Ohio | Common Sense Initiative

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Business Impact Analysis

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Regulation/Package Title *(a general description of the rules' substantive content)*:
Suitability in annuity transactions.

Rule Number(s): ***3901-6-13***

Date of Submission for CSI Review: ***October 7, 2020***
Public Comment Period End Date: ***October 23, 2020 12:00am***

Rule Type/Number of Rules:

☐ New/ rules
☒ Amended/ ***1*** rules (FYR? ***No***)
☐ No Change/ rules (FYR?)
☐ Rescinded/ rules (FYR?)

The Common Sense Initiative is established in R.C. 107.61 to eliminate excessive and duplicative rules and regulations that stand in the way of job creation. Under the Common Sense Initiative, agencies must balance the critical objectives of regulations that have an adverse impact on business with the costs of compliance by the regulated parties. Agencies should promote transparency, responsiveness, predictability, and flexibility while developing regulations that are fair and easy to follow. Agencies should prioritize compliance over punishment, and to that end, should utilize plain language in the development of regulations.

Reason for Submission

1. R.C. 106.03 and 106.031 requires agencies, when reviewing a rule, to determine whether the rule has an adverse impact on businesses as defined by R.C. 107.52. If the agency determines that it does, it must complete a business impact analysis and submit the rule for CSI review.

   Which adverse impact(s) to businesses has the Agency determined the rule(s) create?

   The rule(s):

   ☐ a. Requires a license, permit, or any other prior authorization to engage in or operate a line of business.

   ☒ b. Imposes a criminal penalty, a civil penalty, or another sanction, or creates a cause of action for failure to comply with its terms.

   ☐ c. Requires specific expenditures or the report of information as a condition of compliance.

   ☐ d. Is likely to directly reduce the revenue or increase the expenses of the lines of business to which it will apply or applies.

Regulatory Intent

2. Please briefly describe the draft regulation in plain language.
   Please include the key provisions of the regulation as well as any proposed amendments.

   Annuities are long-term investments that are sold by life insurance companies and provide periodic income payments over a specified period of time. Annuities come in a variety of product types – including fixed, variable, and fixed indexed – that carry different degrees of risk and reward.

   State insurance departments have regulated the sale of annuities since 2003, in part to ensure that insurance companies and insurance agents sell consumers products that are appropriate for them, as well as to ensure consistency with the regulation of securities. The National Association of Insurance Commissioners (NAIC) adopted a model regulation (Model #275), which established a standard of "suitability," rule 3901-6-13 of the Ohio Administrative Code largely mirrors the requirements of the model.

   Beginning in 2017, the NAIC established a working group – chaired by Ohio – to revise the model regulation. In part, this effort was based on parallel movement to increase the standard of care for retail investors within the financial industry. The goal of the working group was to seek clear, enhanced standards for annuity sales so consumers understand the products they purchase, are made aware of any material conflicts of interest, and are assured those selling the products do not place their financial interests above consumers' interests. In February 2019, the NAIC membership approved the revisions to the model establishing a "best interest" standard.

The amendments to this rule will build on the leadership Ohio has established on this critical consumer protection and ensure that Ohio regulations are consistent with the uniform standards of the NAIC model and with all parallel federal regulations.

3. Please list the Ohio statute(s) that authorize the Agency to adopt the rule(s) and the statute(s) that amplify that authority.

   Sections 3901.041, and 3901.19 to 3901.26 of the Revised Code.

4. Does the regulation implement a federal requirement? ☒ Yes ☐ No
   Is the proposed regulation being adopted or amended to enable the state to obtain or maintain approval to administer and enforce a federal law or to participate in a federal program?
   ☐ Yes ☒ No
   If yes, please briefly explain the source and substance of the federal requirement.

   This rule brings Ohio law into compliance with the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Public Law Number 111-203, 111th Cong., 2d sess. (July 21, 2010).

5. If the regulation includes provisions not specifically required by the federal government, please explain the rationale for exceeding the federal requirement.

   Not applicable.

6. What is the public purpose for this regulation (i.e., why does the Agency feel that there needs to be any regulation in this area at all)?

