Assessment of Public Comments to the First Amendment to Part 224 of Title 11 of the Official Compilation of Codes, Rules and Regulations of the State of New York (Insurance Regulation 187).

The New York State Department of Financial Services (the "Department" or "DFS") released First Amendment to Part 224 of Title 11 in December 2017 and received over 35 sets of comments to the proposed amendment (including one set of comments structured as a form letter that was emailed to the Department over 200 times by individual producers). The Department received comments from individuals and entities including insurers, producers, industry trade associations, consumer groups, and others. The Department also met with several commenters before and after the close of the comment period to discuss the proposal and to obtain clarification of the comments that were submitted.

Many commenters commended the Department for its efforts and most commenters expressed support for a best interest standard for life insurance and annuity transactions. Many commenters addressed more than one provision of the proposed amendment, and many requested specific changes. The Department has processed and carefully considered every comment and has made several revisions and clarifications to the proposal. This summary is intended to provide an overview of the categories of comments received by the Department, the revisions and clarifications the Department has made in response to those comments and, where applicable, the reasons for not making additional revisions or clarifications. Generally, comments received during the comment period addressed issues such as the scope and the meaning and/or particular wording of nearly every section of the proposed rule. While the Department made some of the recommended revisions, the Department did not make other recommended revisions because the Department determined, based on its experience and knowledge, that the revisions were unnecessary within the context of the proposal, were inconsistent with the standards or the purpose of the proposal, or were better addressed with an explanation in this assessment.

Harmonization and Other Regulatory Bodies

Some commenters recommended that the proposal should harmonize with standards, both existing and future, of other regulatory bodies. However, these same commenters also recommended changes to the proposal that would result in less harmony with current standards set by the U.S. Department of Labor ("DOL") and the Certified Financial Planner Board of Standards ("CFP Board)." The Department supports the goal of consistency across regulatory standards, where appropriate. The Department made efforts in this proposal to be consistent with the DOL Conflict of Interest rule ("DOL Rule") where the Department felt it was practicable and appropriate to do so. Since the Department released its proposal, the CFP Board has released a proposed best interest standard of its own. The Certified Financial Planner (CFP®) designation is known to be one of the most rigorous and well-regarded designations in the financial services industry, making it an appropriate standard to consider when determining appropriate standards of conduct for licensed producers. Those standards have many similarities to the Department's proposal, including requiring producers to act in the best interest of the consumer, requiring enhanced disclosures related to recommendations, and the elimination of any consideration of the financial or other interests of the producer in making a recommendation. The Department has also shared its proposal with the National Association of Insurance Commissioners (NAIC) and recommended that the NAIC consider the Department's proposal when drafting amendments to its model regulation.

Some commenters recommended that the Department wait for other regulatory bodies to promulgate rules or standards before taking any action to promulgate its own regulation. The

Department does not view this as a viable alternative. The DOL finalized its rule on April 08, 2016 and the Department has been working to have the NAIC propose a viable model regulation. New York has always been a strong leader in financial services regulation and will continue to lead on this issue. The Department is the sole regulator for the overwhelming majority of insurance activities occurring in New York State. Federal agencies such as the DOL and the Securities and Exchange Commission ("SEC") or self-regulatory agencies such as the Financial Industry Regulatory Authority ("FINRA") have only concurrent jurisdiction with the Department over only those products that are both insurance products and securities; the regulation of all other life insurance and annuity products and sales is within the sole purview of the Department. The Department maintains unique expertise related to comprehensive insurance markets and products that make it appropriate for the Department to lead on issues of insurance regulation. There is also uncertainty around whether other regulatory bodies may take action or how long it may take them to act. New York consumers should not be denied the protections of this proposal because other regulators in other jurisdictions have not adopted similar protections within their areas of authority.

Some commenters recommended that the proposal include language to the effect that if insurers or producers comply with standards of other regulatory bodies, such and the NAIC or the FINRA, then they will be deemed to be in compliance with this proposal. The Department did not make that recommended change. As noted above, there is uncertainty around whether other regulatory bodies may take action, or what that action may be. Current NAIC and FINRA standards do not have best interest standards comparable to this proposal. Further, such a provision would essentially delegate the Superintendent's rulemaking authority to another regulator, which the Superintendent is unwilling and unable to do.

