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July 21, 2015

Office of Regulations and Interpretations
Employee Benefits Security Administration
Attn: Conflict of Interest Rule – Retirement Investment Advice
Room N-5655
U.S. Department of Labor
200 Constitution Avenue NW
Washington, DC 20210

RE: **RIN 1210-AB32 –** Definition of the Term "Fiduciary"; Conflict of Interest Rule – Retirement Advice; Proposed Rule
ZRIN 1210-ZA25 – Proposed Best Interest Contract Exemption; Proposed Amendment to and Proposed Partial Revocation of Prohibited Transaction Exemption 84-24 for Certain Transactions Involving Insurance Agents and Brokers, Pension Consultants, Insurance Companies and Investment Company Principal Underwriters

Dear Sir or Madam,

On behalf of NAFA, the National Association for Fixed Annuities, I write today with respect to the Department of Labor's proposed Conflicts of Interest rule, defining who is a "fiduciary" in regard to providing retirement investment advice, as well as the proposed new Best Interest Contract Exemption and the amended Prohibited Transaction Exemption 84-24 (collectively, the "Proposed Rule").

Founded in 1998, NAFA is an advocacy trade association, exclusively dedicated to educate and inform state and federal regulators, legislators, industry personnel, media, and consumers about the value of fixed annuities and their benefits to Americans in financial and retirement planning. NAFA's membership includes insurance companies, independent marketing organizations, and individual producers, representing every aspect of the fixed annuity marketplace and covering 85% of fixed annuities sold by independent agents, advisors, and brokers.

NAFA is pleased to have the opportunity to comment on the Proposed Rule and generally supports the Department's efforts to provide enhanced protections for consumers in the retirement marketplace.

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However, as currently drafted, the Proposed Rule requires significant refinements to ensure that Americans continue to have access to fixed annuities and to the financial professionals who provide the education and services necessary to service their clients. This is especially true for consumers who have investable assets of less than $250,000. At a time when a huge retirement savings gap exists, compounded by the fact that Americans are living longer, regulatory efforts must not hinder the principal-protected savings and lifetime income options uniquely provided by fixed annuities.

The Department appropriately recognizes that non-security annuities – in other words, fixed annuities – are insurance products and asks in its preamble to the Proposed Rule whether the line between insurance and annuity products that are securities and those that are not has been correctly drawn.[1]

NAFA appreciates the opportunity to answer the Department's invitation to comment on the disclosure requirements and other applicable standards governing fixed annuities, the distribution methods and channels applicable to fixed annuities, the common structure of insurance agencies, and the applicability of the Best Interest standard to fixed annuities. However, NAFA contends that fixed annuities are different from securities investments, and we believe the Proposed Rule must not be written so broadly that it has an adverse effect on insured retirement savings and on the insurance professionals who provide consumers with education and retirement advice on fixed annuity products.

The first section of this Comment letter provides an overview of the insurance product and fixed annuities marketplace and discusses why it is entirely appropriate and correct to treat those transactions differently under any proposed expansion of the fiduciary standard.

The second section addresses some of NAFA's general concerns with the Proposed Rule as currently drafted, particularly what we believe will be the unintended consequence of limiting consumer choice and access to retirement advice and products.

The third section provides comments on the base Conflicts of Interest Rule, specifically addressing our concerns regarding the definition of the term "fiduciary," as well as the investment education carve-out and seller's exception.

[1] Proposed Best Interest Contract Exemption, 80 Fed. Reg. 21975

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The fourth section of this letter addresses the amendments to PTE 84-24 and discusses aspects of this exemption that we believe require additional clarification and/or modification.

I. Overview of the Fixed Annuity Insurance Marketplace

A. Fixed Annuities are insurance products, not investments, and should be treated differently under any amended fiduciary standard

First and foremost, fixed annuities are insurance products, not investments. This has been clear under both state and federal law for decades and was clarified under the Dodd-Frank Act.[2] As an insurance product, fixed annuities are regulated by an effective, robust, and time-tested state-based regulatory and compliance framework. State laws govern the organization and licensing of insurance companies, and state insurance departments oversee insurance company operations and agents' sales activities. Fixed annuity contracts and amendments must be filed with, and approved by, each state in which contracts are sold.

Moreover, as an insurance product, fixed annuities are insurance contracts and offer the insurance guarantees of (1) predictable income the owner cannot outlive, (2) protection from investment and market risk, and (3) minimum interest earnings in every economic climate.

Further, unlike securities investments, the sales transaction – the fixed annuity contract – is made between the consumer and the insurance company, and all payments made for the purchase of the fixed annuity contract are paid to the insurance company, not the agent or advisor. These payments are not offset by payment of commissions, but are credited into the consumer's account. The agent does not retain any type of control over the funds.

Key distinctions about fixed annuities include:

- All fixed annuities satisfying state standard non-forfeiture laws ("SNFL") requirements are considered insurance products and are not considered to be securities.[3]

[2] The Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, H.R. 4173.
[3] Generally speaking, the Standard Nonforfeiture Law requires that an individual deferred annuity contract provide the contract holder with a paid-up annuity or cash surrender benefits of a minimum amount, if the contract holder surrenders the policy prior to its maturity date. The nonforfeiture

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- Fixed annuities satisfying standard state non-forfeiture laws must follow state-mandated reserving, guaranteed annuitization payout requirements and disclosure laws.
- In all fixed annuity contracts, the insurance company provides contractual guarantees that a minimum SNFL value will accrue, as well as guarantees protecting the contract owner from market downturns. The insurance company retains the market risk.
- A fixed annuity contract owner does not have a separate account, and interest is paid from the insurance company's general funds.

Insurance products like fixed annuities have no downside market risk and provide state-mandated guarantees to the consumer that investment products cannot provide due to their inherent risk factors. Hence, state regulation already provides a high level of consumer protection and, as will be discussed below, impose standards on insurance agents that the fixed annuity is suitable for the consumer. Thus, NAFA agrees the Department has appropriately categorized fixed annuities as covered transaction eligible for an exemption under PTE 84-24.

