

ANNUITY SUITABILITY

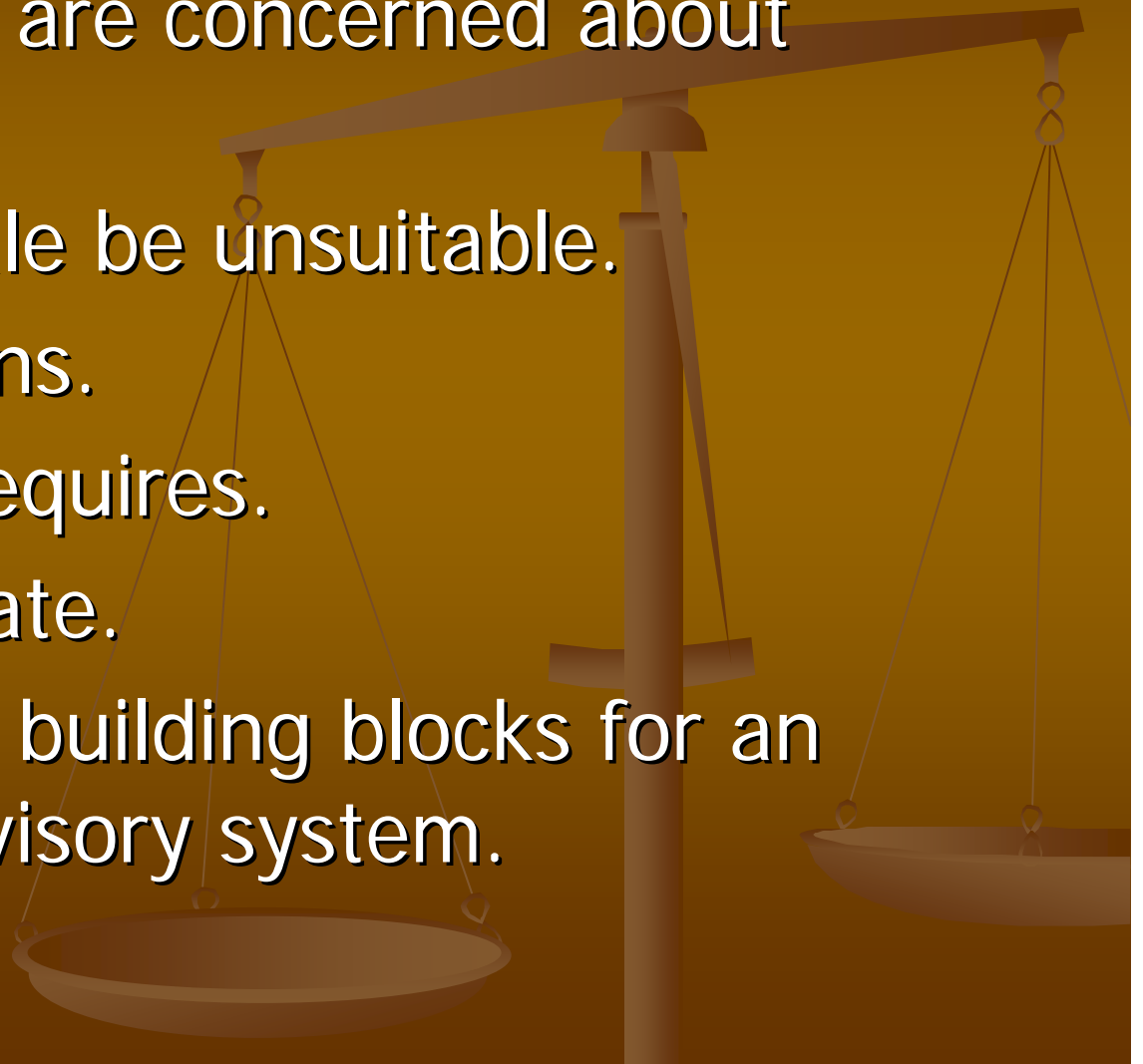
WHY REGULATORS ARE CONCERNED

Wisconsin Office of the Commissioner of Insurance



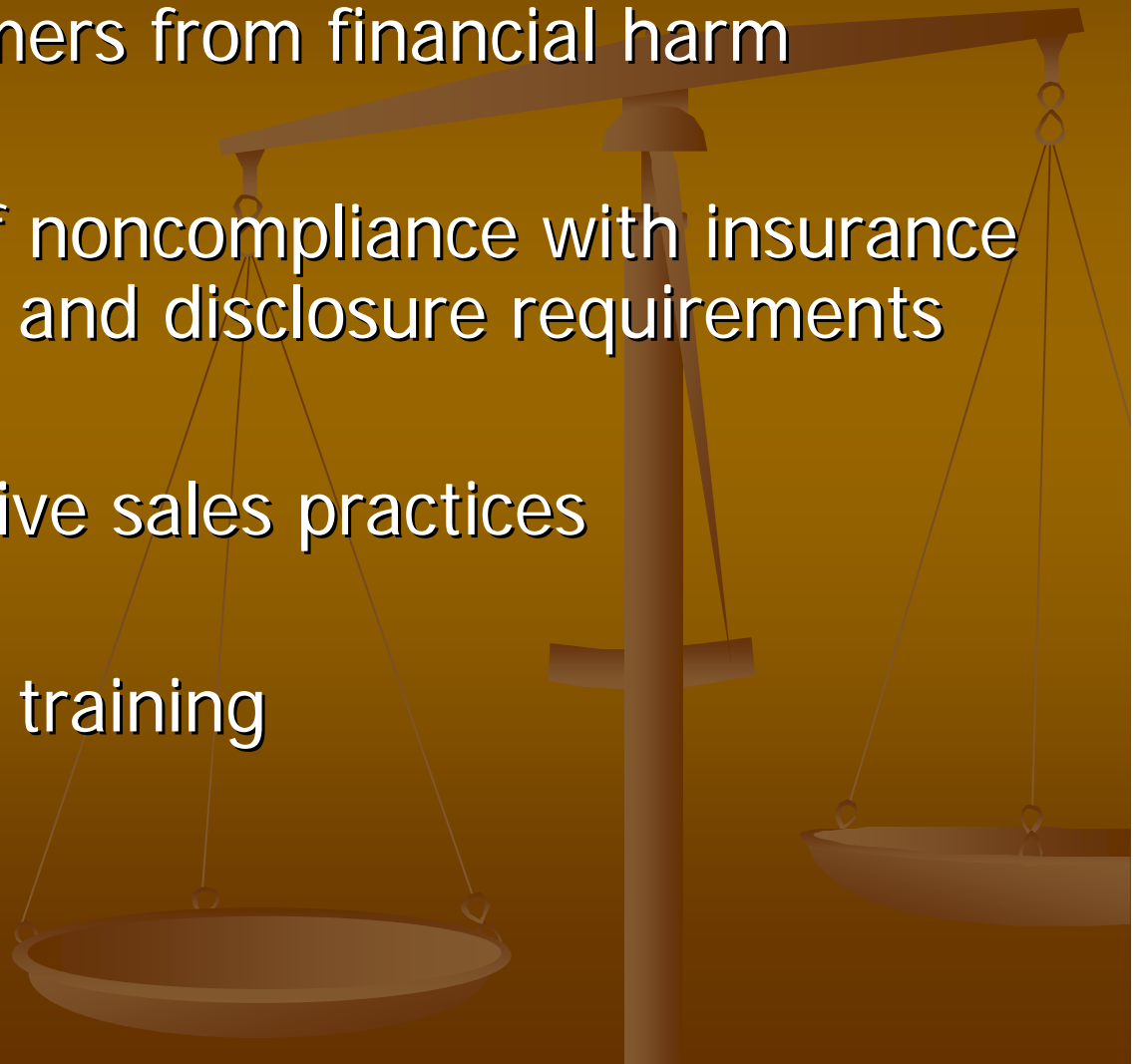
Agenda

- Why regulators are concerned about suitability.
- When may a sale be unsuitable.
- Serious violations.
- What the law requires.
- Legislative update.
- What are some building blocks for an effective supervisory system.



