

**PROPOSED REGULATION OF THE
COMMISSIONER OF INSURANCE**

LCB FILE NO. R165-18I

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**PROPOSED PERMANENT REGULATION OF
THE COMMISSIONER OF INSURANCE**

LCB File No. R ____ - ____

June 22, 2018

EXPLANATION – Matter in *italics* is new; matter in brackets [~~omitted material~~] is material to be omitted.

AUTHORITY: NRS 679B.130 and 686A.015.

A REGULATION relating to insurance; requiring insurers to establish a system to supervise recommendations and to set forth standards and procedures for recommendations to consumers that result in transactions involving annuity products so that the insurance needs and financial objectives of consumers at the time of the transaction are appropriately addressed.

Section 1. Chapter 688A of NAC is hereby amended by adding thereto the provisions set forth as sections 2 to 7, inclusive, of this regulation.

Sec. 2. 1. *"Best interest" means, at the time the annuity is issued, acting with reasonable diligence, care, skill and prudence in a manner that puts the interest of the consumer first.*

2. "Best interest" does not mean a resulting recommendation is the least expensive annuity product, or the annuity product with the highest stated interest rate or income payout rate, available in the marketplace at the time of the annuity transaction. "Best interest" also does not mean the recommendation is the single "best" annuity product available in the marketplace at the time of the annuity transaction, but based on the insurance producer's judgment acting with reasonable diligence, care, skill and prudence, the producer believes the recommendation is in the best interest of the consumer.

Sec. 3. "Continuing education provider" or "CE provider" means a Designated representative as defined by NAC 683A.322.

Sec. 4. "FINRA" means the Financial Industry Regulatory Authority or a succeeding authority.

Sec. 5. "Replacement" has the meaning as ascribed to it in NAC 686A.526.

Sec. 6. "Suitability information" means information that is reasonably appropriate to determine the suitability of a recommendation, including the following:

- 1. Age;*
- 2. Annual Income;*
- 3. Financial situation and needs;*
- 4. Financial experience;*
- 5. Financial objectives;*
- 6. Intended use of the annuity;*
- 7. Financial time horizon;*
- 8. Existing assets or financial products, including investment and life insurance holdings;*
- 9. Liquidity needs;*
- 10. Liquid net worth;*
- 11. Risk tolerance, including changes in nonguaranteed elements in an annuity contract;*
and
- 12. Financial resources used to fund the annuity, including potential surrender charges, tax implications, and penalties that could be incurred by using these funds; and tax status.*

Sec. 7. An insurance producer shall not solicit the sale or replacement of an annuity product unless the insurance producer has adequate knowledge of the product to recommend the

annuity, and the insurance producer is in compliance with the insurer's standards for product training. An insurance producer may rely on insurer-provided product-specific training standards and materials to comply with this subsection.

1. (a) *An insurance producer who engages in the sale of annuity products shall complete a one-time four (4) hour training course approved by the Division of Insurance.*
(b) Insurance producers who hold a life insurance line of authority on the effective date of this regulation and who desire to sell annuities shall complete the requirements of this subsection within six (6) months after the effective date of this regulation. Individuals who obtain a life insurance line of authority on or after the effective date of this regulation may not engage in the sale of annuities until the annuity training course required under this subsection has been completed.
2. *The training required under this subsection shall include information on the following topics:*
 - (a) *The types of annuities and various classifications of annuities;*
 - (b) *Identification of the parties to an annuity;*
 - (c) *How product specific annuity contract features affect consumers;*
 - (d) *The application of income taxation of qualified and non-qualified annuities;*
 - (e) *The primary uses of annuities;*
 - (f) *Financial exploitation of seniors and other vulnerable adults; and*
 - (g) *Appropriate sales practices, replacement and disclosure requirements, including the requirements under this regulation.*
3. (a) *Providers of courses intended to comply with this subsection shall cover all topics listed in the prescribed outline and shall not present any marketing information or*

provide training on sales techniques or provide specific information about a particular insurer's annuity products. Additional topics may be offered in conjunction with and in addition to the required outline.

