of Life Insurance and Annuities**

Carl B. Wilkerson, Vice President & Chief Counsel-Securities & Litigation American Council of Life Insurers © 2010 All Rights Reserved.

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### **I. On July 15, 2008, the NAIC Life Insurance and Annuities (A) Committee adopted a new Model Regulation on the Use of Senior-Specific Certifications and Professional Designations in the Sale of Life Insurance and Annuities.**

- A. This NAIC regulation directly parallels the North American Securities Administrators Association (NASAA) credentialing regulations and was developed in close coordination with NASAA and supported by NASAA.
- B. See [http://www.nasaa.org/content/Files/Senior\\_Model\\_Rule110807.pdf](http://www.nasaa.org/content/Files/Senior_Model_Rule110807.pdf)
- C. The NAIC regulation and an accompanying bulleting can be obtained on the NAIC website at [http://www.naic.org/Releases/2008\\_docs/senior\\_sales.htm](http://www.naic.org/Releases/2008_docs/senior_sales.htm) .

### **II. Purpose of the NAIC Regulation**

- A. The regulation establishes standards to protect consumers from misleading and fraudulent marketing practices with respect to the use of senior-specific certifications and professional designations in the solicitation, sale or purchase of, or advice made in connection with, a life insurance or annuity product.
- B. The regulation will apply to any solicitation, sale or purchase of, or advice made in connection with, a life insurance or annuity product by an “insurance producer,” that is defined as a person required to be licensed under the laws of this State to sell, solicit or negotiate insurance, including annuities.

### **III. Prohibited Uses of Senior-Specific Certifications and Professional Designations [Section 5]**

- A. Under the regulation, it will be an unfair and deceptive act or practice in the business of insurance within the meaning of the Unfair Trade Practices Act for an insurance producer to use a senior-specific certification or professional designation that indicates or implies in such a way as to mislead a purchaser or prospective purchaser that insurance producer has special certification or training in advising or servicing seniors in connection with the solicitation, sale or purchase of a life insurance or annuity product or in the provision of advice as to the value of or the advisability of purchasing or selling a life insurance or annuity product, either directly or indirectly through publications or writings, or by issuing or promulgating analyses or reports related to a life insurance or annuity product.

B. The prohibited use of senior-specific certifications or professional designations includes, but is not limited to, the following:

1. Use of a certification or professional designation by an insurance producer who has not actually earned or is otherwise ineligible to use such certification or designation;
2. Use of a nonexistent or self-conferred certification or professional designation;
3. Use of a certification or professional designation that indicates or implies a level of occupational qualifications obtained through education, training or experience that the insurance producer using the certification or designation does not have; and
4. Use of a certification or professional designation that was obtained from a certifying or designating organization that:
  - a) Is primarily engaged in the business of instruction in sales or marketing;
  - b) Does not have reasonable standards or procedures for assuring the competency of its certificants or designees;
  - c) Does not have reasonable standards or procedures for monitoring and disciplining its certificants or designees for improper or unethical conduct; or
  - d) Does not have reasonable continuing education requirements for its certificants or designees in order to maintain the certificate or designation.
5. Under the regulation, there is a rebuttable presumption that a certifying or designating organization is not disqualified solely for purposes of subsection A(2)(d) when the certification or designation issued from the organization does not primarily apply to sales or marketing and when the organization or the certification or designation in question has been accredited by:
  - a) The American National Standards Institute (ANSI);
  - b) The National Commission for Certifying Agencies; or
  - c) Any organization that is on the U.S. Department of Education's list entitled "Accrediting Agencies Recognized for Title IV Purposes."
6. In determining whether a combination of words or an acronym standing for a combination of words constitutes a certification or

professional designation indicating or implying that a person has special certification or training in advising or servicing seniors, factors to be considered shall include:

- a) Use of one or more words such as “senior,” “retirement,” “elder,” or like words combined with one or more words such as “certified,” “registered,” “chartered,” “advisor,” “specialist,” “consultant,” “planner,” or like words, in the name of the certification or professional designation; and
- b) The manner in which those words are combined.

7. For purposes of this NAIC regulation, a job title within an organization that is licensed or registered by a State or federal financial services regulatory agency is not a certification or professional designation, unless it is used in a manner that would confuse or mislead a reasonable consumer, when the job title:

- a) Indicates seniority or standing within the organization; or
- b) Specifies an individual’s area of specialization within the organization.

8. Under this subsection, financial services regulatory agency includes, but is not limited to, an agency that regulates insurers, insurance producers, broker-dealers, investment advisers, or investment companies as defined under the Investment Company Act of 1940.