   Annuities are long-term investments that come in a variety of product types and carry different degrees of risk and reward. The new standard ensures that consumers can expect that the licensed professionals they trust to make recommendations on annuity products are acting in the consumers' best interest. The revisions also require agents and insurers to act with "reasonable diligence, care, and skill" in making a recommendation. Insurers now have heightened supervision requirements to ensure compliance with the new standard. These requirements include knowing the consumer's financial situation and objectives, understanding the available options, having a reasonable basis for believing the recommended option is in the consumer's best interest, and disclosing their compensation and any conflicts of interest.

7. How will the Agency measure the success of this regulation in terms of outputs and/or outcomes?

   The rule provides important consumer protections by issuing guidance to insurance companies and agents in regard to annuity transactions. Success will be measured by a decrease in consumer complaints and improvement in consumer confidence.

8. Are any of the proposed rules contained in this rule package being submitted pursuant to R.C. 101.352, 101.353, 106.032, 121.93, or 121.931? ☐ Yes ☒ No

If yes, please specify the rule number(s), the specific R.C. section requiring this submission, and a detailed explanation.

Not applicable.

Development of the Regulation

9. Please list the stakeholders included by the Agency in the development or initial review of the draft regulation. *If applicable, please include the date and medium by which the stakeholders were initially contacted.*

   Initial development of the newly enacted NAIC model began with the formation of a working group in 2017. The working group held regular meetings in which various national stakeholders gave input into the drafting of the model. During the spring 2020 national meeting the model regulation was enacted by the NAIC. Since then, multiple states have began the process to enact the model regulation. The department incorporated the new model into existing rule 3901-6-13 of the Ohio Administrative Code.

   On Wednesday, June 10th the department sent the draft rule with request for comment to the following stakeholders: Association of Ohio Life Insurance Companies (AOLIC); American Council of Life Insurers (ACLI); Ohio Insurance Agents Association (OIA); Independent Insurance Agents and Brokers of America (IIABA); The Council of Insurance Agents and Brokers; National Association of Insurance and Financial Advisors; Ohio Chapter, American Fraternal Alliance; Ohio Insurance Institute (OII); Insured Retirement Institute (IRI); and American International Group (AIG).

   Based on comments received the department followed up via phone call with OIA and IIABA on Thursday July 23, 2020.

10. What input was provided by the stakeholders, and how did that input affect the draft regulation being proposed by the Agency?

    The department received multiple comments over the two week comment period. Most of the comments received were technical and structural in nature. Following internal review, many of the suggested amendments are incorporated into the final draft. Additionally, commenters raised issues similar to those discussed as part of NAIC deliberations. The department supports the national model and recognizes the necessity of uniformity in this area of regulation to support consumer protections. IRI requested an effective date for the rule of January 1, 2021. The department intends to file the rule accordingly. Nationwide Insurance submitted a comment of support for the draft rule.

11. What scientific data was used to develop the rule or the measurable outcomes of the rule? How does this data support the regulation being proposed?

Over the last two years the working group held multiple discussions with and received significant input from a wide array of stakeholders on incorporating into the model a heightened standard of conduct for producers and insurers to follow when recommending annuity products to consumers. Many state regulators and industry leaders worked to establish a regulatory framework that strikes a balance between regulatory flexibility and consumer protection. The working group also made significant efforts to remain cognizant of the work being done by other regulatory jurisdictions that overlap with the sale of annuities in order to reduce regulatory duplication and burden for those agents holding multiple licenses. As a result, these revisions align well with the Security & Exchange Commission's (SEC) Regulation Best Interest.

12. What alternative regulations (or specific provisions within the regulation) did the Agency consider, and why did it determine that these alternatives were not appropriate? If none, why didn't the Agency consider regulatory alternatives?

    With the goal of ensuring that consumers that are purchasing these types of products understand them and that the purchase of such a product is in their financial interest, and not driven by a particular product's compensation package – the state regulators and industry considered many different provisions and worked hard to strike a balance between flexibility and consumer protection. Additionally, the working group was keenly aware of the regulatory efforts of the SEC on this same topic and the NAIC model aligns with the SECs new regulations in this space. Further, the Dodd Frank Act generally requires that states must meet or exceed minimum requirements of the NAIC regulations regarding annuities or potentially face federal preemption.