(b) A training course that complies with the requirements of FINRA Rule 1250 meets the requirements of subsection 2.

- 4. A provider of an annuity training course intended to comply with this subsection shall register as a continuing education provider in this State per NAC 683A.327, and comply with the rules and guidelines applicable to insurance producer continuing education courses as set forth in the Continuing Education section of the Nevada Administrative Code under NAC 683A.318 to NAC 683A.370, inclusive.*
- 5. Annuity training courses may be conducted and completed by classroom or self-study methods given that the course has been approved as required under NAC 688A.335.*
- 6. Providers of annuity training shall comply with the reporting requirements and shall issue certificates of completion in accordance with NAC 683A.340.*
- 7. The satisfaction of the training requirements of another state that are substantially similar to the provisions of this subsection shall be deemed to satisfy the training requirements of this subsection in this state.*

An insurer shall verify that an insurance producer has completed the annuity training course required under this subsection before allowing the producer to sell an annuity product for that insurer. An insurer may satisfy its responsibility under this subsection by obtaining certificates of completion of the training course or obtaining reports provided by commissioner-sponsored database systems or vendors, or from a reasonably reliable commercial database vendor that has a reporting arrangement with approved insurance education providers.

Sec. 8. 686A.526 of NAC is hereby amended as follows:

“Replacement” defined. “Replacement” means a transaction in which a new policy is to be purchased and the agent or insurer who proposes the replacement knows or should know, by reason of the transaction, that an existing policy has been or will be:

1. *Lapsed, forfeited, surrendered or partially surrendered, assigned to the replacing insurer or otherwise* ~~terminated~~;
2. Converted to reduced paid-up insurance, continued as extended term insurance or otherwise reduced in value by the use of nonforfeiture benefits or other values in the policy;
3. Amended to reduce benefits or to reduce the term for which coverage would otherwise remain in force;
4. Reissued with any reduction in the cash value of the policy; or
5. Pledged as collateral or subjected to borrowing for an aggregate amount that exceeds 25 percent of the loan value set forth in the policy.

Sec 9. 688A.455 of NAC is hereby amended as follows:

688A.455 Recommendations: Responsibilities of insurer or producer of insurance~~;~~
~~corrective action~~].

1. Except as otherwise provided in subsection ~~24~~, ~~[before an insurer or a producer of insurance recommends to a person the purchase of an annuity, or the exchange of an annuity that results in the purchase or exchange of an annuity in accordance with the recommendation, the insurer or producer of insurance must make reasonable efforts to obtain:~~
~~(a) The financial and tax status of the person;~~

~~(b) The investment objectives of the person; and~~

~~(c) Any other information that the insurer or producer of insurance determines~~

~~would be useful in making such a recommendation.] 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 only make a recommendation that furthers the insurance needs, financial objectives, and is in the best interest of the consumer at the time it is made based on 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, including the consumer's suitability information.~~

2. *Prior to the recommendation of an annuity, an insurance producer, or an insurer where no producer is involved, shall do all of the following:*

(a) Make reasonable efforts to obtain the consumer's suitability information;

(b) Evaluate the types of financial products which correspond to the consumer's disclosed suitability information and address the consumer's financial objectives; and

(c) Provide disclosure of the following information to the consumer:

(1) The scope of services provided;

(2) The scope of the producer's licenses;

(3) Material conflicts of interest arising from financial incentives associated with the recommendation, including any direct interest or ownership the producer or an immediate family member of the producer has in the insurer whose product is being recommended; and

(4) The sources and types of compensation the producer will or may receive as a result of the recommended transaction.