**IV. State-by-State Index** to the NAIC Senior-Specific Certifications Model Regulation appears on page 11 following the outline on the NAIC Suitability in Annuity Transactions Model Regulation..

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## State Laws Governing Suitability in Variable Life Insurance Sales

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### I. State Laws Governing VLI Suitability- Historical SEC & FINRA Parallels

### II. Suitability Requirements in the NAIC Model Variable Life Insurance Regulation

- A. Scope and Impact of Suitability Provisions in the NAIC Model Variable Life Insurance
  - 1. Thirty-one jurisdictions have adopted the NAIC Model Variable Life Insurance Regulation, and an additional eleven have adopted related provisions.<sup>14</sup> Twenty-nine have specific provisions concerning suitability, which are set forth in a chart at the conclusion of this outline segment.
  - 2. Suitability standards are explicit and unequivocal in NAIC Model Variable Life Insurance Regulation, as explained below.
- B. Section 3 of the NAIC Model Variable Life Insurance Regulation establishes qualifications of insurers to issue variable life insurance, and Paragraph (C) sets forth detailed Standards of Suitability.
- C. Section 3(C) states that:
  - 1. Every insurer seeking approval to enter into the variable life insurance business in this state shall establish and maintain a *written statement* specifying the *standards of suitability* to be used by the insurer. See, NAIC Model Regulation Service (January 1996) at 270-731 [emphasis added].
  - 2. The standards of suitability shall specify that no recommendation shall be made to an applicant to purchase a variable life insurance policy and that no variable life insurance policy shall be issued in the absence of reasonable grounds to believe that the purchase of the policy is *not unsuitable* for the applicant on the basis of information furnished *after reasonable inquiry* of the applicant concerning the applicant's insurance and investment objectives, financial situation and needs, and any other information known to the insurer or the agent making the recommendation. *Id.* [emphasis added].
- D. The NAIC commentary on Section 3(C) provides additional clarification
  - 1. This section imposes a duty on both the insurer and its agents to make a *good faith, reasonable inquiry as to the facts and circumstances concerning a prospect's insurance and financial needs* and to make no recommendation that a prospect purchase variable life insurance when such a purchase is not reasonably consistent with the information that is known or reasonably should be known to the insurer or agent. See, NAIC Model Regulation Service (January 1996) at 270-731 [emphasis added].
  - 2. According to the commentary, some of the factors which would be considered

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<sup>14</sup>See, NAIC Model Regulation Service (January 1996) at 270-771.

are:

- a. age,
  - b. earnings,
  - c. marital status,
  - d. number and age of dependents,
  - e. the value of savings and other assets,
  - f. and current life insurance program.
3. The commentary explains that the substantive standard in Section 3(C) was derived from the federal securities laws. *Id.*
  4. The commentary emphasizes that the duty to make a good faith reasonable inquiry must be stressed since an insurer or agent cannot continually seek to avoid the obligations imposed by this section by claiming that a prospect refused to divulge information sufficient to make a professional evaluation of the suitability of variable life insurance to particular circumstances. *Id.*
- E. When the Model Variable Life Insurance Regulation was substantially amended in 1983 to accommodate flexible premium variable life insurance, this suitability provision was revised and updated to reflect state and federal regulatory changes that had evolved since the original Model Variable Life Insurance Regulation that governed only scheduled premium variable life insurance. The commentary explains that:
1. The 1983 amendments made changes in this section to achieve a more practical application of the suitability concept to sales of variable life insurance.
  2. While the concept originally set forth in this section was substantially similar to that utilized in the federal securities laws, the application of the concept was exaggerated as part of the effort to avoid SEC regulation of variable life insurance.
    - a. For example, prior to the 1983 amendments, the section required that the insurer adopt the standards of suitability by *formal action of its board of directors*.
      - (1) This requirement of board adoption was found to be unprecedented in NAIC model insurance statutes and unnecessary to the application of the suitability concept to sales of variable life insurance.
    - b. Similarly, the standards of suitability were “applicable to and binding on the insurer’s officers, directors, employees, affiliates and agents with respect to the suitability of variable life insurance for the applicant.”
      - (1) The potential for mischief of this broad requirement was considerable, raising, for example, the possibility of liability for violations of the suitability standards being imposed on individual officers, directors, employees or agents who never even knew of the transaction involved.
      - (2) These two aspects of the original Model Variable Life Insurance

Regulation were deleted in the 1983 amendments. See, NAIC Model Regulation Service (January 1996) at 270-32.