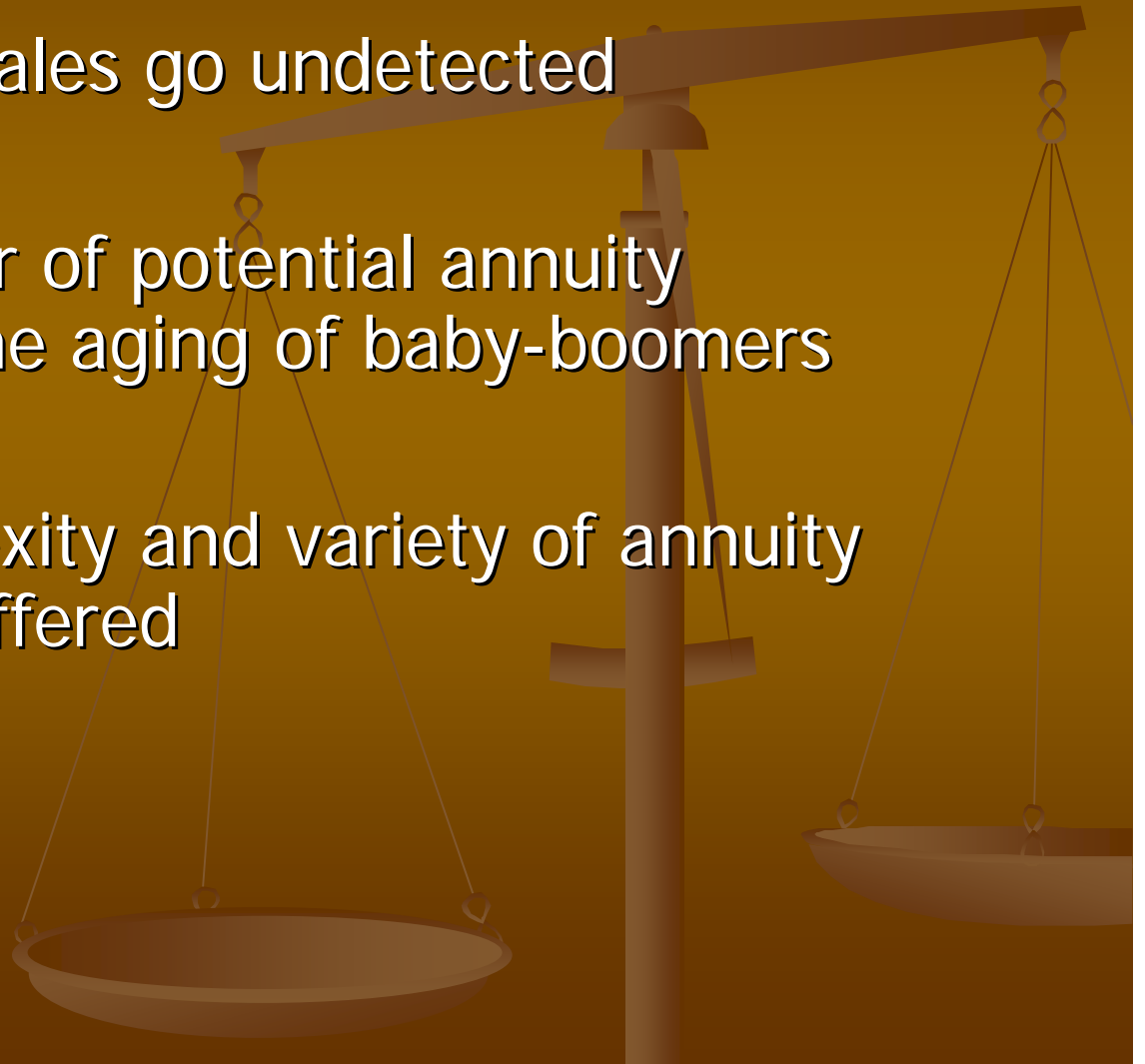
Why Regulators are Concerned about Suitability

- Protecting consumers from financial harm
- Major incidents of noncompliance with insurance laws, regulations, and disclosure requirements
- Improper or abusive sales practices
- Insufficient agent training



Why Regulators are Concerned about Suitability

- Most unsuitable sales go undetected
- Increased number of potential annuity customers with the aging of baby-boomers
- Increased complexity and variety of annuity contracts being offered



Why Regulators are Concerned about Suitability

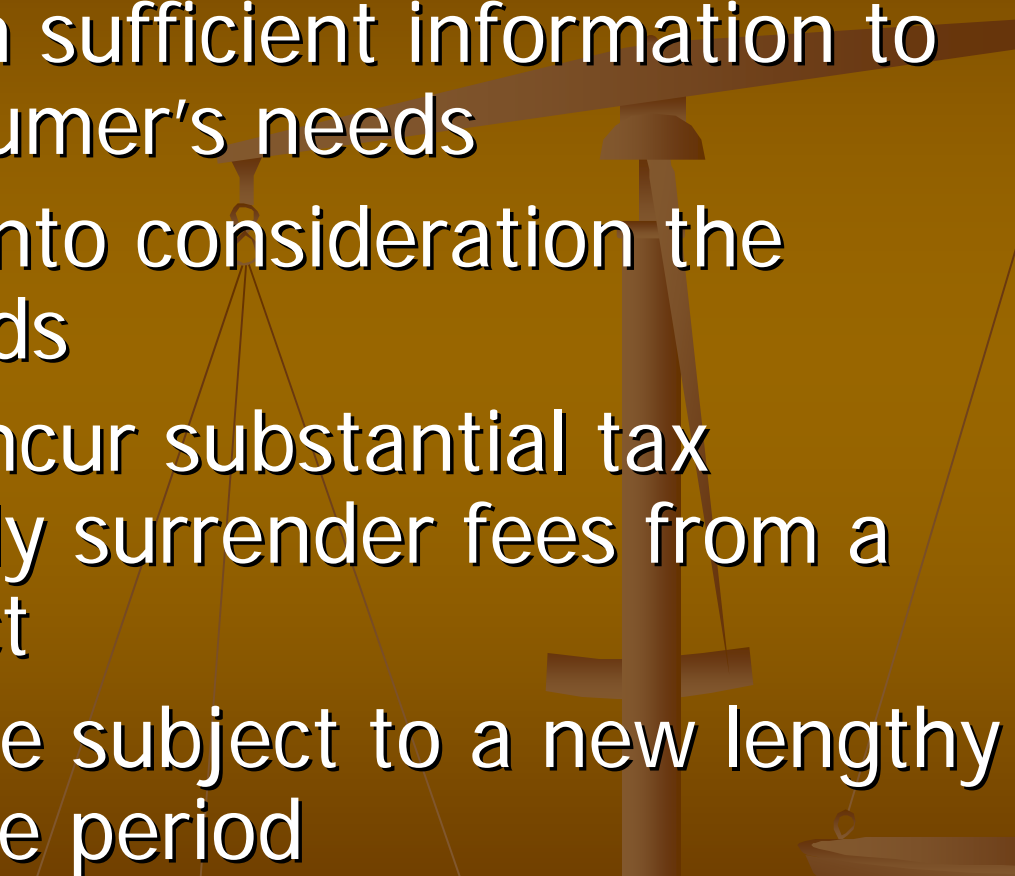
- Companies need uniform “level playing field” guidance to develop standards for monitoring agent sales activities that result in excessive replacements or in inappropriate surrenders.
- Companies need uniform “level playing field” guidance to develop agent training standards and verification.