Scope of the Regulation

Several commenters provided recommendations related to the scope and applicability of the regulation. Comments from consumer groups and some insurers expressed strong support that the proposal include life insurance and applies a consistent standard across life insurance and annuity product lines. Insurers emphasized the need for a level playing field in the insurance marketplace regardless of the type of insurance product insurers offer to consumers. A shortcoming of federal regulations, either by the DOL or the SEC, is that those entities' limited jurisdiction would create a two-tiered standard of conduct for different types of annuities and life insurance products which would be harmful and confusing for consumers and producers alike.

Proposed Exemptions

Other comments from the insurance industry recommended that various products lines be exempted from the proposal. Recommendations for exemptions included: all life insurance; all term life insurance; all whole life insurance; all universal life insurance; all life insurance with a face amount of $35,000 or less; all life insurance and annuities sold to anyone other than a natural person or trust; all annuities described in Internal Revenue Code section 4975(1)(B) through (F); all group life insurance and annuities; all variable life insurance and annuities issued in the private placement setting; all life insurance with a fixed premium sold in the worksite or financial institution markets; and all life insurance containing accelerated death benefits for chronic illness or which are sold in conjunction with long-term care insurance products. The Department agrees with those commenters that support a consistent standard of care across life insurance and annuity product lines. A consistent standard promotes a level playing field among insurers, is more easily understood by consumers and is more auditable for the Department. Consistency across life insurance and annuity product lines also promotes cost savings for producers and insurers who would not have to develop multiple compliance systems and multiple supervision systems. A consistent standard across life insurance and annuity product lines gives certainty to consumers which also has the potential to bolster consumer confidence in the industry and strengthen the marketplace. The Department has carefully considered the comments and made certain changes in the revised proposal, consistent with the purpose of this proposal. If the Department were to adopt the various exemptions recommended by some of the insurance industry commenters, it would result in a patchwork of standards and uncertainty among producers and consumers about the standards of care that producers will provide to consumers in any given transaction.

One commenter requested clarification that the exemption for policies used to fund employee benefit plans would include pension close-out group annuity contracts. The Department interprets the existing exemption to include such contracts. However, for clarity the proposal was revised to specifically address this type of contract as being included in the exemption.

One commenter recommended an exemption for the sale of a group policy to a group policy holder. However, such exemption is not needed because the sale of a group policy to a group policy holder is not subject to the regulation since the definition of policy does not include a group policy.

One commenter recommended adding language to clarify the applicability of the proposal to life settlement contracts. Language has been added to the regulation to clarify that the regulation is not applicable to life settlement contracts. Life settlement contracts were not included in this proposal because the conduct of life settlement providers and life settlement brokers is separately governed by Article 78 of the Insurance Law and 11 NYCRR Part 381.

Three commenters recommended that an exemption be added to the proposal for credit life insurance. The Department believes that such an exemption is appropriate if the coverage is sold on a group basis and in compliance with 11 NYCRR 185 (Insurance Regulation 27A). Where coverage is sold on a group basis, the employee of the financial institution offering the credit life insurance to consumers is not acting as an insurance agent or broker and, pursuant to §185.9 of Regulation 27A, is prohibited from receiving commissions for the sale of the insurance. Regulation 27A also contains protections governing the sale of group credit insurance such as required consumer disclosure, limits on amounts of insurance, and regulation of premium rates.

Some commenters made recommendations related to the existing exemption in the regulation for direct response solicitation. Comments ranged from expanding the scope of the exemption to limiting the scope of the exemption or completely removing the exemption. The recommendations appeared to stem from uncertainty about the meaning of the phrase "direct response solicitation." To address this issue, the phrase "direct response solicitation" was replaced with descriptive language clarifying that the exemption applies where the application is solicited and received in response to a generalized offer by the insurer by mail or under other methods without producer involvement and where there is no recommendation made.

Some commenters recommended an exemption from the regulation for corporate owned or bank owned life insurance products. The Department believes that an exemption is appropriate for corporate owned life insurance or bank owned life insurance issued pursuant to section 3205(d) of the Insurance Law where all benefits under the policy are payable to the corporate or bank policy owner. An exemption was not added for corporate or bank owned life insurance issued pursuant to section 3205(a)(1)(B) of the Insurance Law because the Department believes that small business owners and small partnerships purchasing insurance pursuant to section 3205(a)(1)(B) should benefit from the protections of this proposal.