- F. Other NAIC interpretative guideposts on Section 3(C) suitability appear in a NAIC staff report which the NAIC adopted in 1974, that emphasized *three basic areas of ideal suitability* concerning VLI:
1. needs *perceived* by the insured;
  2. needs *perceived* by the agent; and
  3. *persistence*. See, 1974 Proceedings of the NAIC II at 540 [emphasis added].
- G. The NAIC staff report contains further interpretive guidance.
1. The NAIC staff report was adopted as an interpretive guide to Section 3(C) in 1974 and offers the following language “as an informal consensus” on the meaning of suitability in the model variable life insurance regulation.
    - a. Definition—“Suitability” means the likelihood that the purchase of variable life insurance is reasonably consistent with:
      - (1) The *expressed insurance objectives and needs* as perceived by the prospective insured;
      - (2) The *reasonable objectives and needs* of the prospective insured as determined objectively by a professional agent after a diligent reasonable inquiry into relevant financial, family and other background information concerning the prospective insured; and
      - (3) The *potential that the prospective insured will persist* with the policy for such a period of time that the insurer’s acquisition costs are amortized over a reasonable period of time. See, 1974 Proceedings of the NAIC II at 547 [emphasis added].
    - b. General Rules of Interpretation accompany the staff report that became the interpretive guide adopted by the NAIC, and explain:
      - (1) When variable life insurance meets characteristics (1) and (3) or (2) and (3), it is probably still “suitable” in most instances.
      - (2) Variable life insurance is clearly “unsuitable” when it meets none of the three characteristics for a given prospect.
      - (3) Variable life insurance is probably “unsuitable” in the absence of extraordinary factors when it does not meet characteristic (3).
      - (4) Other situations must be judged on their individual facts.
- H. Even further clarifications to these VI standards of suitability were added in 1983. The commentary explains that:
1. In adopting the 1983 amendments, the NAIC recognized that the proliferation of variable life insurance product designs anticipated as a result of those amendments might make suitability, and particularly factors (1) and (2), even more important. See, NAIC Model Regulation Service (January 1996) at 270-33 [emphasis added].
  2. On the other hand, it was understood that the possibility of more variable life

insurance products designed to compete with investment oriented products of other financial institutions will make factor (3) less significant because policyholders will be more likely to move among competing financial institutions will make factor (3) less significant because policyholders will be more likely to move among competing financial institution products for reasons such as rate of return, tax considerations and economic conditions. *As a result, persistency will be less and less relevant as a measure of suitability.* *Id.*

3. Section 3(C) requires the insurer to *formally adopt* its suitability standards.
  - a. Earlier drafts of Section 3(C) specifically required that the insurer establish and file with the commissioner guidelines or *profiles of applicants and situations* in which variable life insurance would not generally be suitable.
  - b. This specific requirement was deleted from Section 3(C).
- I. Other aspects of interest concerning VLI suitability from the NAIC Model Variable Life Insurance Regulation
  1. Private rights of action. The commentary notes that:
    - a. As to the potential legal implications of adopting standards of suitability, it is not unlikely in those jurisdictions where the doctrine of implied rights of action is accepted, that the theory would give rise to an enforceable obligation to the insured<sup>15</sup>. See, NAIC Model Regulation Service (January 1996) at 270-33 [emphasis added].
    - b. Furthermore, it is probable that the commissioner would have the authority (either formal or informal) to reverse an unsuitable sale upon the request of the policyholder. This would be in addition to the full range of sanctions available to him. *Id.*
  2. Group Contracts
    - a. The commentary states that the requirements of Section 3(C) would not be applicable with respect to each individual employee involved in a non-contributory pension plan situation. See, NAIC Model Regulation Service (January 1996) at 270-33.
  3. Lapse Rates not Germane
    - a. Prior to the 1983 amendments, the section included provisions pursuant to which lapse rates were to be utilized as indicators of suitability.
      - (1) These provisions were based upon the realization that suitability is a difficult area to police and the hope that lapse rates, by indicating persistency, would be an accurate yardstick for suitability.
      - (2) The 1983 amendments eliminated references to lapse rates as measures of suitability.

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<sup>15</sup> *Anderson v. Knox*, 297 F.2d 702 (9<sup>th</sup> Cir.), *cert. Denied*, 370 U.S. 915 (1961), the U.S. Court of Appeals for the Ninth Circuit held that an insurance agent who had induced a client to purchase excessive amounts of bank financed insurance was liable for damages in common-law fraud because the policies were not suitable to the plaintiff's needs.