Why Regulators are Concerned about Suitability

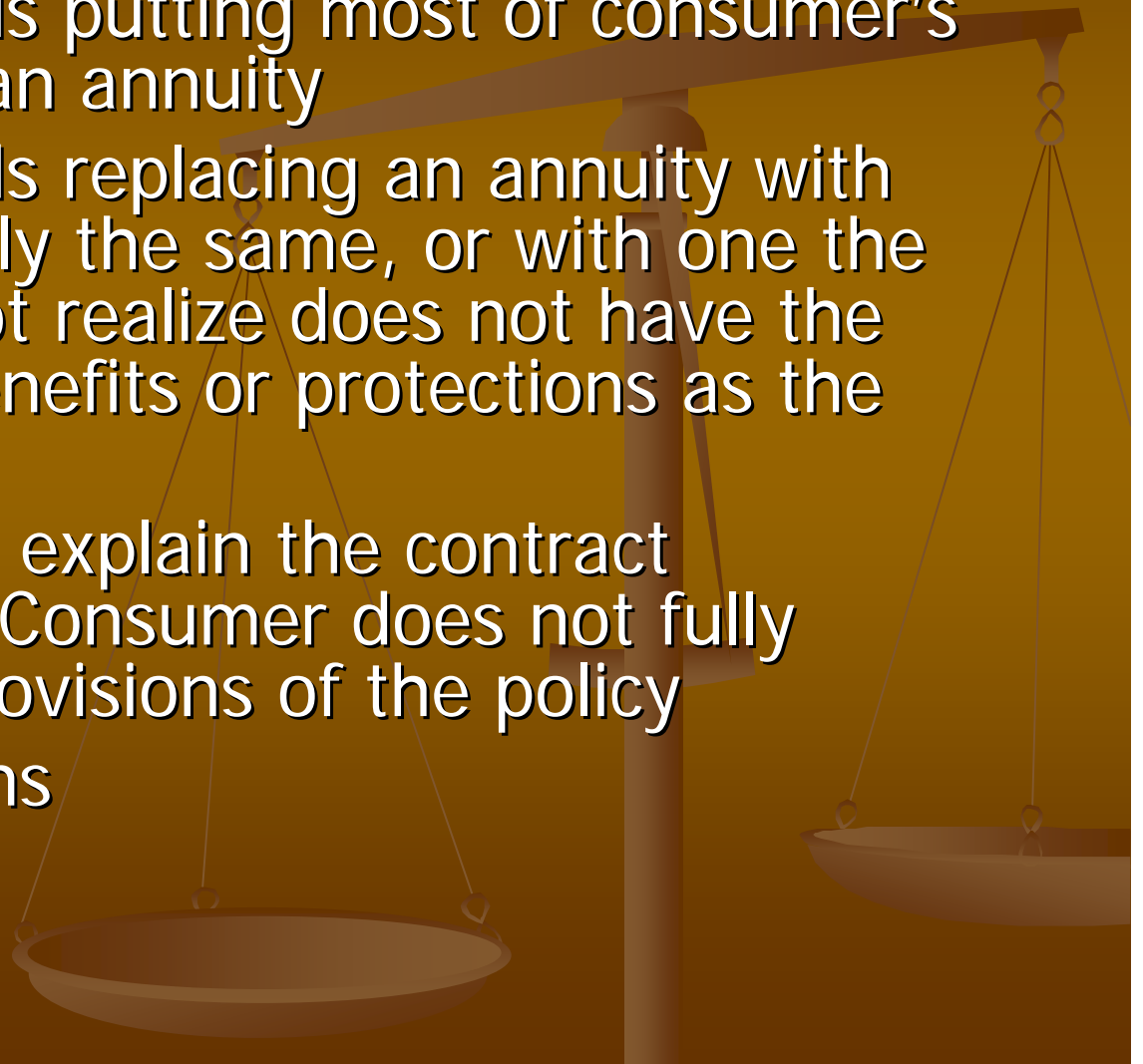
- Companies need uniform “level playing field” guidance to develop standards for training programs designed and provided by managing general agents and broker-dealer agents on suitability of annuity sales and sales practices, and for verification of those programs.
- Companies need uniform “level playing field” guidance on supervision standards for the increasing volume of annuity sales to the senior population, a market that is particularly likely to include vulnerable individuals. Over half the annuities issued by some of the top annuity writers in Wisconsin are issued to seniors age 65 and above.
- Companies need uniform “level playing field” guidance on supervision standards for sales of annuities to seniors involving surrenders or replacement, events that are particularly likely to be a financial issue for seniors. Much of the annuity business issued to seniors age 65 and above involves replacement of an existing life or annuity policy, often causing the person to incur a substantial surrender fee.

When May a Sale be Unsuitable?

- ❑ Failure to obtain sufficient information to determine consumer's needs
 - ❑ Failure to take into consideration the consumer's needs
 - ❑ Consumer will incur substantial tax penalties or early surrender fees from a replaced product
 - ❑ Consumer will be subject to a new lengthy surrender charge period
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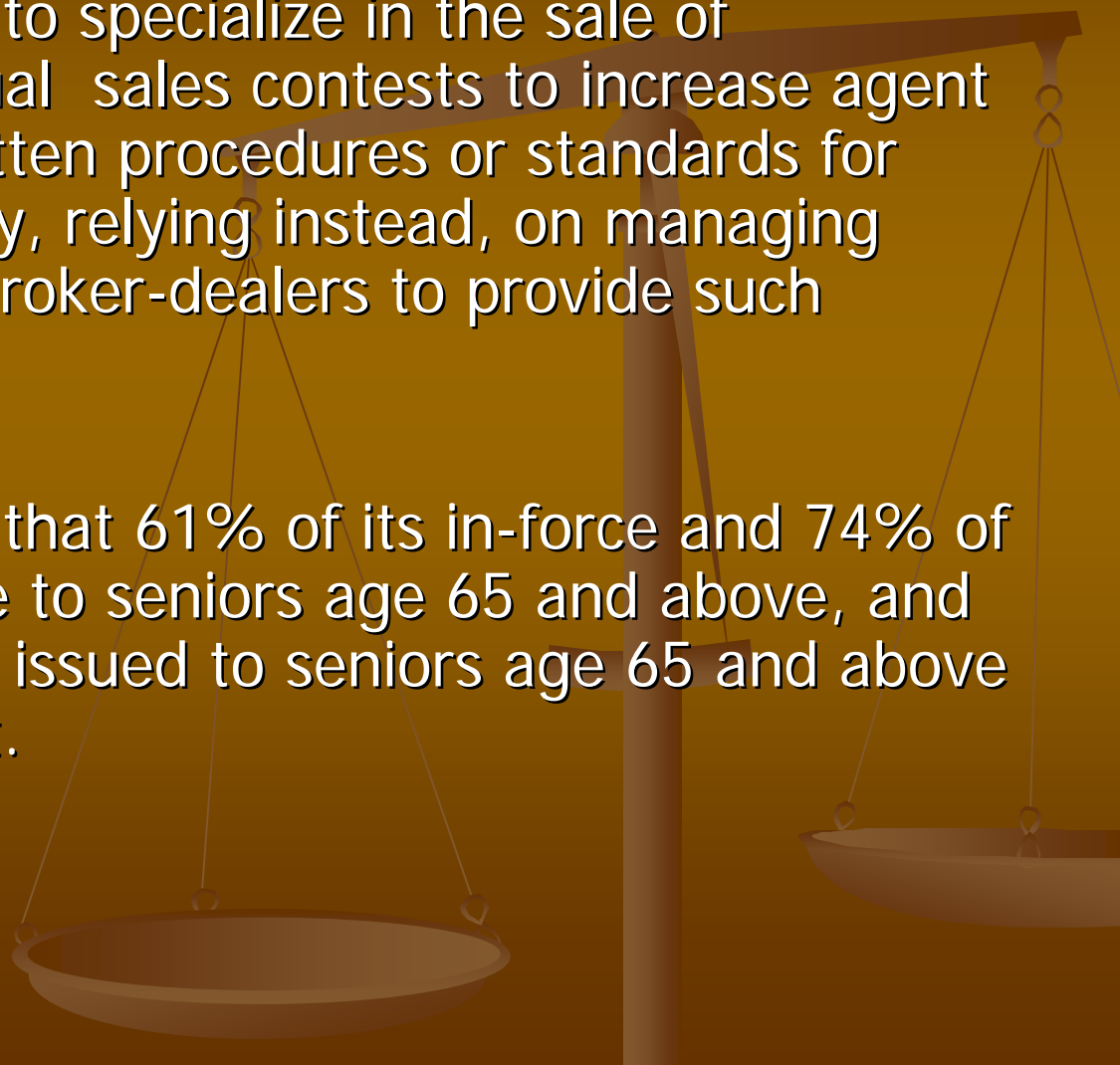
When May a Sale be Unsuitable?