B. Insurance Agents who sell fixed annuities are subject to rigorous and comprehensive licensing requirements.

The bar to become a licensed insurance agent is significant. Insurance agents are bound to act in accordance with the common law requirements of agency and must pass tests of both competency and character before they are granted a state license.[4] Insurance agents need to be licensed in each state in which they operate. Only state-licensed life insurance agents may sell fixed annuity contracts.

After an agent has secured a license from the state, he or she must find an insurance company that will appoint or contract with them, and permit them to act as their selling agent. Insurance carriers review each and every application for appointment, and it's not unusual for an agent to be denied the opportunity to contract with that

amount is a state-mandated portion of the deferred annuity's paid premium, minus any previous withdrawals and certain charges, accumulated at interest rate minimums regulated by statute.

[4] To use the State of Missouri as an example, an individual may be refused a license – or may have his or her license revoked, suspended or not renewed – if the individual has been convicted of a crime involving moral turpitude or if the individual has used fraudulent, coercive, or dishonest practices or demonstrated untrustworthiness or financial irresponsibility in the conduct of business in the state or elsewhere—note that the latter may be a disqualifier even without a criminal conviction. Missouri Rev. Stat., Chapter 375, Provisions Applicable to All Insurance Companies, §375,141(6), (10) (2014), http://www.moga.mo.gov/mostatutes/chapters/chapText375.html.

carrier. This review process occurs each time the agent applies for appointment with a new or additional insurance company.

Once licensed and appointed, and before an insurance agent may sell a fixed annuity, he or she must complete, in addition to the regular and ongoing insurance continuing education requirements, insurer-provided product-specific education to ensure the agent's compliance with the insurer's standards for product training, as well as a one-time, 4-credit annuity suitability training course. The suitability training course includes information regarding the types and various classifications of annuities; the uses of annuities; appropriate sales practices, replacement, and disclosure requirements; how product-specific annuity contract provisions affect consumers; the identification of parties to an annuity; and the application of income taxation of qualified and non-qualified annuities.

C. Insurance agents do not have continued management of or control over the consumer's assets.

With investment advice, the consumer pays the investment advisor to manage his or her money. The consumer gives the money to the investment advisor who then places it in different investment instruments, moving the money around, reallocating it, buying and selling different assets such as stocks and bonds, all in accordance with an investment plan that the advisor has developed. For this service – to provide advice and make decisions about the assets under management – there are ongoing, usually annual, fees that an investor pays to the advisor.

With a fixed annuity, however, the money is not controlled or managed by the insurance agent; the money is paid to the insurance company. A fixed annuity sale is a one-time transaction between the client and the agent. The agent does not have access to the assets used to purchase the fixed annuity and cannot alter anything in the annuity contract.

If the consumer in a fixed annuity transaction is dissatisfied for any reason, he or she may first return the fixed annuity contract for a full refund during the free-look period, which typically ranges between 10 and 30 days. Outside of the free-look period, a fixed annuity consumer can submit complaints to the insurance company or to the state insurance department. If the insurance company or state insurance department finds in favor of the consumer, corrective action is taken by the insurance company to make the consumer whole.

D. Fixed annuity distribution methods and channels are unique to the insurance industry.

Fixed annuities are distributed and marketed in a wide variety of different distribution models, with each and every sale complying with a robust and effective state regulatory compliance framework. There are many different types of salespersons who distribute fixed annuities. Some of these insurance agents operate as "career agents" of carriers, "captive agents" of a carrier, "independent agents" for one or several carriers, employees of carriers or distribution firms, and the like. Some of these agents work directly with carriers, while others may be required by contract or practice to sell only certain types of fixed annuities.

Fixed annuities may be distributed through bank, wire house, broker-dealer, captive, independent, or other sales channels. In some cases, the consumer may contract directly with the insurance carrier without working with an insurance agent. In some instances, the insurance agent selling a fixed annuity may have a securities license and be subject to certain rules and requirements of their broker-dealer for which they are affiliated. Some of these broker-dealers may supervise the sale of certain types of fixed annuities, while others treat insurance sales as outside business activity. Registered Investment Advisor ("RIA") firms and Investment Advisory Representatives ("IARs") of RIAs may too also have varying oversight rules of fixed annuity sales.

While there is a wide array of distribution methods, what is clear is that every salesperson selling fixed annuities must comply with all applicable state insurance regulatory requirements.

All states have comprehensive rules and regulations that govern the sales practices, disclosure, training, conduct, and consumer protection standards that ensure fixed annuities are marketed, sold, and distributed to consumers with fairness, transparency, and recourse in mind. This robust state-based insurance regulatory system has been developed over the past hundred years and has proven to work very effectively. Moreover, state laws and regulations, as well as the insurance agent contracts that carriers require insurance agents to execute, make clear that these salespersons are agents of the carriers.

E. Current disclosure requirements for fixed annuities are comprehensive, provide meaningful information to consumers, and are sufficient to protect consumers' financial interests.

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In the preamble to the Proposed Rule,[5] the Departments invites specific comment on the current disclosure requirements applicable to insurance and annuity contracts that are not securities and asks whether the proposed transaction disclosure requirements can be revised for non-security annuities in such a way to provide meaningful information to consumers. As the following discussion demonstrates, fixed annuities are already subject to comprehensive disclosure requirements and do not warrant additional federal disclosures other than the ones specifically recommended herein.

State insurance departments regulate the sales practices for fixed annuities and include robust regulations related to required disclosure information. States require that a written disclosure statement be provided to the purchaser of a fixed annuity contract at the point of sale to both protect consumers and foster consumer education. The majority of states have adopted the National Association of Insurance Commissioners (NAIC) Annuity Disclosure Model Regulation. In addition, the NAIC updated its Annuity Buyer's Guide in 2013, which is included as part of the Model Regulation's disclosure requirements.[6]

At a minimum, the Model Regulation requires that the following information is included in the disclosure document:

(1) The generic name of the contract, the company product name, if different, and form number, and the fact that it is an annuity;

(2) The insurer's legal name, physical address, website address, and telephone number;

(3) A description of the contract and its benefits, emphasizing its long-term nature, including examples where appropriate:

(a) The guaranteed and non-guaranteed elements of the contract, and their limitations, if any, including for fixed indexed annuities, the elements used to determine the index-based interest, such as the participation rates, caps or spread, and an explanation of how they operate;

(b) An explanation of the initial crediting rate, or for fixed

[5] 80 FR 21975.

