

New York Issues Final Version of Best Interest Rule for Life and Annuities

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On July 18, 2018, the New York Department of Financial Services (the “NYDFS”) issued a final version of amendments to Regulation 187, which adopts a best interest standard in the sale of life insurance and annuities. The amended Regulation 187 will become effective for annuity products on August 1, 2019 and for life insurance products on February 1, 2020.

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While the final version of the rule leaves the best interest standard fundamentally unchanged, it includes several changes from earlier proposed versions in response to concerns expressed by the industry during the comment period.

First, the final version provides additional flexibility in implementing the best interest standard. The regulation sets forth several factors that can be considered when determining which product is in a consumer’s best interest and makes clear that incentive compensation paid to agents in accordance with New York law is still permissible. This last point was of particular concern to the industry, as earlier proposed versions appeared to call into question the traditional commission-based insurance compensation system. However, the core requirement of the regulation remains the same: Only the consumer’s best interest, and not the financial interests of the producer or insurer, can influence a recommendation.

Second, the rule clarifies that it can be enforced only by the NYDFS and does not provide a private right of action.

Finally, the rule clarifies safe harbor provisions and includes some limited relief regarding insurers’ obligations to supervise producer conduct under the regulation.

These changes represent significant improvements to the previously proposed versions on issues of importance to the industry. Practical problems remain, however, as it will likely be difficult for a producer or insurer to prove after the fact that a recommendation was not influenced by the incentive-based compensation. How Regulation 187 works in practice will depend on the NYDFS’ interpretation and enforcement of the rule, and industry groups will continue to work with regulators on these issues.

RULE CHANGES IN DETAIL

Best Interest Standard Clarified

- **Only the Interest of the Consumer Can Be Considered, but Receiving Compensation Does Not Violate the Standard.** The new rule confirms that only the consumer's interests can be considered in making a recommendation, but it broadens the permissible factors in making such a determination to include the benefits provided by the policy, the price of the policy, the financial strength of the insurer and other factors that differentiate products or insurers. The final rule also makes clear that producers may continue to receive all forms of compensation and incentives that are otherwise permitted under New York insurance laws and regulations so long as the compensation does not influence the recommendation.
- **Agent Compensation Can Vary, So Long as Recommendations Are Not Affected.** The final regulation eliminates language from the prior version which obligated insurers to establish standards and procedures to prevent incentives in compensation designed or expected to lead to recommendations that are not in the consumer's best interest. This language was viewed as jeopardizing the traditional commission-based insurance compensation system. Instead, the final rule authorizes an insurer to "maintain within and across product lines variations in compensation or other incentives that comply with the Insurance Law and the Insurance Regulations provided that the insurer's compensation and incentive practices, when taken as a whole, are designed to avoid recommendations by producers that are not in the best interest of consumers."

No Private Right of Action

- The final version removes a reference to Section 4226 of the New York Insurance Law, which permitted private rights of action, and further specifies that the conduct standards imposed by the regulation will be "enforced by the Superintendent."

Safe Harbor Provisions and Limits on Insurer's Obligation to Supervise

- Section 224.6 adds a new safe harbor permitting an insurer to rely on a producer's certification of compliance for in-force transactions even if they result in compensation to the producer. However, this safe harbor is not available for new transactions.
- Section 224.6 also adds clarifications to limit an insurer's obligations to supervise in several respects, including (i) eliminating an insurer's obligation to determine or confirm the suitability of transactions that result from the exercise of a contractual right in a policy (e.g., additional annuity deposits, policy loans), (ii) confirming that

an insurer's determination of suitability may be based on only its own products and (iii) clarifying that an insurer's obligation to ensure that a producer is trained does not entail a warranty that a producer is acting in a consumer's best interest.

- **Third-Party Supervision Permitted.** The rule permits insurers to use a third party to establish and maintain the system of supervision required by Regulation 187, though NYDFS is likely to take the view that insurers still bear ultimate responsibility for the third party's proper handling of that system.

Other Areas of Clarification

- **Required Documentation Clarified.** The final version adds language allowing disclosure of suitability considerations in a "reasonable summary format." In addition, while an insurer or a producer must still document if an individual refuses to provide suitability information or opts to undertake a transaction that is not recommended, the final version deletes the requirement to obtain a signed statement from the consumer in such circumstances.
- **No Recommendation Arises from the Use of an Interactive Tool Comparing Products.** Regulation 187 exempts from the rule's definition of "recommendation" the use by consumers of interactive tools that estimate insurance and other financial needs, compare products or refer a consumer to a producer.
- **Agents Cannot Call Themselves Financial Advisors.** The rule adds a provision barring an agent from calling himself or herself a financial advisor, financial planner or other similar title unless properly licensed as such and actually providing financial services beyond insurance, but the rule does authorize agents to state or imply that the insurance transaction is a component of a financial plan.
- **Additional Exemptions Added.** In addition to the exemptions added in the March 2018 revision of Regulation 187, the final version clarifies two categories of exemption:
 - The final rule does not apply to insurance applications received in response to a general offer, including at a place of employment, without producer involvement and clarifies that a producer or insurer may be involved to provide "customer service, administrative support, or enrollment services" without losing the exemption.
 - The final version also exempts corporate- or bank-owned life insurance policies where "substantially" all benefits under the policy are payable to a bank or corporate owner, deleting the earlier requirement that all such benefits must be payable to such owner.

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Please do not hesitate to contact us with any questions.

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