- ❑ Agent recommends putting most of consumer's liquid assets into an annuity
- ❑ Agent recommends replacing an annuity with one that is basically the same, or with one the consumer does not realize does not have the same expected benefits or protections as the first
- ❑ Agent fails to fully explain the contract provisions, or the Consumer does not fully understand the provisions of the policy
- ❑ Many other reasons



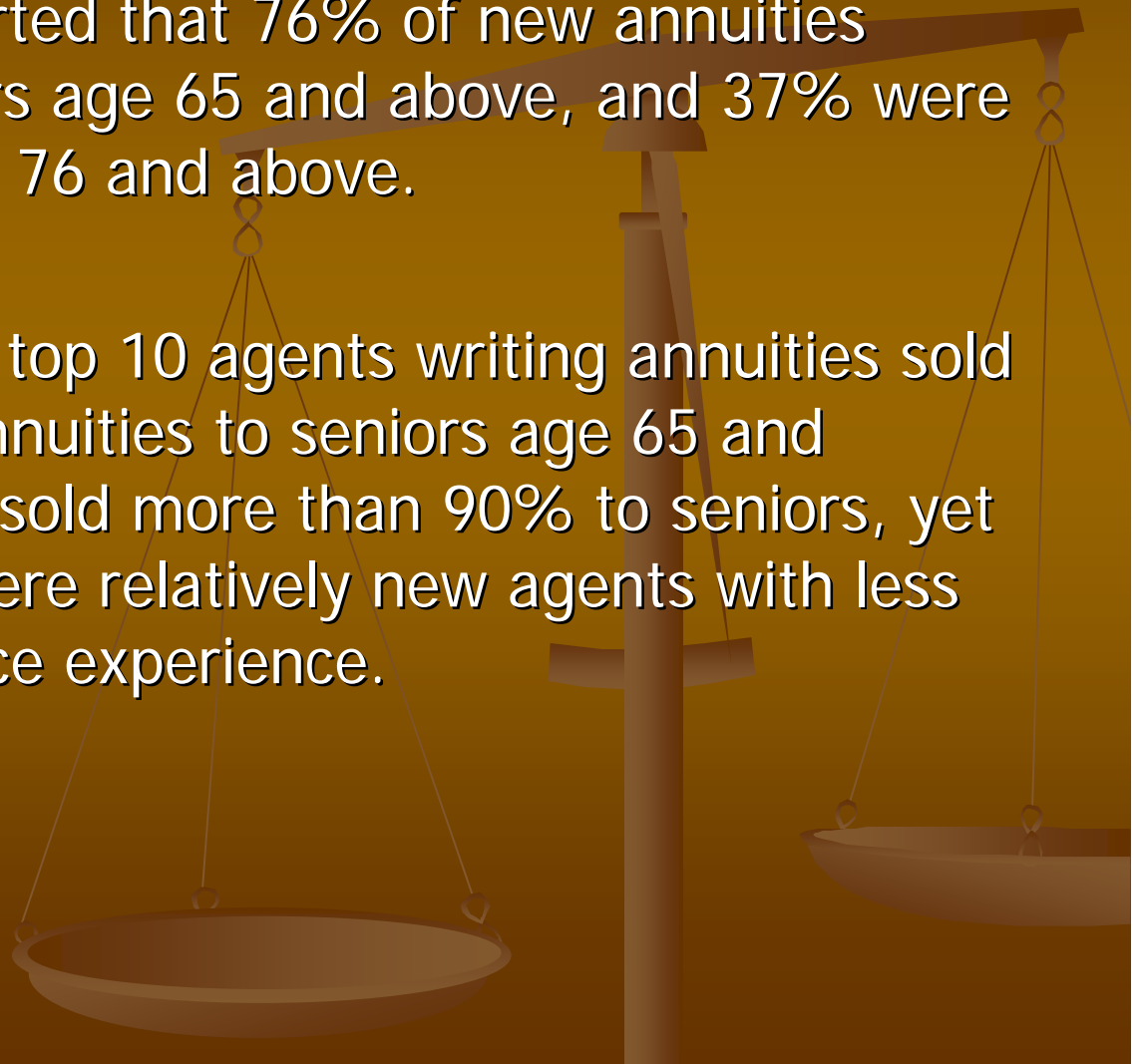
Reasons to Worry?

- One insurer claiming to specialize in the sale of annuities, holds annual sales contests to increase agent sales, but has no written procedures or standards for determining suitability, relying instead, on managing general agents and broker-dealers to provide such supervision.
- The insurer reported that 61% of its in-force and 74% of annuities issued were to seniors age 65 and above, and 35% of the annuities issued to seniors age 65 and above involved replacement.



Reasons to Worry?

- Another insurer reported that 76% of new annuities issued were to seniors age 65 and above, and 37% were issued to seniors age 76 and above.
- Eight of the insurer's top 10 agents writing annuities sold more than 50% of annuities to seniors age 65 and above, and 2 agents sold more than 90% to seniors, yet 7 of the 10 agents were relatively new agents with less than 3 years insurance experience.



Serious Violations

- A review of a sample of ten of the agent investigations conducted by the office in the last two years shows those investigations and enforcement actions resulted in forfeitures totaling \$422,550.00, and the revocation of the insurance license of eight agents for alleged violations of Wisconsin insurance regulations relating in part to the agent's failure to consider suitability when selling annuities to seniors .

Serious Violations

- For example, one enforcement action alleged that an agent repeatedly violated the law by making unsuitable sales of annuities to elderly consumers. The OCI alleged that the agent:
 - Made false and misleading communications in the marketing of annuities.
 - Failed to obtain sufficient information from consumers to establish the suitability of the annuities he recommended.
 - Used methods that endangered the legitimate interests of his customers and the public.
- The agent was ordered to pay restitution to 7 elderly consumers and a \$40,000 forfeiture, and had his license to sell insurance revoked.