- (a) The commentary explains that “[w]ith regard to conventional insurance policies, lapse rates, even those reflecting experience over a very long period of time, are suspect as an indicator of whether or not sales of insurance were suitable when made. Lapse rates are even less relevant to the suitability of sales of variable life insurance.” See, NAIC Model Regulation Service (January 1996) at 270-33.
- (b) Lapse rates are affected by a variety of factors, the most significant of which ordinarily is changes in the policyholder’s perception of the attractiveness of the policy due to changes in the general economy and in the economic circumstances of the policyholder. *Id.*
- (c) In the case of variable life insurance, an additional important factor is the performance of the separate account relative to other financial alternatives. Because of the significance of these factors, the use of lapse rates as a measure of suitability was found to be inappropriate. *Id.*

#### J. Suitability Information Required on Applications

1. Section 8(C) the NAIC Model Variable Life Insurance Regulation requires that variable life insurance applications *contain questions designed to elicit suitability information from applicants.* See, NAIC Model Regulation Service (2010) at 270-18.
  - a. This requirement dovetails with the suitability requirements in Section 3(C) discussed above.
  - b. The commentary to Section 3(C) cross references the required application information in Section 8(C). See, NAIC Model Regulation Service (2010) at 270-64.

#### STATES WITH SUITABILITY PROVISIONS IN VARIABLE LIFE INSURANCE LAWS AND REGULATIONS

State	Suitability Standard	Suitability Information in Application
Arizona	Ariz. Rev. Stat. § 20-2602(C)	Ariz. Rev. Stat. § 20-2608
Arkansas	Ark. Code Ann. § 33-Article III	Ark. Code Ann. § 33- Article VIII.
California	Cal. Code Regs. tit. 10, § 2534.2(c)	
Colorado	Colo. Code Regs. § 4-1-3(V)	Colo. Code Regs. § 4-1-3(VI)
Connecticut	Conn. Agencies Reg. § 38a-433-3(c)	Conn. Agencies Reg. § 38a-433-8
Delaware.	Admin. Code § 44(3)	Del. Admin. Code § 44(8)

D.C.	D.C. Mun. Regs. Tit. 26, § 2704.1	D.C. Mun. Regs. Tit. 26, § 2730.1
Georgia	Ga. Comp. R. & Regs. R. 120-2-32-.03	Ga. Comp. R. & Regs. R. 120-2-32-.09
Indiana	Ind. Admin. Code tit. 760, r.1-33-3	Ind. Admin. Code tit. 760, r.1-33-8
Kentucky	806 Ky. Admin. Regs. 15:030	
Louisiana	La. Admin. Code tit. 35, § 8303(3)	
Maine	Code Me. R. § 02-031 Chapter 300 Article V § 3 Authority of Insurer to Issue Variable Life Insurance	Code Me. R. § 02-031 Chapter 310 Article V § 3 Authority of Insurer to Issue Variable Annuity Contracts
Maryland	Md. Regs. Code tit. 31, § 09.12.01.02(D)	
Massachusetts	Mass. Regs. Code tit. 211, § 95.02 (3).	
Michigan	Mich. Admin. Code r. 500.844 Rule 4	Mich. Admin. Code r. 500.864 Rule 24
Mississippi	Miss. Reg. 84-101(3)(c)	
Missouri	Mo. Code Regs. Ann. Tit. 20, §400- 1.030(2)(C)	Mo. Code Regs. Ann. Tit. 20, §400-1.030(7)(C)
Nebraska	Neb. Admin. Code 210.15.003.03	Neb. Admin. Code 210.15.008.03
New Mexico	N.M. Admin. Code tit. 13, § 9.8.10	N.M. Admin. Code tit. 13, § 9.8.35
North Carolina	N.C. Admin. Code tit. 11, r. 12 .0435(3)	N.C. Admin. Code tit. 11, r. 12 .0440
North Dakota	N.D. Admin. Code § 45-04-02-03(3)	N.D. Admin. Code § 45-04- 02-07
Ohio	Ohio Admin. Code § 3901-06-08(D)	Ohio Admin. Code § 3901- 06-08(I)
Pennsylvania	31 Pa. Code § 82.14.	31 Pa. Code § 82.62.
South Carolina	25A S.C. Code Ann. Regs. 69-12, Article III	25A S.C. Code Ann. Regs. 69-12, Article VIII
Texas	28 Tex. Admin. Code § 3.803(3)	28 Tex. Admin. Code § 3.808
Vermont	Vt. Code R. I-88-3(3)	Vt. Code R. I-88-3(8)
Virginia	14 Va. Admin. Code § 5-80-50	14 Va. Admin. Code § 5-80- 310