3. In making a recommendation, the insurance producer, or insurer where no producer is involved, shall have a reasonable basis to believe all of the following:

(a) The consumer has been reasonably informed of various features of the annuity, such as the potential surrender period and surrender charge, potential tax penalty if the consumer sells, exchanges, surrenders or annuitizes the annuity, mortality and expense fees, investment advisory fees, potential charges for and features of riders, limitations on interest returns, insurance and investment components and market risk;

(b) The consumer would benefit from certain features of the annuity, such as tax-deferred growth, annuitization or death or living benefit;

(c) The particular annuity as a whole, the underlying subaccounts to which funds are allocated at the time of purchase or exchange of the annuity, and riders and similar product enhancements, if any, further the insurance needs, financial objectives, and are in the best interest of the consumer (and in the case of an exchange or replacement, the transaction as a whole furthers the insurance needs, financial objectives, and is in the best interest of the consumer) for the particular consumer based on his or her suitability information; and

(d) In the case of an exchange or replacement of an annuity, the exchange or replacement furthers the insurance needs, financial objectives, and is in the best interest of the consumer including taking into consideration whether:

- (1) The consumer will incur a surrender charge, be subject to the commencement of a new surrender period, lose existing benefits (such as death, living or other contractual benefits), or be subject to increased fees, investment advisory fees or charges for riders and similar product enhancements;*
- (2) The consumer would benefit from product enhancements and improvements and the replacing product would provide a substantial financial benefit to the consumer over the life of the product;*
- (3) The consumer has had another annuity exchange or replacement and, in particular, an exchange or replacement within the preceding 60 months; and*
- (4) This section is a supplement to and does not replace the requirements of NAC 686A.573 or NAC 686A.577 concerning replacement of an annuity contract.*

4. 1. Before an insurer or a producer of insurance recommends to a person the purchase of a variable annuity, or the exchange of a variable annuity that results in any additional insurance transaction, the insurer or producer of insurance must make reasonable efforts to obtain:

- (a) The information described in subsections 1 *and* 2; or
- (b) The information described in ~~{Conduct Rule 2310 of the National Association of Securities Dealers}~~ *the FINRA requirements pertaining to suitability, including but not limited to FINRA Rule 2111.*

2. The requirements of Section 9 shall be in addition to any applicable duties and requirements placed on producers of insurance in NRS chapter 628A and Sec. 1.7, subsection 1, of the 2017 Nevada Legislature Senate Bill 383.

5. *Except as permitted under subsection 6, an insurer shall not issue an annuity recommended to a consumer unless there is a reasonable basis to believe the annuity furthers the insurance needs, financial objectives, and is in the best interest of the consumer based on the consumer's suitability information.*

~~3—Except as otherwise provided in subsection 4, if an insured is harmed financially because an insurer or a producer of insurance failed to comply with subsection 1 or 2, the Commissioner may require the insurer or producer of insurance to take corrective action.~~

~~4—An insurer or a producer of insurance is not responsible for any financial damages incurred by an insured relating to the purchase or exchange of an annuity that was recommended by the insurer or producer of insurance if the insured:~~

~~(a) Refused to provide to the insurer or producer of insurance the information described in subsection 1 or 2;~~

~~(b) Provided to the insurer or producer of insurance information that was incomplete or inaccurate; or~~

~~(c) Entered into an insurance transaction that was not based on the recommendation of the insurer or producer of insurance.]~~

6. *An insurer is not obligated to determine an annuity furthers the insurance needs, financial objectives, and is in the best interest of the consumer, but instead, shall determine the annuity is reasonable prior to issuance based on the circumstances actually known to the insurer at the time the annuity is issued if any of the following situations occur:*

(a) The producer makes no recommendation;

- (b) A recommendation was made and was later found to have been prepared based on materially inaccurate information provided by the consumer;*
- (c) A consumer refuses to provide relevant suitability information and the annuity transaction is not recommended; or*
- (d) A consumer decides to enter into an annuity transaction that is not based on a recommendation of the insurer or the insurance producer.*

7. An insurance producer or, where no insurance producer is involved, the responsible insurer representative, shall at the time of sale:

- (a) Make a record of any recommendation and the basis or bases of the recommendation subject to this regulation;*
- (b) Obtain a customer signed statement documenting a customer's refusal to provide suitability information, if any; and*
- (c) Obtain a customer signed statement acknowledging that an annuity transaction is not recommended if a customer decides to enter into an annuity transaction that is not based on the insurance producer's or insurer's recommendation.*