Serious Violations

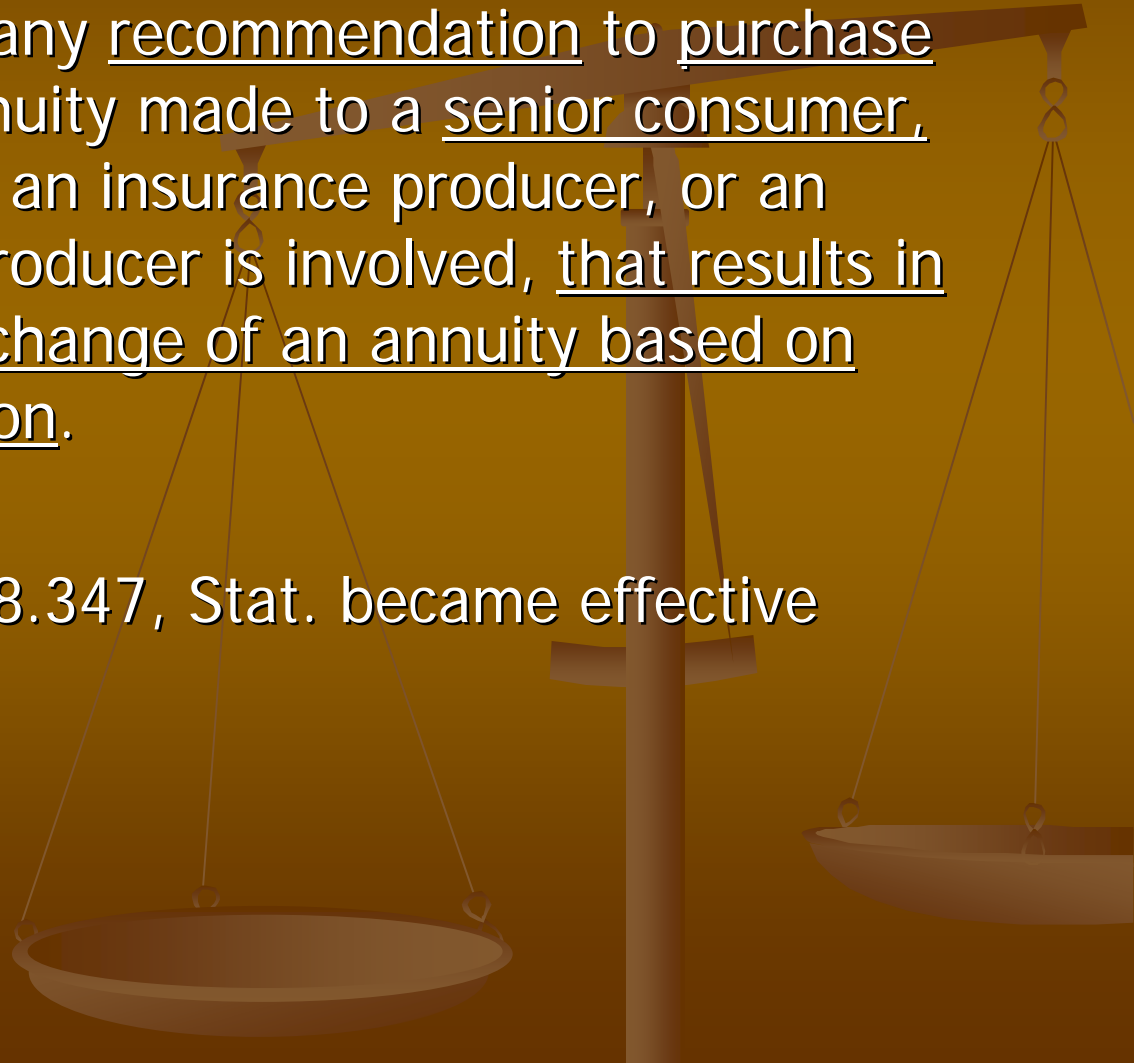
- OCI alleged in another enforcement action that an agent repeatedly violated the law by making unsuitable sales of annuities to elderly consumers. The OCI ordered the agent to pay restitution to 40 elderly consumers, pay a \$281,000 forfeiture, and revoked the agent's license to sell insurance.
- The agent was also alleged to have:
 - Made multiple misrepresentations to consumers, insurers, and the Office of the Commissioner of Insurance (OCI).
 - Forged signatures.
 - Used false and misleading advertisements and representations in the sales of annuities.

Serious Violations

- Another OCI enforcement action alleged that an agent made an inappropriate sale of an immediate annuity to a 92 year old woman, causing her to incur surrender penalties when existing products were replaced. The \$500,000 annuity provided for a death benefit of 25% of the initial premium if death occurred within 10 years after purchasing the policy, which would have required the woman to live to be 102 to avoid her beneficiary losing 75% of the funds in the annuity. She died 6 months after purchase and her estate suffered more than a \$300,000 loss. The agent disputed the allegations, including with respect to suitability, but agreed to a stipulation imposing a forfeiture.

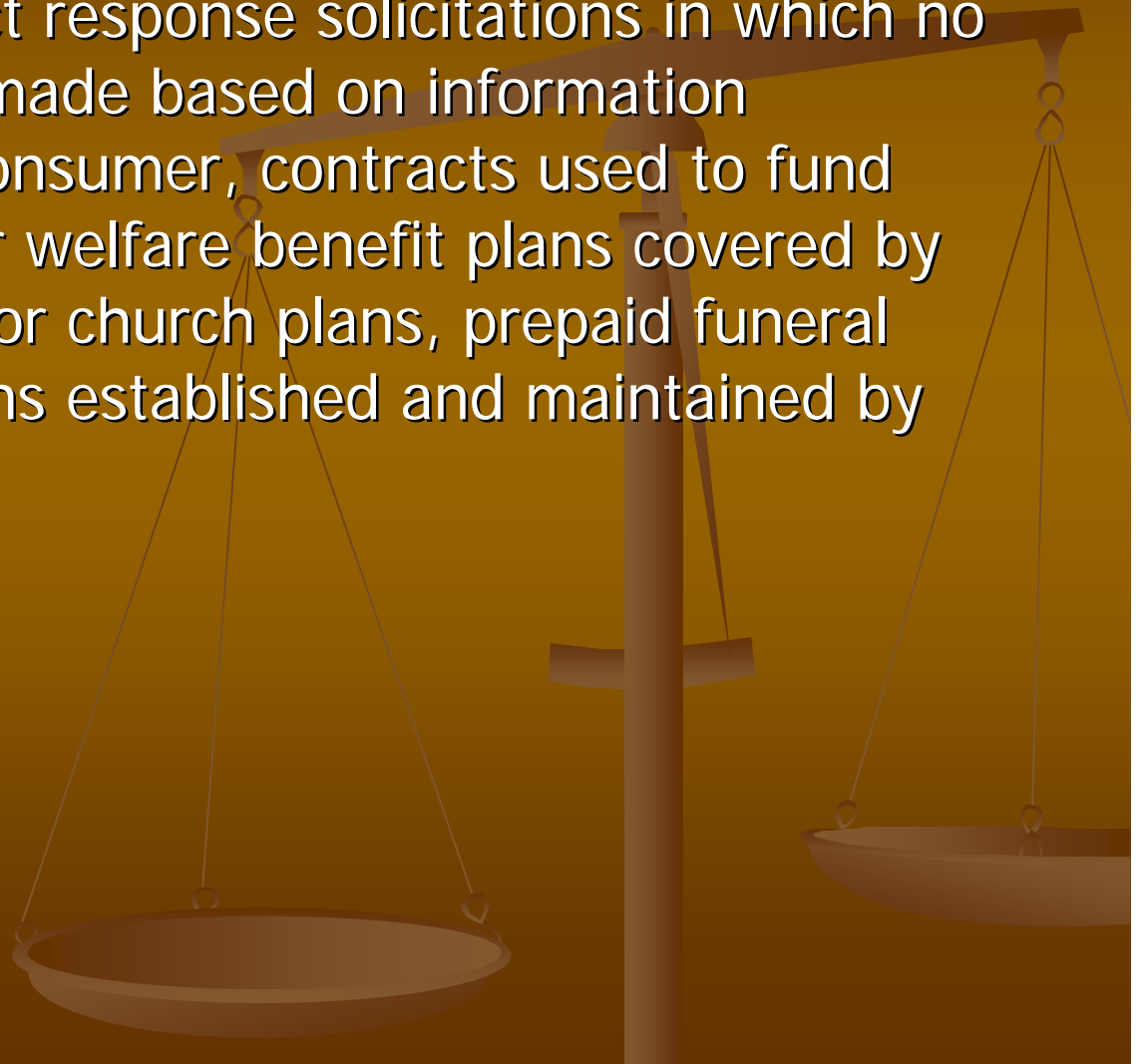
What The Annuity Suitability Law Requires

- The law applies to any recommendation to purchase or exchange an annuity made to a senior consumer, age 65 or older, by an insurance producer, or an insurer where no producer is involved, that results in the purchase or exchange of an annuity based on that recommendation.
- In Wisconsin, s. 628.347, Stat. became effective 11-1-2004.