[6] The states that have not yet adopted the revised model disclosure regulation do, however, have state insurance regulations concerning annuity disclosure requirements; moreover, insurance companies that operate on a nationwide basis have adopted internal policies and protocols that meet or exceed the state or model requirements and apply them in all states.

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indexed annuities, an explanation of how the index-based interest is determined, 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;

(c) Periodic income options both on a guaranteed and non-guaranteed basis;

(d) Any value reductions caused by withdrawals from or surrender of the contract;

(e) How values in the contract can be accessed;

(f) The death benefit, if available and how it will be calculated;

(g) A summary of the federal tax status of the contract and any penalties applicable on withdrawal of values from the contract; and

(h) Impact of any rider, such as a long-term care rider.

(4) Specific dollar amount or percentage charges and fees shall be listed with an explanation of how they apply; and

(5) Information about the current guaranteed rate or indexed crediting rate formula, if applicable, for new contracts that contain a clear notice that the rate is subject to change.

In addition to requiring a product-specific disclosure statement, as previously noted, the disclosure requirements include the delivery of a free Annuity Buyer's Guide that must be provided no later than five days after receipt of the annuity contract application. The NAIC created the Annuity Buyer's Guide in collaboration with the insurance industry and consumer groups.

F. Beyond disclosure requirements, additional state-based laws and rules impose a comprehensive and effective regulatory system over fixed annuities.

In addition to the Annuity Disclosure Model Regulation, state insurance departments have adopted comprehensive regulations related to the sale of fixed annuities. Insurance companies have, in turn, implemented policies to carry out these rules and objectives. They include the following:

1. Suitability in Annuity Transactions Model Regulation

Originally adopted in 2003 as the Senior Protection in Annuity Transactions Model Regulation, the Suitability Model Regulation now applies to all fixed annuity transactions, regardless of the age of the purchaser. It establishes a system for state regulators and insurance carriers to supervise recommendations to purchase

annuities and sets forth standards and procedures for fixed annuity transactions so that the insurance needs and financial objectives of consumers at the time of the transaction are appropriately addressed.

The Suitability Model Regulation was most recently updated in 2010, imposing more extensive suitability standards on the sale of fixed annuities, clarifying that the insurance company is responsible for ensuring compliance with the suitability standards, including the review of all recommendations prior to the issuance of a contract, and requiring insurance agents to undergo mandatory product-specific training as well as general suitability training before making any fixed annuity recommendation.

In fact, these enhanced suitability requirements were codified in the Dodd-Frank Act of 2010,[7] requiring the adoption of suitability standards that are modeled after the most-recent NAIC Suitability Model Regulation by the state in which the insurance annuities are sold or by the insurer issuing the contract.

Currently 35 states, plus the District of Columbia, have adopted the 2010 version of the Suitability Model, with three additional states in the process of its adoption. Moreover, insurance companies that operate on a nationwide basis have adopted practices and protocols that meet or exceed the standards set forth in the 2010 model.

2. Insurance and Annuity Replacement Model Regulation

The purpose of this NAIC model law is to regulate the activities of insurers and producers with respect to the replacement of existing life insurance and annuities, by establishing minimum standards of conduct to be observed in replacement or financed purchase transactions. The regulation ensures that those who decide to purchase a replacement annuity receive the information necessary to make an informed purchase decision.

3. Advertisements of Life Insurance and Annuities Model Regulation

This regulation establishes minimum standards and guidelines to assure a full and truthful disclosure to the public of all material and relevant information in the advertising of life insurance and annuity products.

4. State "Free Look" (or Right to Return) Requirements

Most states require that insurance annuity contracts include a "free look" or "right to return" provision, allowing annuity contract purchasers the right to cancel their

[7] The Harkin Amendment was added to the Dodd-Frank Act, H.R. 4173, as section 989G, and is codified as a note to 15 U.S.C. §77c(a)(8).

contract within a certain number of days of the contract's delivery – typically between 10 – 30 days. In fact, the Annuity Buyer's Guide calls particular attention to this feature, as follows:

> ***When You Receive Your Annuity Contract***
> When you receive your annuity contract, carefully review it. Be sure it matches your understanding. Also, read the disclosure or prospectus and other materials from the insurance company. Ask your annuity salesperson to explain anything you don't understand. In many states, a law gives you a set number of days (usually 10 to 30 days) to change your mind about buying an annuity after you receive it. This often is called a **free look** or **right to return** period. Your contract and disclosure and prospectus should prominently state your free look period. If you decide during that time that you don't want the annuity, you can contact the insurance company and return the contract. Depending on the state, you'll get back all of your money or your current account value.

5. Use of Senior Specific Certifications and Professional Designations in the Sale of Life Insurance and Annuities Model Regulation

While this model regulation is targeted squarely at protecting senior consumers, it sets forth standards to protect *all* 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 fixed annuity product.

6. State Insurance Unfair Trade Practice Laws

The NAIC's Unfair Trade Practices Act provides the framework to regulate trade practices in the business of insurance by defining and prohibiting a broad range of conduct and practices that constitute unfair methods of competition or unfair or deceptive activities or practices. This Model Act was most recently revised in 2008, and most states have adopted this Act or similar regulations. Adoption of the Act grants broad powers to State Insurance Commissioners to examine and investigate the affairs of every person or insurer in the state to determine if the person or insurer is engaged in any unfair trade practices.

7. Market Conduct Exams

All state departments of insurance have the regulatory authority to investigate carriers and insurance agents to ensure compliance with applicable laws and regulations. State departments of insurance will each examine its domestic carriers on a regular basis. More than 40 state departments of insurance, working in conjunction with the NAIC, will annually collect compliance related data from all

carriers via the Market Conduct Annual Statement. This data is utilized to identify "outliers" and address potential issues through a market conduct exam or targeted exam regarding specific issues.