8. An insurance producer shall not dissuade, or attempt to dissuade, a consumer from:

- (a) Truthfully responding to an insurer's request for confirmation of suitability information;*
- (b) Filing a complaint; or*
- (c) Cooperating with the investigation of a complaint.*

9. An insurer is responsible for compliance with this regulation. If a violation occurs, either because of the action or inaction of the insurer or its insurance producer, the Commissioner may order:

- (a) An insurer to take reasonably appropriate corrective administrative action for any consumer harmed by the insurer's, or by its insurance producer's, violation of this regulation;*
- (b) A general agency, independent agency or the insurance producer to take reasonably appropriate corrective administrative action for any consumer harmed by the insurance producer's violation of this regulation; and*
- (c) Appropriate penalties and sanctions.*

Sec. 10. 688A.460 of NAC is hereby amended as follows:

1. An insurer shall *establish* ~~[provide for]~~ a *supervision* system ~~[to supervise recommendations which]~~ *that* is reasonably designed to ~~[comply]~~ *achieve the insurer's and its insurance producers' compliance* with the provisions of this chapter ~~[and which is established and maintained pursuant to subsections 3, 4 and 5. The system must include, without limitation, a process for maintaining written procedures and a process for reviewing records which is reasonably designed to detect and prevent violations of the provisions of this chapter.]~~ , *including, but not limited to, the following:*

- (a) The insurer shall maintain reasonable procedures to inform its insurance producers of the requirements of this regulation and shall incorporate the requirements of this regulation into relevant insurance producer training manuals;*
- (b) The insurer shall establish standards for insurance producer product training and shall maintain reasonable procedures to require its insurance producers to comply with the requirements of section 9 of this regulation;*
- (c) The insurer shall provide product-specific training and training materials which explain all material features of its annuity products to its insurance producers;*

- (d) The insurer shall maintain procedures for review of each recommendation prior to issuance of an annuity that are designed to ensure that there is a reasonable basis to determine that a recommendation furthers the insurance needs, financial objectives, and is in the best interest of a consumer. Such review procedures may apply a screening system for the purpose of identifying selected transactions for additional review and may be accomplished electronically or through other means including, but not limited to, physical review. Such an electronic or other system may be designed to require additional review only of those transactions identified for additional review by the selection criteria;*
- (e) The insurer shall maintain reasonable procedures to detect recommendations that do not further the insurance needs, financial objectives, and are not in the best interest of the consumer. This may include, but is not limited to, confirmation of consumer suitability information, systematic customer surveys, interviews, confirmation letters and programs of internal monitoring. Nothing in this subparagraph prevents an insurer from complying with this subparagraph by applying sampling procedures, or by confirming suitability information after issuance or delivery of the annuity; and*
- (f) The insurer shall annually provide a report to senior management, including to the senior manager responsible for audit functions, which details a review, with appropriate testing, reasonably designed to determine the effectiveness of the supervision system, the exceptions found, and corrective action taken or recommended, if any.*

2. A producer of insurance shall *establish* ~~[provide for]~~ a *supervision* system ~~[to supervise recommendations which]~~ *that* is reasonably designed to ~~[comply]~~ *achieve the insurer's and its insurance producers' compliance* with the provisions of this chapter ~~[and]~~

~~which is established and maintained pursuant to subsections 3, 4 and 5. The system must include, without limitation, a process for maintaining written procedures and a process for reviewing records which is reasonably designed to detect and prevent violations of the provisions of this chapter.] , including, but not limited to, the following:~~

(a) The producer of insurance shall maintain procedures for review of each recommendation prior to issuance of an annuity that are designed to ensure that there is a reasonable basis to determine that a recommendation furthers the insurance needs, financial objectives, and are in the best interest of the consumer. Such review procedures may apply a screening system for the purpose of identifying selected transactions for additional review and may be accomplished electronically or through other means including, but not limited to, physical review. Such an electronic or other system may be designed to require additional review only of those transactions identified for additional review by the selection criteria;

(b) The producer of insurance shall maintain reasonable procedures to detect recommendations that do not further the insurance needs, financial objectives, and are in the best interest of the consumer. This may include, but is not limited to, confirmation of consumer suitability information, systematic customer surveys, interviews, confirmation letters and programs of internal monitoring. Nothing in this subparagraph prevents an insurer from complying with this subparagraph by applying sampling procedures, or by confirming suitability information after issuance or delivery of the annuity.