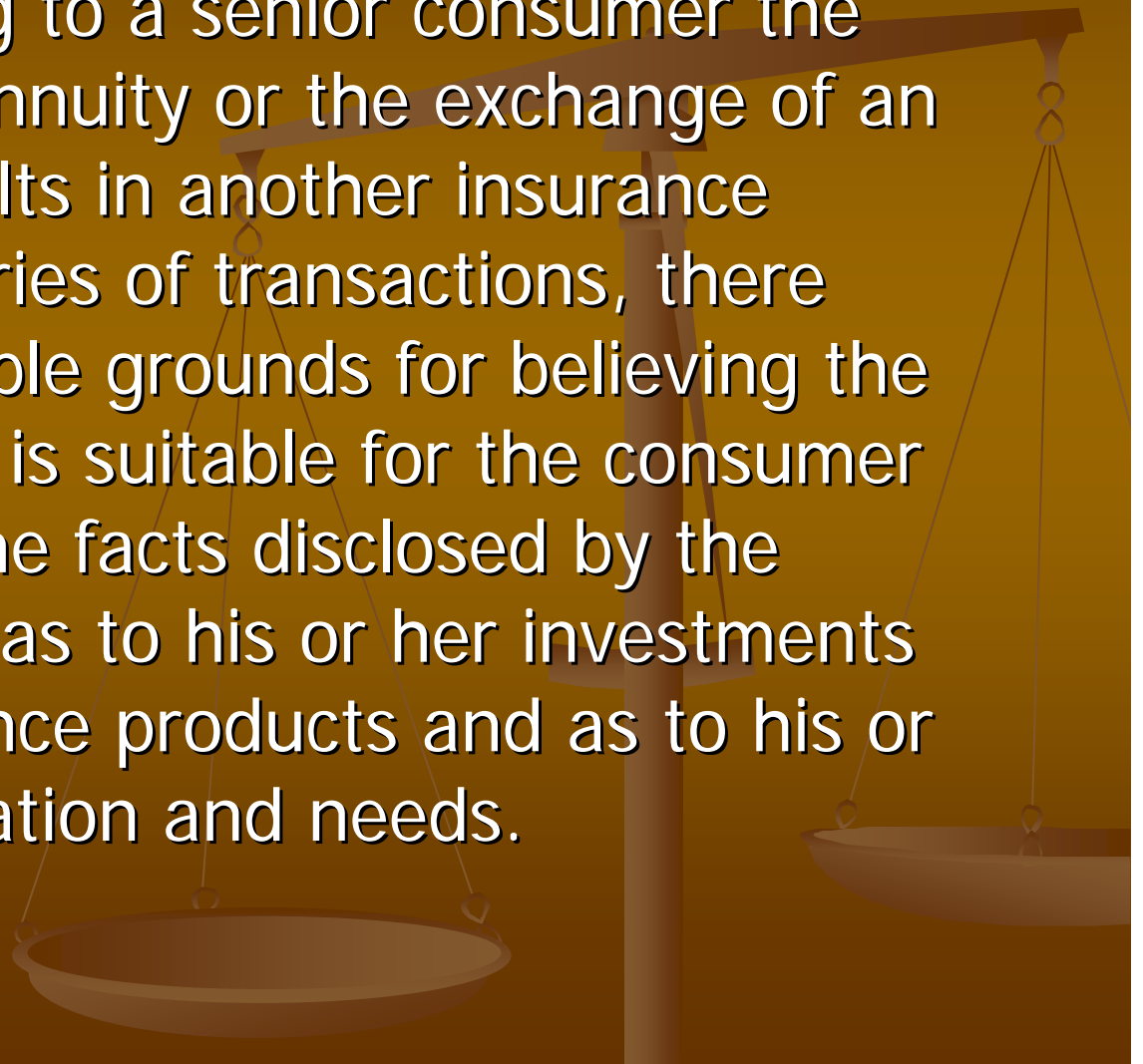
What The Annuity Suitability Law Requires

- **Exemptions:** Direct response solicitations in which no recommendation is made based on information collected from the consumer, contracts used to fund employee pension or welfare benefit plans covered by ERISA, government or church plans, prepaid funeral plans, and other plans established and maintained by an employer.



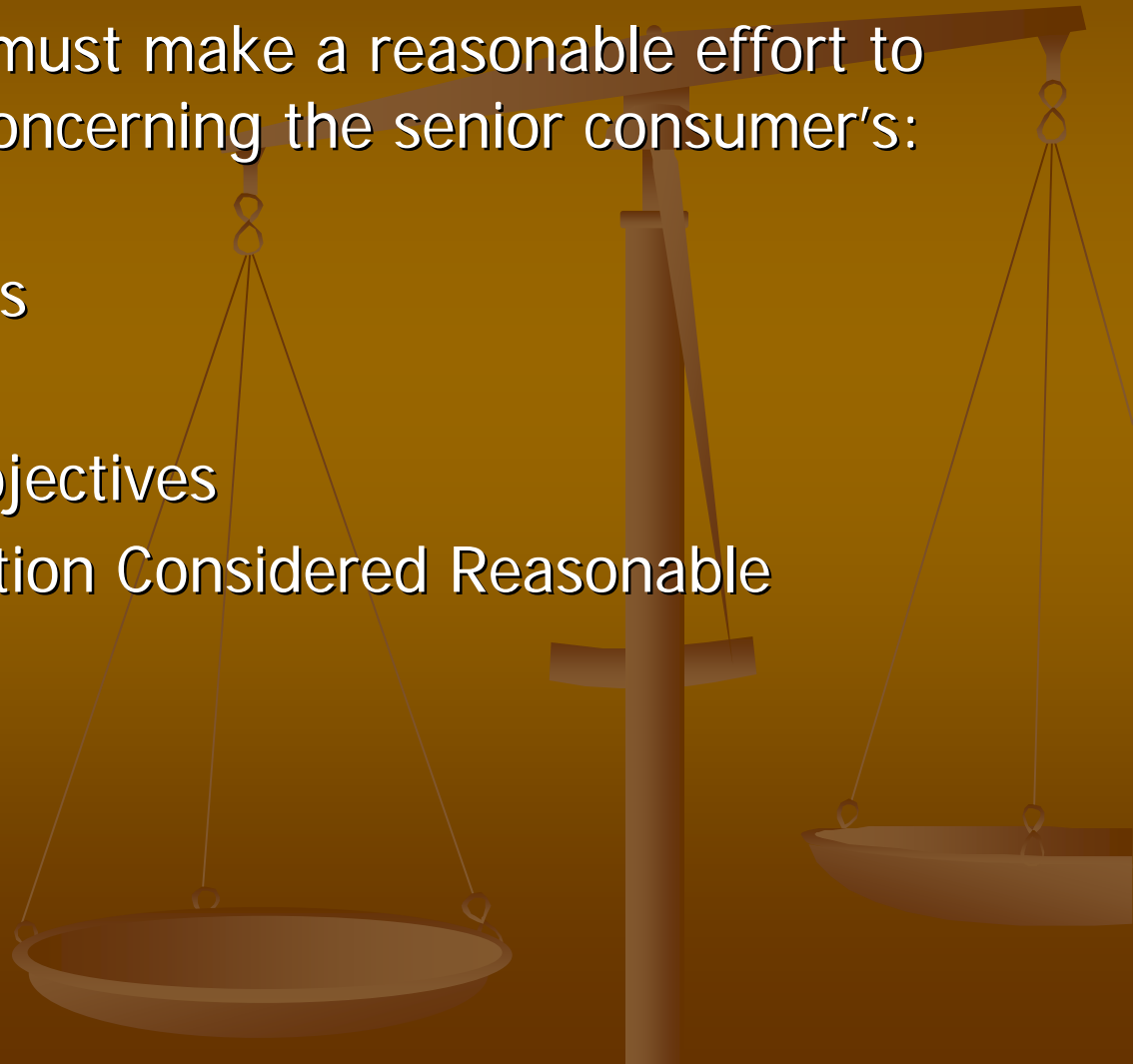
What The Annuity Suitability Law Requires