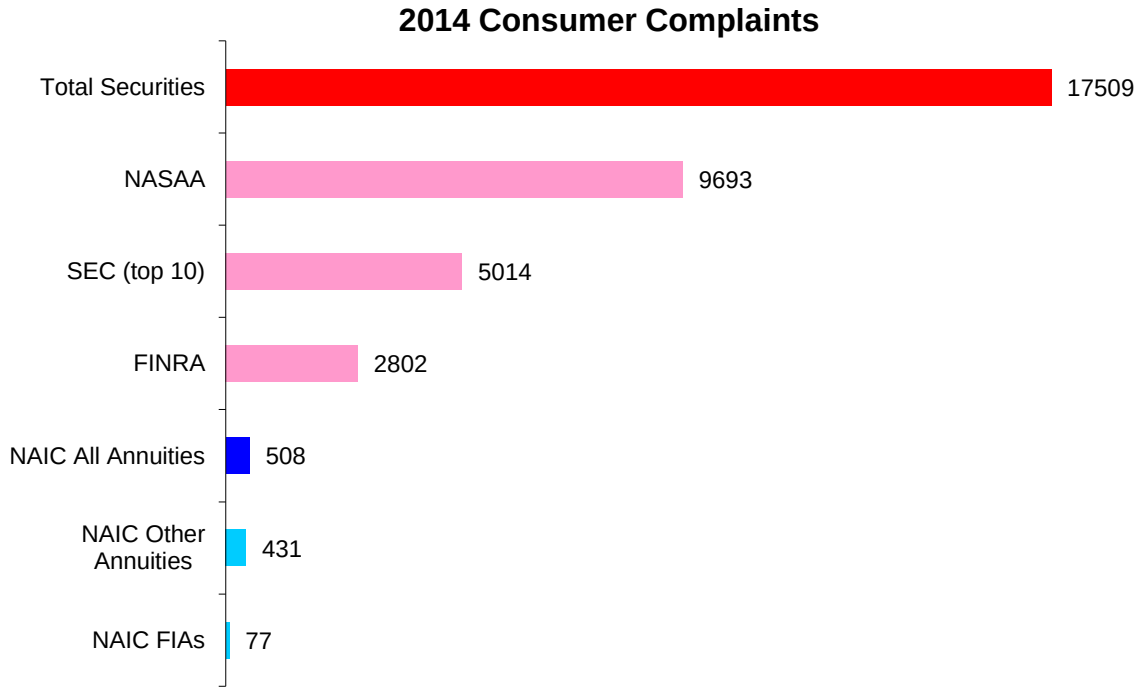
We include here links to the following documents discussed in this Section:

- NAIC Annuity Disclosure Model Regulation (MDL-245)
- NAIC Suitability in Annuity Transactions Model Regulation (MDL-278)
- NAIC Standard Nonforfeiture Law for Individual Deferred Annuities (MDL-805)
- NAIC Life Insurance and Annuities Replacement Model Regulation (MDL-613)
- NAIC Advertisements of Life Insurance and Annuities Model Regulation (MDL-570)
- NAIC Annuity Buyer's Guide – Fixed Deferred
- NAIC Use of Senior Specific Certifications and Professional Designations in the Sale of Life Insurance and Annuities Model Regulation (MDL-278)
- NAIC Unfair Trade Practices Act (MDL-880)

G. The protections provided by the state regulatory structure has resulted in a very low number of consumer complaints for fixed annuities.

The state-based regulatory structure governing the manufacture, distribution, and sale of fixed annuity products is effective as demonstrated by the minimal number of consumer complaints. In fact, in 2014 consumer complaints involving securities and advisors represented over 97% of combined annuity and securities complaints – but only .03% of total complaints were lodged by owners of fixed annuities.[8] This low number of complaints involving fixed annuities demonstrates the effectiveness of the state-based regulatory structure.

[8] Data Sources: FINRA: http://www.finra.org/newsroom/statistics; NAIC: https://eapps.naic.org/documents/cis_aggregate_complaints_by_coverage_types.pdf; SEC: http://www.sec.gov/news/data.htm; NASAA: http://www.nasaa.org/regulatory-activity/enforcement-legal-activity/enforcement-statistics/ (*NASAA only has compiled complaints for 2013)



As the preceding discussion demonstrates, the current state-based regulatory oversight of fixed annuity transactions is most effective in protecting consumers' financial interests when they purchase these contracts. State Insurance Departments oversee all aspects of the transaction: from the development and approval of each fixed annuity product sold in the state to the operations and compliance protocols of the insurance companies to the licensure and sales activities of the individual agents. In each instance, the objective is to protect the financial interests of the fixed annuity purchaser. In all practicalities, this comprehensive regulatory scheme serves the best interest of the consumer.

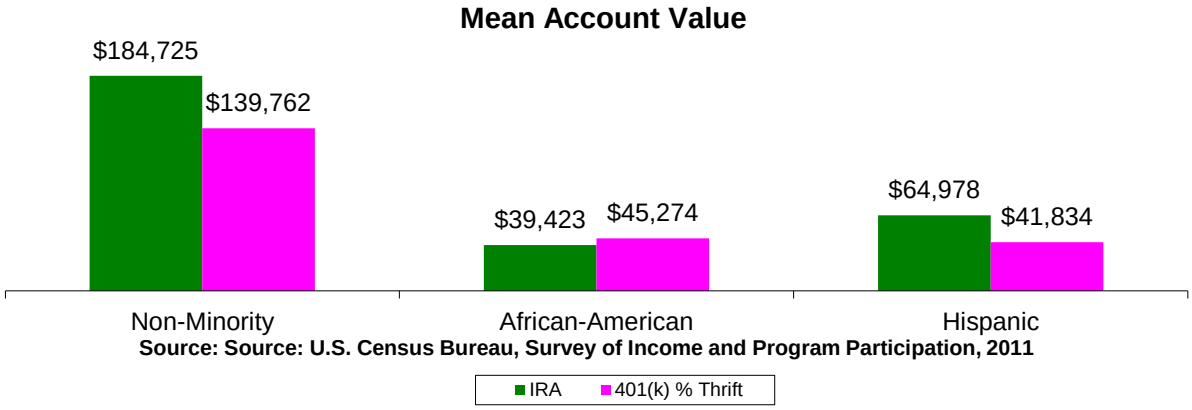
II. While NAFA appreciates the Department's efforts to provide enhanced protections for retirement investors, the Proposed Rule would cause tremendous disruption in the distribution and sale of fixed annuities, disproportionately impacting lower- and middle-income consumers.

