

# New York's "Best Interest" Rule for Life and Annuities Found Constitutional

October 21, 2022

On October 20, 2022, New York State's highest court unanimously held that the First Amendment to New York Department of Financial Services ("NYDFS") Insurance Regulation 187 (11 NYCRR pt. 224), "Suitability and Best Interests in Life Insurance and Annuity Transactions" ("Regulation 187"), is constitutional. This decision marks the end of the debate over the constitutionality of the amended Regulation 187 and clarifies that the amended regulation remains in effect.

As we previously [discussed](#), the amended Regulation 187 sets forth the duties and obligations of producers when making recommendations to consumers with respect to any life insurance policy or annuity contract delivered or issued for delivery in New York to help "ensure that the transaction is in the best interest of the consumer and appropriately addresses the insurance needs and financial objectives of the consumer at the time of the transaction." 11 NYCRR 224.0(c). The best interest standard set forth in the amended Regulation 187 "requires a producer, or insurer where no producer is involved, to adhere to a standard of conduct to be enforced by the superintendent, but does not guarantee or warrant an outcome." *Id.* In a subsequent February 2020 guidance note, NYDFS clarified that Regulation 187: (i) is intended to be a principles-based approach, setting standards that must be met but also affording significant flexibility in how producers and insurers meet those standards; and (ii) does not impose any particular systems, forms or procedures for meeting the requirements of the regulation. Indeed, the principles-based approach and lack of particular systems—both of which were advocated by many in the industry leading up to Regulation 187's adoption—were focal points in the court's decision in striking down the amendment for being unconstitutionally vague.

Before the amended Regulation 187 became effective, the Independent Insurance Agents and Brokers of New York, Inc., the Professional Insurance Agents of New York State, Inc., Testa Brothers, Ltd. and Gary Slavin ("Petitioners") filed an Article 78 petition challenging the amendment, alleging that the promulgation of the amendment violated the State Administrative Procedure Act and that the amendment lacked a rational basis, was arbitrary and capricious and was otherwise unconstitutionally vague. The same day, the National Association of Insurance and Financial Advisors—New

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York State, Inc. also filed a petition challenging the amendment on similar grounds. On August 7, 2020, the Supreme Court dismissed both petitions on the merits, determining that NYDFS complied with the State Administrative Procedure Act in promulgating the amendment, that it did not unlawfully usurp legislative authority when it did so and that the amendment was not arbitrary, capricious, irrational or unconstitutionally vague. The Independent Insurance Agents and Brokers of New York, Inc. and Testa Brothers, Ltd. appealed.

As we previously [noted](#), the Appellate Division reversed the trial court's decision, concluding that the amendments violated due process rights and were unconstitutionally vague. Specifically, the Appellate Division held that "while the consumer protection goals underlying promulgation of the amendment are laudable, as written, the amendment fails to provide sufficient concrete, practical guidance for producers to know whether their conduct, on a day-to-day basis, comports with the amendment's corresponding requirements for making recommendations and compiling and evaluating the relevant suitability information of the consumer."

NYDFS appealed, and the New York State Court of Appeals reversed, concluding that NYDFS "appropriately exercised its authority to create a carefully considered and clear regulation" that was not unconstitutional. Specifically, the Court of Appeals addressed the three terms that Petitioners argued rendered Regulation 187 unconstitutionally vague on its face because they failed to provide notice of what conduct is or is not permitted: "recommendation," "suitability information" and "best interest."

"Recommendation" as defined in the amended regulation has both an objective and subjective definition. The objective definition is a statement or act that "reasonably may be interpreted by a consumer to be advice and that results in a consumer entering into or refraining from entering into a transaction in accordance with that advice." The subjective definition is a statement or act that "is intended by the producer . . . to result in a consumer entering into or refraining from entering into a transaction." Petitioners argued that "may be interpreted by a consumer" is too amorphous and too general to give notice of what conduct is prohibited. The Court held that neither the objective nor the subjective definition was unconstitutionally vague and that "[e]mploying long-accepted terms, the definition establishes clear, objective legal guidelines to ensure that a communication's legal impact will not depend on the sensitivities of a communications recipient [(i.e., the consumer)], and is both sufficiently definite to provide notice to those regulated and to prevent arbitrary enforcement."

"Suitability information" is defined as "information that is reasonably appropriate to determine the suitability of a recommendation commensurate with the materiality of the transaction to a consumer's financial situation at the time of the recommendation and the complexity of the transaction recommended." This includes various categories

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of information for life insurance and annuities (e.g., the consumer's age, annual income, financial situation). Petitioners challenged that both the definition and certain of its terms were unconstitutionally vague. The Court held that the regulation "provides flexibility as to what exact information a producer or insurer must consider for a particular consumer, [and] the definition of 'suitability information' provides clear boundaries for what must be considered." The Court also noted that the impetus for the amendment was to require that a producer or insurer may need to consider more data for the complex types of transactions that were the impetus for the amendment, and similarly more information may be needed when transactions involve a significant change to the consumer's finances. Petitioners argued that it is unclear in whose "best interest" a producer must act when making a recommendation. The Court found that the statute makes clear that producers must act in the best interest of the consumer. As to the term "best interest" itself, the Court explained that the regulation employs standard legal terms to explain exactly what a producer needs to do to discharge this duty and held that "following these steps does not require producers and insurers to identify the single best policy for a consumer. It simply requires them to reasonably recommend a suitable policy that will benefit the consumer, while refraining from considering their own financial gain."

The Court also addressed Petitioners' three alternative arguments for invalidating the amendment that the Appellate Division did not reach: (1) NYDFS exceeded its authority in promulgating the amended regulation; (2) NYDFS violated the State Administrative Procedures Act; and (3) the amendment is arbitrary and capricious. The Court found each of these arguments unavailing.

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Please do not hesitate to contact us with any questions.

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