- In recommending to a senior consumer the purchase of an annuity or the exchange of an annuity that results in another insurance transaction or series of transactions, there must be reasonable grounds for believing the recommendation is suitable for the consumer on the basis of the facts disclosed by the senior consumer as to his or her investments and other insurance products and as to his or her financial situation and needs.



What The Annuity Suitability Law Requires

- An insurer or agent must make a reasonable effort to obtain information concerning the senior consumer's:
 - Financial Status
 - Tax Status
 - Investment Objectives
 - Other Information Considered Reasonable



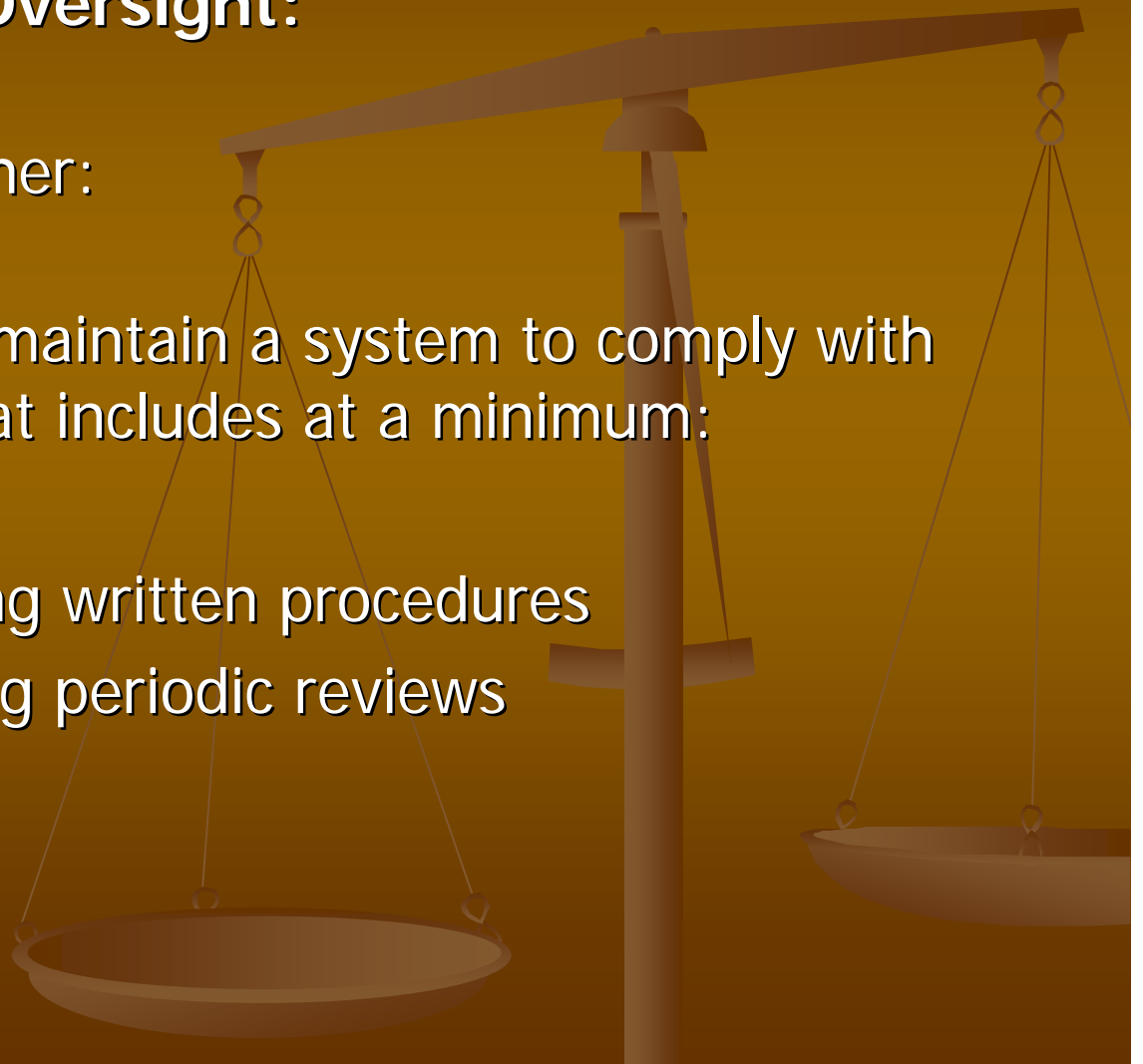
What The Annuity Suitability Law Requires

- **Supervision and Oversight:**

An insurer shall either:

Establish and maintain a system to comply with the model, that includes at a minimum:

- Maintaining written procedures
- Conducting periodic reviews



What The Annuity Suitability Law Requires

OR

Contract with a third party (may be a general agent or independent agency) to establish and maintain a system of supervision with respect to insurance agents under contract with or employed by the third party; and