A. A fiduciary-only standard, without workable exceptions, will ultimately harm the consumers it was intended to protect.

As NAFA understands the Proposed Rule, the Proposed Rule is premised on the assumption that a commission-based payment model creates an inherent, de facto conflict of interest that works to the detriment of consumers. Consequently, the Proposed Rule disallows commission-based compensation for all qualified accounts unless the transaction was permitted under a Prohibited Transaction Exemption ("PTE"). The Department creates a paradigm whereby only fee-based compensation could avoid the conflict of interest.

NAFA disagrees with this assumption. While fee-based advice may be appropriate for some consumers, it does not follow that a one-size-fits-all prescriptive payment model is appropriate for all consumers or retirement products.

More than 80% of fee-based advisors define their core market as clients with a minimum of $250,000 of investable assets.[9] The real world consumer marketplace reality is that requiring a fiduciary-only standard discriminates against lower and middle income savers because they do not have sufficient assets to be accepted as clients by the vast majority of fee-based advisors. The bulk of middle and mass market financial assets are in qualified accounts where the median value of an IRA account is $34,000, and the median value of a 401(k) plan account is $30,000.[10]



Even if fee-based advisors were encouraged to drop their minimum asset requirements and accept consumers with investable assets of $100,000, this would still mean that a majority of retirement savers, particularly minority Americans, would have insufficient assets to meet the minimum requirement and would be

[9] Mary Beth Franklin, *Financial Planning for the Middle Class*, Kiplinger (online) August 2011, *available at* http://www.kiplinger.com/article/retirement/T023-C000-S002-financial-planning-for-the-middle-class.html

[10] U.S. Census Survey of Income Program and Participation, 2011, *available at* http://www.census.gov/people/wealth/files/Wealth_Tables_2011.xlsx.

unable to receive personal, individualized professional financial and retirement assistance.

Even if fee-based advisors eliminated a minimum asset requirement, few middle- or lower-income consumers could afford the fees the advisor would necessarily charge to cover their operating expenses.

A fiduciary-only rule without workable, common sense carve-outs effectively creates two classes of retirement consumers: the affluent who have sufficient assets to justify the time and fees of the advisor and the much larger mass market who will be unable to obtain in-person professional financial and retirement advice. Moreover, it would relegate many Americans to robo-advisors or internet-based sales, which would deny them in-person education on the importance of saving for retirement.

B. The fee-compensation model can create higher costs to consumers than under the commission-based compensation model.

In a 2014 survey of 55 Washington, D.C. area advisory firms, the median fee-based advisor minimum required assets under management was $1,000,000. Although ten of the surveyed advisory firms said they did not have a minimum asset requirement, the minimum annual fees listed for those firms ranged from $3,000 to $9,000. For a consumer with just $60,000 of investable assets, those first year fees would be the equivalent of 5% to 15% of his or her assets. [11]

By contrast, the typical minimum payment required to purchase a fixed annuity ranges from $5,000 to $25,000 – and is often less for a qualified account. Importantly, fixed annuity agents can and do provide the same professional service for all their consumers, whether the annuity purchase payment is $5,000 or $500,000.

When a fee-only advisor accepts smaller accounts, the annual fee is often at least 2% of the assets year after year after year. If we use a hypothetical consumer with $100,000 of investable assets, it is demonstrable that over time the consumer will pay more in fees to the investment advisor than the insurance company would pay in commissions to an insurance agent. For this example, we will assume that the yield is 3% and that the timeframe is 5 years.

[11] http://www.washingtonian.com/articles/work-education/top-money-advisors-2014-fee-only-financial-planners/index.php

Under the fee-based advisor alternative, the total advisor fees would be $10,190. However, that same consumer could purchase a fixed annuity for $100,000 from an insurance company. The entire purchase payment would earn interest under the contract, and no funds would be deducted to pay the agent's commission. The insurance company would make a one-time payment to the insurance agent of $2,400.[12] Thus, the consumer has paid nothing directly to the agent, and yet his or her annuity contract's value will grow based on the full premium payment. In the fee-based model, the consumer's investment is reduced over time by $10,190.

Often the justification for a fee-based, fiduciary-only standard is that it is less expensive for the consumer than is a commission-based compensation model. Although that may be true for consumers with substantial financial assets, it is not necessarily true for the majority of consumers. Over time, the upfront commission paid by the insurance company to the agent is less than the ongoing, annual, cumulative fees paid to the investment advisor, who is managing the investment account.

III. The Proposed Rule's significant expansion of what constitutes investment advice, thereby triggering fiduciary status, is overly broad.

While NAFA supports the Department's efforts to study and propose reasonable rules that can provide new consumer protection standards to better protect the financial interests of consumers, the changes to the definition of "fiduciary" as set forth in the Proposed Rule needs modification in order to preserve consumer access to financial professionals, to maintain broad choice in retirement savings products, and to ensure compliance certainty for product providers and financial professionals.

A. The definition of "fiduciary" should require a mutual understanding that the advice is individualized to the consumer and will serve as a primary basis for the investment decision.

The current definition of "investment advice" (and thus the trigger for fiduciary obligations) under ERISA section 3(21)(A)(ii)[13] requires that the investment advice

[12] Per annuityratewatch.com, 6/26/2014, examining 37 multiple-year guarantee annuity policies with a 5-year rate guarantee.
[13] See 29 CFR §2510.3-21.

rendered to the plan is provided on a regular basis pursuant to a mutual agreement, arrangement, or understanding, written or otherwise, between the person rendering the advice and the plan and that such advice serves as the primary basis for investment decisions with respect to plan assets. (Emphasis added.)

The Proposed Rule, in addition to expanding the definition to include investment advice to IRAs and IRA owners, eliminates the requirements that the advice is rendered on a regular basis and that the advice serves as the primary basis for the investment decisions with respect to the plan. It would also no longer require a mutual understanding between the parties, but would rather capture advice that is "individualized to" or "directed to" the advice recipient "for consideration" in making investments decisions with respect to the plan or IRA.