<u>Definitions</u>

Several commenters requested narrowing the definition of “Recommendation” or “Transaction” to exclude in-force transactions. Some commenters stated that the inclusion of in-force transactions would increase cost and complexity to insurers and producers and may infringe upon a policyowner’s contractual rights with respect to her or his policy. Some commenters also suggested that any best interest requirement only apply to those transactions that generate compensation for the producers, which are the transactions most at risk of conflicted advice. In response, the Department amended the definition of “Transaction” to reflect a distinction between “Sales Transaction” and “In-Force Transaction.” The Department defined “In-Force Transaction” as any modification or election of a contractual provision with respect to an in-force policy that does not generate new sales compensation. Producers and insurers making recommendations with respect to in-force transaction must still act in the best interest of the consumer and have a reasonable basis to believe the consumer has been reasonably informed of the relevant features of the policy and consequences of the transaction, both favorable and unfavorable, but other requirements otherwise related to “Sales Transactions” have been narrowed or eliminated. The Department believes these changes will significantly reduce any costs for producers and insurers and will not infringe upon a policyowner’s contractual rights with respect to her or his policy.

Several commenters requested narrowing of the definition of “Recommendation” to exclude educational information. In response, the Department revised the definition to exclude general factual information.

Several commenters requested additional tailoring and/or narrowing of the definition of “Recommendation.” The Department has not revised the definition further because the Department believes the breadth of the definition is appropriate and should not be further narrowed or limited.

Several commenters requested tailoring the definition of "Suitability Information" by product type. In response, the Department addressed term insurance separately and maintained the definition for other products as the Department believes the breadth of the definition is sufficient.

Several commenters requested clarification that the definition of "Suitable" applies only to those products a producer has available to sell. In response, the Department clarified the definition, as this was the original intent. A producer is only required to consider those products which are available for her or him to offer. A producer is not required to consider or recommend to a consumer any products that she or he is not able to offer to a consumer. An insurer, where no producer is involved, is not required to consider or recommend all products available in the marketplace from any issuer, but must consider all products that the insurer itself offers to consumers.

Best Interest Standard

Several commenters requested that the language "without regard to the financial or other interests of the producer, insurer, or any other party" in section 224.4(b)(1) be removed, replaced or clarified. In response, the Department replaced the language to address concerns over the implication that "without regard to" may trigger legal cases in other contexts not intended to be addressed by this regulation. The new language reflects the Department's intent that all recommendations must be free of conflict and the Department does not believe the new language is inconsistent with the DOL Rule, Investment Advisors Act of 1940 or the proposed CFP Board standards of conduct. In addition, the Department did not replace the "without regard to" language with a standard proposed by some commenters that would simply place the interests of the consumer above those of the producer. Under such a standard, producers could consider their own financial interests when making a recommendation and therefore the Department does not believe that all transactions would be required to be in the best interest of the consumer under such a definition. The suggested revision is inconsistent with the Department's goal of implementing a best interest standard.

Some commenters requested that the best interest standard only apply to producers and not to insurers. The Department did not make this change, as the best interest standard does not apply to insurers when a producer is involved in the recommendation. In such cases, insurers are held to a suitability standard and other supervisory requirements as required under section 224.6.

A few commenters requested that references to "suitable" be replaced with "best interest" to achieve a true best interest and fiduciary standard. Conversely, the Department received comment suggesting the term "best interest" has been interpreted under common law to create a fiduciary obligation and therefore should be replaced with a different term. The Department has considered these comments but did not make any changes in response. It is the Department's objective to create a standard where recommendations are made in the best interest of consumers. The Department does not believe that the proposed best interest language is inconsistent with the DOL Rule or the proposed CFP Board standards of conduct. In addition, a best interest recommendation as set forth in section 224.4(b) requires an evaluation of the relevant suitability information and the recommendation to be suitable. The use of the term "best interest" in defining the best interest standard would be circular and create uncertainty.

A few commenters requested section 224.4(b) be revised to require producers to recommend the product that a prudent expert would determine meets the insurance needs and financial objectives of the consumer. The Department did not make any changes in response, as the Department views best interest as an evaluation process resulting in a recommendation in the best interest of the consumer rather than a recommendation of the one singular product that is in the consumer's best interest. There may be more than one product that is consistent with a consumer's best interest.

Several commenters requested a revision to clarify that a recommendation in the best interest of the consumer does not require that the recommendation be the least expensive product available. The Department considered the comments but does not believe that any clarification is necessary. Best interest is an evaluation process resulting in a recommendation in the consumer's best interest. The Department agrees that best interest does not necessarily mean the least expensive product available.