3. ~~[An insurer may contract with a third party, including, without limitation, a producer of insurance, to establish and maintain a system to supervise recommendations pursuant to~~

~~the provisions of subsection 1 with respect to producers of insurance under contract with or employed by the third party.]~~ *Nothing in this subsection restricts an insurer from contracting for performance of a function (including maintenance of procedures) required under subsection 1. An insurer is responsible for taking appropriate corrective action and may be subject to sanctions and penalties regardless of whether the insurer contracts with a third party and regardless of the insurer's compliance with the provision of subsection 4.*

4. ~~[An insurer shall make a reasonable inquiry to ensure that a third party with whom the insurer contracts pursuant to subsection 3 complies with the provisions of subsection 1 and shall take reasonable action to enforce the contractual obligation to comply with the provisions of subsection 1. An insurer may comply with its obligation to make a reasonable inquiry by:]~~

An insurer's supervision system under subsection 1 shall include supervision of contractual performance under this subsection. This includes, but is not limited to, the following:

- (a) Monitoring and, as appropriate, conducting audits to assure that the contracted function is properly performed*~~[Obtaining a certification that the third party is complying with the provisions of subsection 1 from a senior manager of the third party who has responsibility for complying with the provisions of subsection 1];~~ *and*
- (b) Annually obtaining a certification from a senior manager who has responsibility for the contracted function that the manager has a reasonable basis to represent, and does represent, that the function is properly performed* ~~[Periodically reviewing the performance of the third party to determine whether the third party is complying with the provisions of subsection 1. The insurer shall use reasonable procedures in conducting the review].~~

5. The provisions of subsections 1 and 2 do not require an insurer or a producer of insurance to:
- (a) Review, or provide for the review of, all solicited transactions of a producer of insurance;
 - or
 - (b) Include in its system to supervise recommendations advice given to consumers by a producer of insurance concerning products other than the annuities offered by the insurer or producer of insurance.
6. A producer of insurance contracting with an insurer pursuant to subsection 3, when requested by an insurer pursuant to subsection 4, shall provide to the insurer a certification as described in subsection 4 or a clear statement that the producer of insurance is unable to meet the criteria for certification within 10 days after the producer of insurance receives the request from the insurer.
7. A person may not provide a certification pursuant to paragraph (b) of subsection 4 unless:
- (a) The person is a senior manager with responsibility for complying with the provisions of subsection 1; and
 - (b) The person has a reasonable basis for making the certification.
8. *Sales made in compliance with FINRA requirements [~~Compliance with Conduct Rule 2310 of the National Association of Securities Dealers~~] pertaining to suitability *standards and supervision of annuity transactions shall satisfy [satisfies]* the requirements of this section [~~for the recommendation of variable annuities~~]. *This subsection applies to FINRA broker-dealer sales of annuities if the suitability standard and supervision is similar to those applied to variable annuity sales. However, nothing in this subsection shall limit the Commissioner's ability to enforce (including investigate) the provisions of this regulation.**
9. *For subsection 8 to apply, an insurer shall:*

(a) Monitor the FINRA member broker-dealer using information collected in the normal course of an insurer's business; and

(b) Provide to the FINRA member broker-dealer information and reports that are reasonably appropriate to assist the FINRA member broker-dealer to maintain its supervision system.

10[9]. An insurer that contracts *for performance of a function* ~~[with a third party]~~ pursuant to subsection 3 and that complies with the requirements set forth in subsection 4 shall be deemed to have complied with the provisions of subsection 1.