NAFA does not disagree with the notion that a one-time rendering of investment advice might create a fiduciary relationship, so we do not object to the removal of the "regular basis" element from the current definition. However, we believe it would serve the best interests of the advice recipient if the person rendering the investment advice were able to define, through disclosure, the scope of the fiduciary duty as to its duration – whether ongoing, one-time, or limited in time relative to the particular plan or IRA investment transaction.

Our greater concerns with the proposed changes to the definition are the removal of the requirement that the agreement, arrangement or understanding be mutual and the elimination of the primary basis element such that the advice recipient need only consider the rendered advice in making plan or IRA investment decisions. Additionally, we are concerned that the inclusion of the term "directed to" will capture under the fiduciary standard communications that are more generalized in nature, such as marketing and advertising materials.

Additionally, the Proposed Rule needs clarification that it is the individual person who renders the investment advice who becomes the fiduciary to the plan or IRA, not the company whose products they recommend.

Consistent with the American Council for Life Insurers' position, NAFA believes that fiduciary obligations arise where the relationship between the financial professional and the consumer creates an expectation of trust. The investment advice industry has long functioned under the premise that "investment advice" that creates a trusted relationship between the financial professional and an investor must be customized and deemed suitable for and based on the needs of the specific investor.

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The Department's decision to capture communications that are merely "directed to" the advice recipient upends traditional passive marketing activity that is often the primary way by which investors become aware of their product and service options. In effect, the inclusion of communications that are merely "directed to" a potential consumer creates a presumption that the communication is investment advice , thus triggering a fiduciary relationship, a relationship which neither party intended, expected or agreed to. Further, the lack of clarity within the rule will have a chilling effect on all types of marketing activity, because the line between traditional marketing and fiduciary investment advice cannot be determined in advance with any degree of certainty.

Accordingly, NAFA suggests that the base definition of "fiduciary" under the Proposed Rule be revised as follows:

> § **2510.3-21 Definition of "Fiduciary."**
>
> (a) Investment advice. For purposes of section 3(21)(A)(ii) of the Employee Retirement Income Security Act of 1974 (Act) and section 4975(e)(3)(B) of the Internal Revenue Code (Code), except as provided in paragraph (b) of this section, an individual person renders investment advice with respect to moneys or other property of a plan or IRA described in paragraph (f)(2) of this section if—
>
> (1) Such person provides, directly to a plan, plan fiduciary, plan participant or beneficiary, IRA, or IRA owner the following types of investment advice, whether one time or ongoing, in exchange for a fee or other compensation, whether direct or indirect:
>
> (i) A recommendation as to the advisability of acquiring, holding, disposing or exchanging investments ~~securities or other property~~, including a recommendation to take a distribution of benefits (other than a distribution required by the plan or the Code) or a recommendation as to the investments ~~of securities or other property~~ to be rolled over or otherwise distributed from the plan or IRA;
>
> (ii) A recommendation as to the discretionary management of investments by a party other than the party making the recommendation ~~securities or other property~~, including recommendations as to the management of investments ~~securities or other property~~ to be rolled over or otherwise distributed from the plan or IRA;
>
> (iii) An appraisal, fairness opinion, or similar statement whether verbal or written concerning the value of investments ~~securities or other property~~ if provided in connection with a specific transaction or

transactions involving the acquisition, disposition, or exchange, of such investments ~~securities or other property~~ by the plan or IRA;

~~(iv) A recommendation of a person who is also going to receive a fee or other compensation for providing any of the types of advice described in paragraphs (i) through (iii)~~; and

(2) Such person, either directly or indirectly (e.g., through or together with any affiliate),—

(i) Represents or acknowledges that it is acting as a fiduciary within the meaning of the Act with respect to the investment advice described in paragraph (a)(1) of this section; or

(ii) Renders the investment advice pursuant to a written or verbal agreement, arrangement, or understanding that the advice is individualized ~~or that such advice is specifically directed to, the advice recipient for consideration in making investment or management decisions with respect to securities or other property of the plan or IRA.~~ to meet the specific investment goals of the investor, and is provided at the request of the investor pursuant to the agreement, arrangement, or understanding.

B. Agents must be able to sell fixed annuity products under the "seller's carve-out" without triggering fiduciary status.

As noted in Section I above, fixed annuity contracts are very different than securities products. With fixed annuities, consumers are not purchasing an investment that can be bought and sold in a bid market; they are entering into a legal contract with an insurance company.

Insurance agents cannot make any alterations to the terms, benefits, or commitments of the fixed annuity contract; in fact, they are prohibited from making any changes. They may not negotiate benefits on behalf of the annuity client, nor can they sell the contract to another party. Rather, insurance agents consider the annuity products that are available to sell from the insurance company or companies and make recommendations to their clients and prospective clients about the fixed annuity product contract options that would best serve the client's financial objectives.

As such, the sale of an insurance product by an insurance agent is not fiduciary in nature and should not trigger fiduciary obligations. The Department has recognized this distinction when it distinguishes "incidental advice as part of an arm's length transaction with no expectation of trust or acting in the customer's best interest,

from those instances of advice where customers may be expecting unbiased investment advice that is in their best interest."[14]

In a fixed annuity sales transaction, the contract purchaser understands that he or she is purchasing a proprietary insurance product and that the insurance agent represents the insurance company that designed the product. Moreover, the purchaser understands that the agent is not providing (and in fact cannot provide) impartial investment advice comparing the fixed annuity product against a universe of annuity products or investment products unavailable to the agent—but, rather, the agent is describing the value and benefits of the proposed fixed annuity product as part of the sales transaction.

NAFA believes that fixed annuity purchasers fully understand this agency relationship, but would nonetheless support reasonable disclosures or agreements that make clear that the insurance agent represents the insurance company and is selling only products then available to the agent.

Moreover, insurance agents selling fixed annuities deal directly with individual consumers and small plans. The Proposed Rule's carve-out for sellers is limited to transactions with large plans with either greater than 100,000 beneficiaries or with assets greater than $100 million. Given that there is no market risk to the consumer or plan purchasing an insurance product, the robust state insurance regulatory regime governing the transaction and the agent, including disclosures, NAFA recommends that the seller's carve-out under section 2510.3-21(b)(4) be expanded to state that the mere "selling" of non-security insurance products to a plan or IRA by a person does not constitute fiduciary investment advice as long as the proper state-mandated insurance and other appropriate sales disclosures are provided, and that the exclusion is not limited by the asset size or number of participants in the plan.