Some commenters suggested a revision to add the phrase "acting in a like capacity" to the prudent person standard in 224.4(b)(1). In response, the Department added the requested language to clarify that the evaluation of the relevant suitability information reflects that of a prudent person acting in a like capacity.

A few commenters suggested that the requirement a producer have a reasonable basis to believe the consumer has the financial ability to meet the financial commitment under the policy is overly broad and should be removed, or alternatively be revised to clarify that the requirement does not apply to annuities that do not require additional premium payments. The Department did not make any revisions in response, as the Department believes it is important for consumers to be recommended policies with financial obligations they are able to meet. The Department believes a "reasonable basis to believe" standard adequately addresses this concern and is appropriate. In addition, the Department believes it is sufficiently clear that the requirement applies only to the extent of the financial commitment under the policy. In addition, this requirement is already required by FINRA Rule 2111.06 and is consistent with other regulatory regimes.

Disclosure and Documentation

Several commenters suggested that the duty to disclose "all relevant suitability considerations and product information" is too broad, not meaningful, overly burdensome or not reasonable. The Department has considered the comments requesting the language be deleted, replaced or clarified, but has decided not to make any changes in response. The Department believes that the requirement is appropriate and that all suitability considerations relevant to the recommendation should be disclosed to the consumer. The list of suitability criteria is not exhaustive, as any such list cannot possibly capture all of the factors that might be relevant to particular consumer and which would need to be considered by the producer. In response to one comment, providing such disclosure in the prospectus is insufficient because the proposal requires the disclosure to highlight all relevant suitability considerations and product information. The disclosure is intended to be consumer specific. One commenter requested that transactions through electronic distribution channels not involving a producer be exempt from the documentation and disclosure requirements. The Department did not make any changes in response, as the Department believes such disclosure and documentation is an integral component of any sales transaction regardless of whether the recommendation is made via an electronic platform. However, the Department recognizes how technology and electronic platforms could make the communications, disclosure and documentation more efficient, easier to maintain and easier to supervise.

One commenter suggested that the Department strengthen the documentation requirements to reinforce the best interest standard and to clarify that the producer must document the facts, assumptions and analysis that led the producer to conclude that the particular policy recommended is the best of the available options for the consumer. The producer is required to document these items with respect to the recommendation made; the producer is not required to document the reasons, facts and analysis that led to the conclusion that all other product considered were not in the best interest of the consumer. The Department believes the documentation requirements are appropriate. In response, the Department made a change to clarify that the facts and analysis that formed the basis of recommending a product must be documented. In addition, the Department views best interest as an evaluation process resulting in a recommendation in the consumer's best interest rather than one singular product that is in the consumer's best interest. In response to another commenter who expressed concerns about the effect of a documentation requirement for in-force policies, the Department made a change to the requirements for an "In-Force Transaction" that documentation is not required; documentation is required for a transaction with respect to an in-force policy if that transaction will generate new sales compensation to the producer, in which case that transaction falls under the definition of "Sales Transaction".

Producer Certifications, Designations and Titles

Many commenters requested revisions or clarification with respect to the requirement that a producer have a specific certification or professional designation if stating or implying that a recommendation is part of financial planning, financial advice or other related services. The Department considered the comments and in response made certain changes to section 224.4(i) to acknowledge that the sale of insurance may be considered financial advice or be a part of financial planning. However, the revisions do reflect the Department's concern where a producer states or implies that a recommendation is financial planning or constitutes comprehensive financial advice when the producer is not specifically certified or licensed in either of those areas. While some commenters requested a narrow list and others requested an expansive list, the Department decided not to set forth a specific list of acceptable certifications or designations so to avoid a list that may be unintentionally exclusive. In addition, the Department's revisions make clear that the use of such titles and designations are not appropriate if the producer does not actually sell securities or other non-insurance financial services. It is the Department's view that producers, even if certified or licensed as a financial planner, financial advisor or other similar title, should not hold themselves out as such if all they actually sell are insurance products. This requirement shall not prohibit or discourage producers from engaging in team-based recommendations so long as the capabilities of each specific producer within the team are not misrepresented in accordance with Sections 224.4(i) and 224.5(c).