13. Did the Agency specifically consider a performance-based regulation? Please explain. *Performance-based regulations define the required outcome, but don't dictate the process the regulated stakeholders must use to achieve compliance.*

    The proposed amendments to this rule establish a best interest standard. As outlined in the rule, to make appropriate product recommendations for consumers crucial consumer profile information is to be reviewed and considered. The regulation provides a minimum course of conduct and a minimum amount of information that must be considered. The course of conduct is described because the actual outcome for each customer may and likely will be different. A performance based regulation is not appropriate as the rule seeks to maintain a process of accountability to the consumer.

14. What measures did the Agency take to ensure that this regulation does not duplicate an existing Ohio regulation?

    The NAIC working group worked carefully to avoid duplication or conflict with other regulatory jurisdictions that overlap with the sale of annuities, including the Security & Exchange Commission's (SEC) Regulation Best Interest. When drafting the amendments to

the rule, the department reviewed Ohio statutes and rules and determined that these rules do not duplicate other regulations.

15. Please describe the Agency's plan for implementation of the regulation, including any measures to ensure that the regulation is applied consistently and predictably for the regulated community.

    The rule has been amended to delay implementation to January 1, 2021 at the earliest to allow industry more time for implementation and the development of industry training and compliance measures. Department staff will continue dialogue with stakeholders to ensure the rule is implemented clearly and applied consistently and address any issues that arise on an ongoing basis. The department maintains agent licensing, enforcement and market conduct divisions to assist both industry and Ohio consumers. Additionally, information will be available on our web site to address questions regarding the updated rule.

Adverse Impact to Business

16. Provide a summary of the estimated cost of compliance with the rule. Specifically, please do the following:
    a. Identify the scope of the impacted business community;
    b. Identify the nature of the adverse impact (e.g., license fees, fines, employer time for compliance); and
    c. Quantify the expected adverse impact from the regulation.
       The adverse impact can be quantified in terms of dollars, hours to comply, or other factors; and may be estimated for the entire regulated population or for a "representative business." Please include the source for your information/estimated impact.

    a. Insurance companies and agents engaging in the sale of annuities in the state of Ohio are impacted by the requirements of this rule.

    b. The existing rule and proposed amendments impact insurance agent training and diclosure requirements. Agents and companies will need to ensure complaince with training standards and will need to provide the new disclosure forms furnished in the rule, or one that is substantially similar. Staff time would be required to explain the policy to consumers each time an annuity transaction takes place.

    c. Costs associated with the continuing education requirements vary within the market, however, education requireemnts are already existing and should not impose additional costs. Required resources such as printed copies of the policies and disclosures are relative to the type and the frequency of the transactions.

17. Why did the Agency determine that the regulatory intent justifies the adverse impact to the regulated business community?

Ohio adopting the national model for standard of conduct allows the industry to foster consistency and predictability in regulation. The standards included in the model are critical for the protection of consumers and must be met or exceeded in order to remain in compliance with federal requirements established in Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Public Law Number 111-203, 111th Cong., 2d sess. (July 21, 2010).

Regulatory Flexibility

18. Does the regulation provide any exemptions or alternative means of compliance for small businesses? Please explain.

    This rule is promulgated to establish consumer protections and professional standards, the rule is adopted from the recently amended NAIC model which is established for national consistency. All insurance agents, agencies, and companies are expected to adhere to this rule regardless of size.

19. How will the Agency apply Ohio Revised Code section 119.14 (waiver of fines and penalties for paperwork violations and first-time offenders) into implementation of the regulation?

    Minor errors would be handled by advising the agent or insurer and giving them an opportunity to remedy the ommission.

20. What resources are available to assist small businesses with compliance of the regulation?

    Department staff is available to answer questions, regardless of the size of business. The department intends to continue dialogue with stakeholders through the finalization of the amendments to ensure compliance and facilitate questions. Additionally, the department will provide a guide for frequently asked questions regarding this rule on the department web site.