C. The narrowly-drawn education carve-out will result in consumers not having sufficient information to make informed retirement decisions.

NAFA believes it is essential that the Department maintain the important distinction between non-fiduciary investment *education* and fiduciary investment *advice*.

The Proposed Rule would radically change the way insurance agents communicate with their clients who are looking for sound and helpful retirement education. As

[14] 80 FR 21941.

NAFA understands the Proposed Rule, fiduciary obligations would be triggered at the first instance an insurance agent provides education material to a prospective client on a particular or specific annuity product to consider in a plan or IRA investment or distribution option. Additionally, any discussions about distributions and rollovers would be considered investment advice and, therefore, fiduciary in nature.

A narrow investment education carve-out would render these essential communications as little more than abstractions. Insurance agents must introduce clients to fixed annuities, help them understand the value proposition they provide in retirement planning, and educate them on the variety of annuities and their corresponding features.

The investment education carve-out under section 2510.3-21(b)(6) must make it clear that non-fiduciary education includes discussions about annuities generally, as well as discussions about particular product features that address concerns regarding liquidity, inflation, premature death, etc., including models generated with regard to such features. Purely informational discussions about annuities or distributions should not create a fiduciary relationship. The intense educational component of a fixed annuity sale is unique to this product.

Moreover, the Proposed Rule should clarify that fixed annuity advertising and marketing materials and illustrations that conform to state insurance laws and regulations should not be considered investment advice and should fall under the Rule's investment education carve-out.

Industry has been able to operate well under the Department's guidance on educational investment advice provided in Interpretive Bulletin 96-1. We strongly recommend that the proposed investment education carve-out be replaced with language that incorporates the guidance provided in IB 96-1.

IV. NAFA agrees that PTE 84-24 is the appropriate regulatory exemption for fixed annuities; however, the amended exemption requires further refinements to assist insurance companies and agents with their compliance duties and to protect the interests of retirees.

As stated previously, NAFA applauds the Department for recognizing the distinction between securities and insurance products. We agree with the

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Department that PTE 84-24 is the appropriate exemption to use for non-security annuity contracts (i.e., fixed annuities) when the insurance agent is acting as a fiduciary.[15] To confirm our understanding of the amendments to the exemption and to ensure that consumers of all investable asset size have continued choice and access to insurance retirement advisors, NAFA seeks clarification regarding the applicability and scope of PTE 84-24.

NAFA urges the Department to continue its long-time support of a regulatory exemption to support the efforts of life insurance companies, their partners in the fixed annuity distribution channels, and the individual insurance agents to offer everyday Americans access to products that provide a stream of retirement income that they will not outlive.

In that spirit, NAFA offers the following comments on proposed amended PTE 84-24:

A. Section I. Covered Transactions – Scope of the Exemptions.

The current proposal should better clarify those annuity contracts that are intended to be outside of PTE 84-24. NAFA seeks clarification from the Department that the intent is to disallow from this exemption (in addition to mutual fund shares) annuity products that are registered under federal securities law.

B. Section II. Impartial Conduct Standards – Best Interest.

Under Section II(a), the Impartial Conduct Standards are satisfied as it pertains to the sale of insurance products only when the insurance agent or insurance company

[15] NAFA notes that the Department invites public input regarding whether the conditions of the proposed Best Interest Contract (BIC) Exemption, other than the disclosure conditions, would be inapplicable to non-security annuities. (80 FR 21975.) Again, NAFA agrees that to the extent that an insurance agent may be acting as a fiduciary in relation to a plan or IRA transaction, PTE 84-24 is the appropriate exemption. Nevertheless, we would comment that the conditions of the BIC Exemption (BICE) are completely inapplicable to the sale of fixed annuities and would impose onerous and, frankly, unworkable conditions on the sale of these insurance products. In particular, we want to highlight the following points: the pre-recommendation contract requirement under BICE is entirely impractical in an insurance sales transaction. Requiring the insurance agent to warrant that he or she has complied with all applicable federal and state laws regarding the rendering of investment advice, places the insurance-only agent in an untenable position: insurance agents may not, under state or federal law, render investment advice as they are not securities registered. Should an insurance-only agent warrant that she or she is in compliance with all applicable securities laws, the agent would be in violation of both insurance and securities regulations and would be exposed to administrative and legal action.

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(a) acts in the "Best Interest" of the plan or IRA with respect to the assets involved in the transaction and (b) does not make misleading statements nor fail to disclose a "Material Conflict of Interest."[16]

'Best Interest' is later defined in the amended PTE as acting "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person would exercise based on the investment objectives, risk tolerance, financial circumstances and needs of the plan or IRA, *without regard to* the financial or other interests of the fiduciary, any affiliate, or other party."[17] (Emphasis added.)

'Material Conflict of Interest' is later defined as existing "when a person has *a* financial interest *that could affect* the exercise of its best judgment as a fiduciary in rendering advice to a plan or IRA."[18] (Emphasis added.)

NAFA is concerned with the breadth and ambiguity of the definitions of both "Material Conflict of Interest" and "Best Interest" under the proposed new Impartial Conduct Standards, and with their uncertain application to the insurance company that the agent may represent. Insurance agents and the companies for which they sell insurance products all have a financial interest in making a fixed annuity sale. Consumers understand that insurance agents receive compensation and that annuity providers must make money to stay in business in order to satisfy the insurance guarantees promised to the consumer. Without greater clarity it is conceivable that the payment of *any* commission would create – even with proper disclosure – a material conflict of interest under the proposed definition, inviting confusion and legal exposure as a violation of the Impartial Conduct Standards.

Moreover, the rule is unclear whether the Impartial Conduct Standards under Section II apply to the insurance company that issued the insurance product or annuity purchased with plan assets. Only the agent deals directly with the retirement investor and is the person who provides the investment advice that triggered the fiduciary duty in the first place. Thus, NAFA recommends clarifying the rule so that it is clear the impartial conduct standards apply only on the individual person who directly and personally provides investment advice to the Retirement Investor.