Multiple Producer Sales

Many commenters requested revisions or clarification with respect to producers involved in a transaction who do not have direct contact with the consumer. The Department considered the comments and made revisions in response. The revisions clarify that the requirements are intended to apply to all producers who participate in making the recommendation and receive compensation as a result of the transaction. It is not necessary that the producer have any direct contact with the consumer.

Producer Compensation

One commenter requested a revision to the compensation disclosure requirement to require disclosure of how compensation is determined rather than the amount of compensation. The Department did not make any changes in response, as section 224.4(b)(3)(i) is clear that the manner in which the producer is compensated must be disclosed. A few commenters also suggested the compensation disclosure requirement is duplicative of the requirements in Regulation 194 and requested clarification whether the requirements applicable to compensation disclosure impose a new requirement in addition to the disclosure obligation under Regulation 194, or whether compliance with either requirement is acceptable. The Department does not believe the compensation disclosure requirements are duplicative because the proposal requires compensation disclosure in accordance with Regulation 194 and Insurance law section 119.

A few commenters suggested a revision to clarify that compensation paid to a producer can be in the form of cash or non-cash compensation. The Department did not make any changes in response, as the Department believes section 224.4(k) is sufficiently clear that nothing in the regulation prohibits the type or amount of compensation paid to a producer that is otherwise permitted under the Insurance Law.

Proprietary Products

Some commenters voiced concerns and requested revisions to address how the best interest standard would apply to producers who sell proprietary products. In response, the Department considered the concerns and revisions and created a new subsection (l) in section 224.4. The new subsection affords a producer selling proprietary products based on a captive or affiliation agreement with a particular insurer the ability to limit the policies it recommends if the nature and limitations of the agreement are fully disclosed to the consumer. The Department does not believe that producers who sell proprietary products are at a disadvantage compared to those producers who are independent. A proprietary producer who provides the proper disclosure to each and every consumer does not have to make products available that are outside the producer's captive or affiliation agreement with the insurer. The disclosure is required to set forth the circumstances under which a producer will and will not limit recommendations.

Financial Exploitation

Some commenters requested that the requirement to establish and maintain procedures designed to prevent financial exploitation and abuse should be removed and treated elsewhere. The Department did not accept the suggestion as the Department believes this requirement is appropriate.

Product Comparison Disclosure

Several commenters suggested that the policy and product comparison disclosure to consumers was too broad or burdensome. In response, the Department revised the proposal by limiting the comparison disclosure to those circumstances where the insurer offers different versions of a product, one with a fee based structure and one with a commission based structure. The Department believes this clarification will reduce the volume of disclosures provided to consumers, except where such disclosure is necessary for the consumer to make an informed purchasing decision.

Insurer Requirements and Supervision

Some commenters asserted that insurers should not be held to a suitability standard with respect to transactions where no recommendation is made. The Department did not make any changes in response, as the Department believes an insurer should not effectuate any transaction if it actually knows that such transaction is not suitable. The insurer's suitability obligation is based only on information actually known to the insurer at the time of the transaction.

Some commenters requested clarification and expansion of the section requiring that insurers establish a supervision system designed to achieve the insurer's and producer's compliance with the proposal. Some commenters recommended the elimination of incentives that could potentially lead a producer to make a recommendation not in the best interest of the consumer. The Department revised the proposal to set forth some general minimum standards. Insurers are required to establish, maintain, and audit a supervision system in order to reasonably ensure: (1) the collection of the consumer's suitability information with respect to "Sales Transactions;" (2) documentation and disclosure of the basis for any recommendation with respect to "Sales Transactions;" (3) the review of consumer complaints regarding recommendations that are inconsistent with the best interest of the consumer; and (4) the prevention of incentives intended to or that would reasonable be expected to cause producers to make recommendations that are not in the best interest of the consumers. Insurers are also required to audit and/or contemporaneously review producers' compliance with the requirements of the regulation. This review may be risk-based so long as the approach does not focus solely on recommendations posing the greatest risk with no review of other recommendations. The Department believes these clarifications will significantly reduce the time, complexity and cost of supervision.