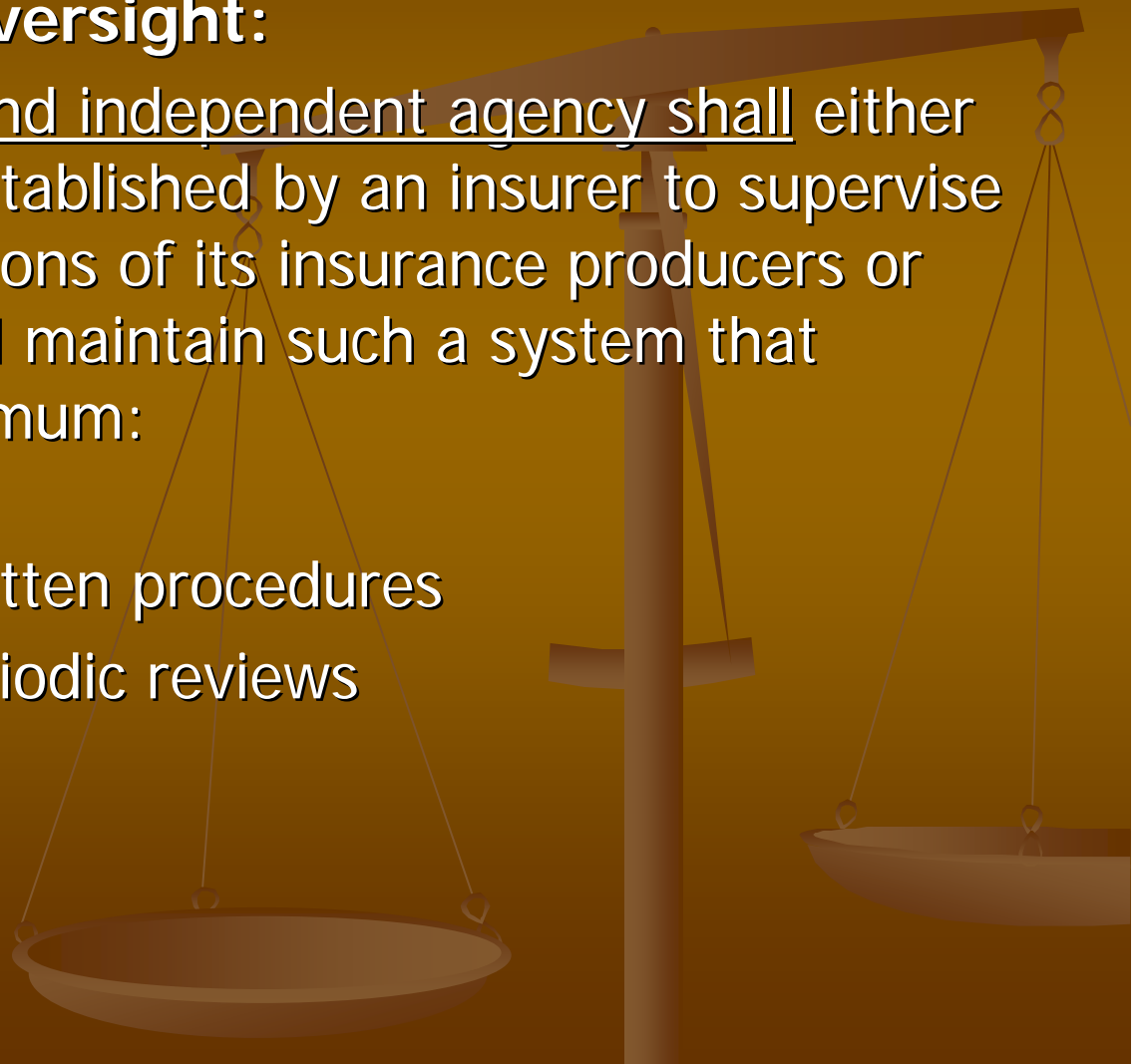
Make reasonable inquiries to ensure that the third party is performing its supervisory functions by requiring an annual certification from a senior manager of the third party who has responsibility for the delegated functions, and by periodically conducting a review of the third party's activities.

What The Annuity Suitability Law Requires

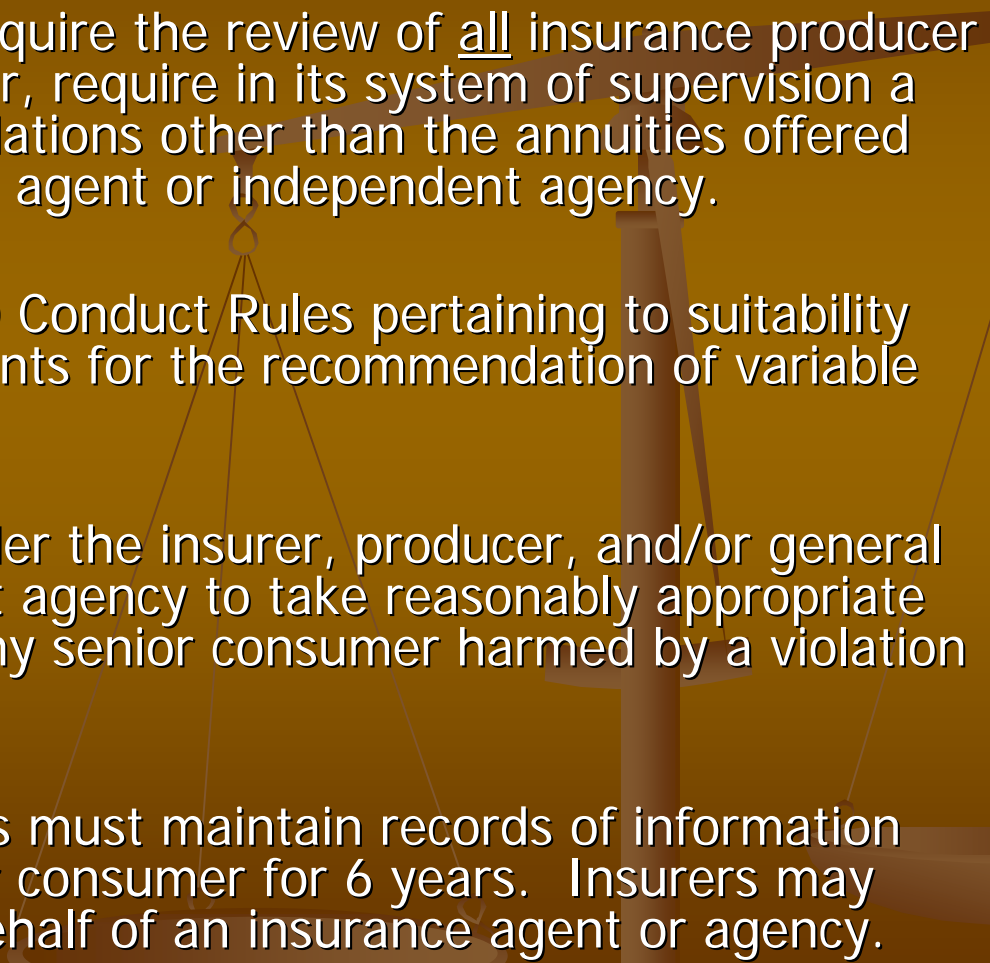
■ **Supervision and Oversight:**

A general agent and independent agency shall either adopt a system established by an insurer to supervise the recommendations of its insurance producers or shall establish and maintain such a system that includes at a minimum:

- Maintaining written procedures
- Conducting periodic reviews



What The Annuity Suitability Law Requires

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- The model does not require the review of all insurance producer solicited transactions or, require in its system of supervision a producer's recommendations other than the annuities offered by the insurer, general agent or independent agency.
 - Compliance with NASD Conduct Rules pertaining to suitability satisfies the requirements for the recommendation of variable annuities.
 - Commissioner may order the insurer, producer, and/or general agency or independent agency to take reasonably appropriate corrective action for any senior consumer harmed by a violation of the law.
 - Insurers and producers must maintain records of information collected from a senior consumer for 6 years. Insurers may maintain records on behalf of an insurance agent or agency.

Legislative Update

State Adoption of NAIC Suitability Model

- Model— All Ages Adopted (16)
 - AL, AZ, CO, GA, IA, KS, LA, MA, ME, MI, NV, OH, OK, RI, UT, VA
- Model— All Ages Proposed (9)
 - HI, IL, IN, MD, MT, ND, NE, TN, TX
- Model—Age 65+ Adopted (8)
 - AR, CT, DE, FL, ID, IN, NE, WI
- Model—Age 65+ Proposed (1)
 - CA
- Nonmodel Suitability Laws (6)
 - IA, MN, MO, ND, OR, & WV

As of 3/1/07

What Are Some Building Blocks For Having an Effective Supervisory System:

RECOGNITION

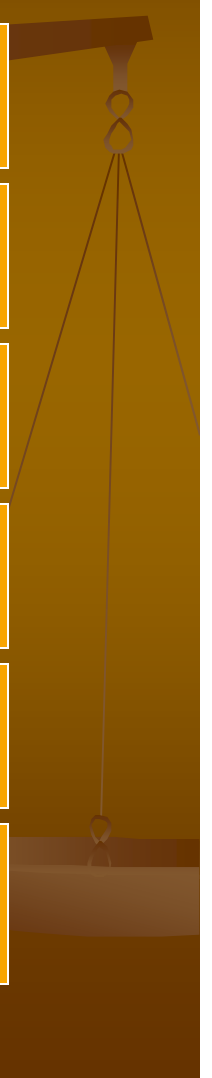
DOCUMENTATION

COMMUNICATION

TRAINING

MONITORING/VERIFICATION

MEANINGFUL CONSEQUENCES



Questions?