[16] 80 FR 22018.
[17] 80 FR 22020.
[18] Ibid.

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C. Section II. Impartial Conduct Standards – Assets Involved in the Transaction.

Unlike securities representatives, fixed annuity agents have a limited and defined array of products that they may recommend for purchase to a consumer. As discussed previously, insurance agents can only offer fixed annuity products that are available to them to sell from the insurance companies with which they have a contractual/agency relationship.

NAFA seeks clarification that when the assets involved in the transaction are fixed annuities, the Best Interest standard is met as long as the insurance agent considers all of the fixed annuity products that such agent is authorized by one or more insurance company to sell at the time the recommendation is made and acts in accordance with all applicable laws and regulations, including state insurance suitability requirements.

D. Section III. General Conditions – Reasonable Compensation.

Section III(c)(2) states that the combined total of all fees, Insurance Commission, and other consideration received by the insurance agent … or insurance company may not be in excess of "reasonable compensation." [19]

Section VI(f) further defines 'Insurance Commission' as "a sales commission paid by the insurance company or an Affiliate to the insurance agent … for the service of effecting the purchase or sale of an insurance or annuity contract, including renewal fees and trailer, but not revenue sharing payments, administrative fees or marketing payments, or payments from parties other than the insurance company or its Affiliates."[20]

NAFA believes that the term "reasonable compensation" needs to be clarified further and suggests that, as it pertains to Insurance Commissions, the determination as to whether compensation is "reasonable" should be fact-specific to the writing agent. In other words, the reasonable compensation would be based on the array of fixed annuity products and associated product specific commission arrangements available from the company or companies with whom the agent has an appointment or agent contract at the time of sale.

[19] 80 FR 22019.
[20] 80 FR 22020.

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Additionally, because it is difficult, if not impossible in practical terms, to determine the ultimate "compensation" to the issuing insurance company on the sale of a fixed annuity, the reasonable compensation analysis should be focused exclusively on the compensation received by the writing agent.

E. Section IV. Conditions for Transactions Described in Section (1)(a)(1) through (4).

Section IV(b)(1)(B) – As part of the required written disclosures with respect to the execution of the transaction, the Insurance Commission paid by the insurance company to the agent … in connection with the purchase of the recommended contract must be disclosed. NAFA seeks clarification that the disclosure is the sales commission paid by the insurance company to the writing agent for effecting the purchase of the fixed annuity contract.

Section IV(b)(2) – The Proposed Rule would require that the independent fiduciary acknowledge in writing receipt of the required disclosure information with respect to the transaction, as well as written approval on behalf of the plan [or IRA]. The marketplace reality is that parties who one would normally consider to be independent fiduciaries are not readily available in IRA transactions. Therefore, NAFA seeks clarification that the independent fiduciary is the IRA owner or plan recipient or beneficiary.

Section IV(d)(2) – With respect to repeated disclosure requirements for the purchase of subsequent or additional insurance or annuity contracts, Section IV(d)(2) states that written disclosures need not be repeated where the subsequent contract being recommended for purchase is not "materially different" from that for which the initial disclosures were obtained. NAFA seeks clarification regarding how the Department will define and apply the term "materially different."

Accordingly, NAFA proposes the following changes to the proposed amended PTE 84-24:

Revise Section I(a)(4) as follows:

> (4) The purchase, with plan assets, of an insurance or annuity contract from an insurance company <u>and the resulting receipt of compensation by the insurance company in connection with the purchase of the insurance or annuity contract</u>.

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Revise Section I(b) as follows:

The exemptions set forth in Section I(a) do not apply to the purchase by an Individual Retirement Account as defined in Section VI, of (1) a variable annuity contract or other annuity contract that is ~~a security~~ registered under federal securities laws, or (2) mutual fund shares.

Revise Section II, as follows:

If the insurance agent or broker, pension consultant, insurance company or investment company Principal Underwriter is a fiduciary within the meaning of ERISA section 3(21)(A)(ii) or Code section 4975(e)(3)(B) with respect to the assets involved in the transaction and provides investment advice directly and personally to the Retirement Advisor, the following conditions must be satisfied with respect to the transaction to the extent they are applicable to the fiduciary's actions:

Revise Section VI(b) as follows:

(b) The insurance agent or broker, pension consultant, insurance company or investment company Principal Underwriter that is a fiduciary acts in the "Best Interest" of the plan or IRA is when the fiduciary acts either with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person would exercise based on the investment objectives, risk tolerance, financial circumstances and needs of the plan or IRA or when providing advice that satisfies state suitability standards for insurance products ~~without regard to~~, and places the interests of the Retirement Investor before the financial or other interests of the fiduciary, any affiliate or other party.

Revise Section VI(h) as follows:

(h) A "Material Conflict of Interest" exists when a person has a material financial interest that ~~could~~ places the person's own financial interest before that of the Retirement Investor and thereby affects the exercise of its best judgment as a fiduciary in rendering advice to a plan or IRA.

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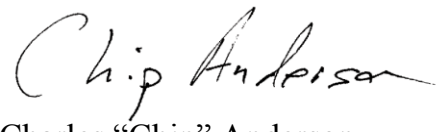
V. Conclusion

The Department has clearly devoted a great deal of time and effort in drafting the Proposed Rule, and NAFA commends those efforts. However, we firmly believe that the Proposed Rule as currently written, while well intentioned, will result in diminished access to financial and retirement advice and products, particularly for low- and medium-balance retirement savers and particularly for insurance products such as fixed annuity contracts. NAFA respectfully requests the Department to consider and implement the changes and revisions suggested in this letter, which we believe will result in greater clarity and understanding for the industry, while ensuring that the financial interests and goals of retirement consumers are fully met. Without these proposed changes, it would be impossible to meet all the requirements set forth by the Proposed Rule.

Again, on behalf of NAFA and its members, I want to thank you for the opportunity to submit these comments. We hope they will help the Department understand why the Proposed Rule should be amended as we have requested.

Please do not hesitate to contact me if you would like additional information or further clarification.

Sincerely,



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