Regulatory Impact Statement

One commenter asserted that the Regulatory Impact Statement should include reports or studies that evidence the need for the proposal. The Department made certain revisions to the Statement of Needs and Benefits section of the Regulatory Impact Statement to clarify that the Department has been monitoring news releases, published articles, reports from the DOL, and the DOL's Regulatory Impact Analysis for the DOL Rule, consumer complaints, and the market conduct of New York insurers and producers. According to the DOL's Regulatory Impact Analysis, the DOL found that conflicted advice is causing harm to consumers and that disclosure alone would not remedy the harm. This is consistent with the Department's own observations in New York. Like the DOL, the Department believes that regulatory action is necessary. The proposal will impose a consistent standard of care across life insurance and annuity product lines and protect consumers from conflicted advice. The Department has also had discussions with its regulated individuals and entities as well as with consumer groups. The Department believes the proposal is necessary in light of the growth and complexity of insurance products and the recent examinations of insurers.

There are currently over 160 licensed life insurance and annuity providers in New York State and over 143,000 insurance agents and 15,000 insurance brokers with the life insurance line of authority, each of which have different business models that may be impacted by the proposed amendment differently. These firms are also subject in various respects to the DOL Rule and, despite the uncertainty created by recent court cases, are at different levels of readiness for compliance with that regulation. The Department went to great lengths to ensure that the revisions to the proposed amendment were consistent with the core requirements of the DOL Rule but significantly less onerous in terms of supervision and compliance requirements. The Department believes that firms that have already brought themselves into compliance with the DOL Rule would have minimal additional costs to comply with the proposed amendment, regardless of whether or not the DOL Rule ultimately takes full effect. The Department further held multiple meetings with regulated entities and interested parties to ascertain which, if any, components of the proposed amendment might increase costs for particular firms; those provisions were then removed or significantly reduced in scope.

Importantly, the benefits of the regulation are expected to be substantial. Consumers often are unaware they have received conflicted recommendations from producers or insurers and the harm caused by such conflicts are not readily apparent, materialize over the many years of a life insurance policy or annuity contract or take the form of an "opportunity cost," i.e., the lost benefits from not having taken the option in the best interest of the consumer at the time. The elimination of conflicted recommendations to consumers is expected to yield cost savings to consumers in the form of lower cost and better suited product recommendations, lower transactions costs to remedy improper recommendations, fewer replacements of insurance policies and fewer complaints to producers and insurers over time.

Another commenter suggested that the Regulatory Impact Statement did not identify deficiencies in the current regulatory scheme regarding in-force policies that lead to consumer harm thereby demonstrating a need for the proposal. In response, the Department has distinguished between in-force transactions and sales transactions, and clarified in the Regulatory Impact Statement the need to require a best interest standard for transactions with respect to an in-force policy. The proposal further distinguishes the requirements for an in-force transaction and a sales transaction, which now includes any modification or election of a contractual provision that generates new sales compensation. Inclusion of such recommendations with respect to an in-force policy is important for consistency and to address potential consumer harm arising out of such recommendations that are not covered by the existing Regulation 187. The same conflicts that exist when a producer recommends the purchase of a policy can also be present when the producer recommends a transaction with respect to an in-force policy that generates new compensation for the producer, and it is important that those transactions be considered the same as and contained within the definition of sales transaction. For example, a recommendation to purchase additional insurance under an existing policy, for which the producer receives compensation, presents the same potential conflicts as a recommendation to purchase the additional insurance under a new policy. In both instances, the producer's recommendation should be based on the best interest of the consumer, not on the compensation that the producer will receive for the transaction.

One commenter asserts that the Regulatory Impact Statement fails to provide any evidence in the Needs and Benefits section that the annuity and life insurance market has grown more complex since 2013. Further, the commenter suggests that the current regulatory scheme is a well-functioning consumer protection system and that the proposal is not necessary. In response, the Department added clarification to the Needs and Benefits section of the Regulatory Impact Statement. Conflicted advice is causing harm to consumers and the Department agrees with the DOL's Regulatory Impact Analysis, which concludes that disclosure alone would not provide adequate consumer protection. The Department's experience and observation in reviewing and approving insurance products for sale in New York as well as conducting market conduct examinations of insurers has revealed an increased complexity in the market. The products submitted to the Department for approval since 2013 include more complex structures for annuities and life insurance products as industry innovation continues to evolve. Products often offer a wider range of benefits and the benefits are more complex, as discussed in the Regulatory Impact Statement, making disclosure alone inadequate and additional standards for producer knowledge, supervision and standards of care necessary. Also, a number of Department investigations and examinations since 2013 have demonstrated the need for a best interest standard of care for life insurance and annuity sales. In 2015, the Department launched an investigation of deferred-to-immediate annuity replacements, whereby consumers with in-force deferred and variable annuity contracts with robust income options were induced to replace those contracts with immediate annuity contracts providing lower benefits and where producers were then compensated for the replacements. On December 8, 2016, the Department issued Insurance Circular Letter No. 7, which reminds producers and insurers of their disclosure requirements and other suitability determination responsibilities related to these types of replacements. Multiple insurers have also been examined for compliance with 11 NYCRR 51 (Insurance Regulation 60), which requires extensive disclosure related to proposed replacements. In addition to violations of the disclosure requirements in Regulation 60, the Department also found many instances where sales and replacements that were clearly not in the best interest of consumers were justified on the basis of the existing suitability standard for annuities, or not justified at all due to a lack of an existing standard for life insurance. The Department believes, in light of all of the facts and its expertise, that a regulation is needed to prevent insurers and producers from recommending a transaction that is properly disclosed and determined to be suitable for a consumer, but that is otherwise not in the best interest of that consumer and is designed to maximize compensation to the sellers. This standard is missing from the current state regulatory scheme and once promulgated will provide a consistent standard of care across product lines and protect consumers from conflicted advice.

Some commenters suggest an inconsistency in the Needs and Benefit section of the Regulatory Impact Statement wherein the Department's goal of a consistent standard of care across life insurance and annuity product lines conflicts with the Department's decision to implement the proposal without waiting for other regulatory bodies such as DOL, SEC, FINRA, NAIC and other state insurance departments to act. The commenter states that potential variations will be confusing and harmful to consumers. New York has always been a strong leader in financial services regulation and will continue to lead on this issue. New York consumers should not be denied the protections of this proposal because other regulators in other jurisdictions have not adopted similar protections within their areas of authority. The Department does not consider waiting to see if other regulators develop (or never develop) standards to be a viable alternative.

The Department cannot analyze standards that other regulators may or may not develop in the future.

Some commenters asserted that the Costs section of the Regulatory Impact Statement should include the sources of the information on which the projected costs are based and the methodology upon which the cost analysis is based. Further, such commenters offered that the Department has underestimated the cost of people and systems needed to implement the proposal. In response, the Department has added clarification in the Statement of Costs section to underscore the flexibility of the proposal. The proposal takes a principle-based approach to compliance. The proposal does not impose any particular systems or procedures for meeting the requirements of the regulation. Rather, insurers and producers are free to leverage existing systems and procedures. For example, most producers already have systems and procedures in place to document information about their clients and to document their interaction or conversations with their clients. These existing systems and procedures can be leveraged to document the client's suitability information and the basis for the producer's recommendation to the consumer. Also, many insurers were already preparing to implement the DOL Rule by making changes to processes, procedures and technology. Although, recent conflicting court decisions have left uncertainty about the implementation of the DOL Rule, much of the work has already been done. Some producers have indicated an intention to move forward with implementing a best interest standard regardless of what happens with the DOL Rule. The Department anticipates that many insurers have already incurred up-front costs to achieve compliance with the DOL Rule so these insurers can leverage the systems that are already in place or are well under way. While there will likely be some up-front cost associated with this proposal, the Department believes that there will, over time, be a cost savings to insurers and producers that are able to apply the same standards across all life insurance and annuity product types and potentially avoid maintaining separate systems for separate product lines.

One commenter stated that the Duplication section of the Regulatory Impact Statement should be expanded to clarify that the DOL Rule applies to all qualified plan and IRA distribution recommendations and to the reinvestment of those distributions in any type of annuity or life insurance policy, as well as to clarify that future revisions to federal standards could result in duplication and/or conflict. In response, the Department has clarified the recommendations to which the DOL Rule applies, but has not further revised the section based on future potential duplication that could develop at a later date. Currently, there is no conflict with the portion of the DOL Rule that has been implemented. This is particularly true since very recent conflicting court decisions have left uncertainty about the implementation of the DOL Rule.

One commenter asserted that the Alternatives section of the Regulatory Impact Statement does not contain supporting analysis for the need to implement this proposal. In response, the Department revised the Alternatives section to clarify that since the promulgation of Regulation 187 in 2013, the Department has monitored developments in suitability standards and has ascertained that additional oversight and regulation is needed for a level playing field and to protect consumers. The Department has participated in discussions with various stakeholders regarding the potential impact of the DOL Rule on producers and insurers. The Department has also participated in discussions with the NAIC's suitability working group and is monitoring developments of additional suitability standards considered by the NAIC. The Department has conducted outreach to discuss issues that have arisen as a result of the DOL Rule. The Department considered not implementing the amendment, but the Department has rejected this alternative because doing nothing would be disadvantageous to consumers. Moreover, New York consumers should not be denied the protections of this proposal because other regulators in other jurisdictions have not adopted similar protections within their areas of authority. The Department is the sole regulator for the overwhelming majority of insurance activities occurring in New York State. Federal agencies such as the DOL and SEC or self-regulatory agencies such as FINRA have only concurrent jurisdiction with the Department over only those products that are both insurance products and securities; the regulation of all other life insurance and annuity products and sales is within the sole purview of the Department. The Department maintains unique expertise related to comprehensive insurance markets and products that makes it appropriate for the Department to lead on issues of insurance regulation. A shortcoming of federal regulations, either by the DOL or the SEC, is that those entities' limited jurisdiction with respect to life insurance and annuity products would create a two-tiered standard of conduct for different types of annuities and life insurance products which would be harmful and confusing for consumers and producers alike.

Several commenters expressed concern with the compliance schedule of the proposal to life insurance and annuity transactions. In response, the Department revised the Compliance Schedule within the Regulatory Impact Statement. The amendment will take effect on March 1, 2019 for any transaction with respect to an annuity contract and September 1, 2019 for any transaction with respect to a life insurance contract.

One commenter disagreed with the Department's conclusion within the Job Impact Statement that the proposal will not have a substantial impact on jobs and employment opportunities in New York. The Department did not make any changes to the Job Impact Statement. Several commenters representing producers and insurers stated that producers and insurers already work in the best interest of consumers every day and are committed to operating in their clients' best interests. The Department believes that enacting a best interest standard could promote the industry and benefit producers. Although recent conflicting court decisions have raised uncertainty about the implementation of the DOL Rule, parts of the rule did take effect prior to those conflicting decisions. New York did not observe any significant negative impact on jobs in New York as a result. Also, while there is currently uncertainty about the DOL Rule, some producers have indicated an intention to move forward with implementing a best interest standard regardless of what happens with the rule. One commenter suggested that the proposal will impact producers' financial situation in that the proposal disallows consideration of the producers' own financial interests when recommending products to consumers. The Department believes that consideration of a producers' own financial interests in the making of a recommendation is not in the best interest of the consumer. Although the commenter attempted to compare potential job impact under the DOL Rule to potential job impact under the Department's proposal, this is not a proper comparison because New York's proposal differs from the DOL Rule in important ways. For example, while the DOL rule creates a private right of action for consumers, the New York proposal does not. It is the Department's understanding that the private right of action was the factor that raised the greatest concern about potential job impact. This factor is not an issue for the New York proposal.

One commenter asserted that the Regulatory Flexibility Analysis for Small Businesses and Local Governments does not adequately address the adverse economic impact on small businesses. Also, the commenter asserts a contradiction in the Regulatory Flexibility Analysis for Small Businesses and Local Governments since the Department states the proposal is a new higher standard of care but the same as the current standard. In response, the Department has clarified in the Regulatory Flexibility Analysis for Small Businesses and Local Governments that many producers and insurers are already using a best interest standard of care for consumers. In fact, several commenters representing producers and insurers stated that producers and insurers have been committed to operating in their clients' best interests for years. The Department does not see the supposed "contradiction" noted by the commenter. The proposal contains a higher standard (best interest) than the current Regulation 187 (suitable), but the industry has said that many producers and insurers are already meeting the higher standard of a best interest standard of care even though it has not yet been required under existing state regulatory framework. Given this and the fact that most producers already have systems and procedures in place to document information about their clients and to document their interaction or conversations with their clients, any impact on small businesses is expected to be minimal.

Effective Date and Enforcement

One commenter recommended adding language to section 224.7 of the proposal to specify what action the Superintendent would take in the event of a violation of the regulation. The Department did not add such language. The Superintendent's enforcement authority is already addressed in the Insurance Law. Action taken by the Superintendent in response to a violation of the regulation will be in accordance with the Insurance Law and will depend on the facts and circumstances of the particular violation.

Several commenters requested changes to the effective date. The Department revised the effective date of the proposal to March 1, 2019 and added a new Section 224.9 to provide that insurers and producers requiring compliance with the requirements as to annuities on the effective date, and the requirements as to life insurance within six months from the effective date, to ensure consumers are treated fairly and to provide sufficient time for compliance.