



Slater All Lines
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Pre-License Education and Continuing Education

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**WA Best Interest
Standards of Conduct
1 Hour Course**

#618870

Washington State Insurance

Continuing Education

2024

Produced by Slater All Lines Insurance School

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A. WA Best Interest Standards of Conduct (1 Hour Course).

<https://www.govinfo.gov/content/pkg/CFR-2022-title17-vol4/pdf/CFR-2022-title17-vol4-sec240-15l-1.pdf>

§ 240.15l-1 Regulation best interest. (a) Best interest obligation.

(1) A broker, dealer, or a natural person who is an associated person of a broker or dealer, when making a recommendation of any securities transaction or investment strategy involving securities (including account recommendations) to a retail customer, shall act in the best interest of the retail customer at the time the recommendation is made, without placing the financial or other interest of the broker, dealer, or natural person who is an associated person of a broker or dealer making the recommendation ahead of the interest of the retail customer.

(2) The best interest obligation in paragraph (a)(1) of this section shall be satisfied if:

(i) Disclosure obligation. The broker, dealer, or natural person who is an associated person of a broker or dealer, prior to or at the time of the recommendation, provides the retail customer, in writing, full and fair disclosure of:

(A) All material facts relating to the scope and terms of the relationship with the retail customer, including:

(1) That the broker, dealer, or such natural person is acting as a broker, dealer, or an associated person of a broker or dealer with respect to the recommendation;

(2) The material fees and costs that apply to the retail customer's transactions, holdings, and accounts; and

(3) The type and scope of services provided to the retail customer, including any material limitations on the securities or investment strategies involving securities that may be recommended to the retail customer; and

(B) All material facts relating to conflicts of interest that are associated with the recommendation.

(ii) Care obligation. The broker, dealer, or natural person who is an associated person of a broker or dealer, in making the recommendation, exercises reasonable diligence, care, and skill to:

(A) Understand the potential risks, rewards, and costs associated with the recommendation, and have a reasonable basis to believe that the recommendation could be in the best interest of at least some retail customers;

(B) Have a reasonable basis to believe that the recommendation is in the best interest of a particular retail customer based on that retail customer's investment profile and the potential risks, rewards, and costs associated with the recommendation and does not place the financial or other interest of the broker, dealer, or such natural person ahead of the interest of the retail customer;

(C) Have a reasonable basis to believe that a series of recommended transactions, even if in the retail customer's best interest when viewed in isolation, is not excessive and is in the retail customer's best interest when taken together in light of the retail customer's

investment profile and does not place the financial or other interest of the broker, dealer, or such natural person making the series of recommendations ahead of the interest of the retail customer.

(iii) Conflict of interest obligation. The broker or dealer establishes, maintains, and enforces written policies and procedures reasonably designed to:

(A) Identify and at a minimum disclose, in accordance with paragraph (a)(2)(i) of this section, or eliminate, all conflicts of interest associated with such recommendations;

(B) Identify and mitigate any conflicts of interest associated with such recommendations that create an incentive for a natural person who is an associated person of a broker or dealer to place the interest of the broker, dealer, or such natural person ahead of the interest of the retail customer;

(C)(1) Identify and disclose any material limitations placed on the securities or investment strategies involving securities that may be recommended to a retail

customer and any conflicts of interest associated with such limitations, in accordance with subparagraph (a)(2)(i), and

(2) Prevent such limitations and associated conflicts of interest from causing the broker, dealer, or a natural person who is an associated person of the broker or dealer to make recommendations that place the interest of the broker, dealer, or such natural person ahead of the interest of the retail customer; and

(D) Identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific securities or specific types of securities within a limited period of time.

(iv) Compliance obligation. In addition to the policies and procedures required by paragraph (a)(2)(iii) of this section, the broker or dealer establishes, maintains, and enforces written policies and procedures reasonably designed to achieve compliance with Regulation Best Interest.

(b) Definitions. Unless otherwise provided, all terms used in this rule shall have the same meaning as in the Securities Exchange Act of 1934. In addition, the following definitions shall apply for purposes of this section:

(1) **Retail customer** means a natural person, or the legal representative of such natural person, who:

(i) Receives a recommendation of any securities transaction or investment strategy involving securities from a broker, dealer, or a natural person who is an associated person of a broker or dealer; and

(ii) Uses the recommendation primarily for personal, family, or household purposes.

(2) **Retail customer investment profile** includes, but is not limited to, the retail customer's age, other investments, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, risk tolerance, and any other information the retail customer may disclose to the broker, dealer, or a natural person who is an associated person of a broker or dealer in connection with a recommendation.

(3) **Conflict of interest** means an interest that might incline a broker, dealer, or a natural person who is an associated person of a broker or dealer —consciously or unconsciously—to make a recommendation that is not disinterested.

[84 FR 33491, July 12, 2019]

Other definitions

For the purposes of this regulation:

- A. **“Buyer’s Guide”** means the National Association of Insurance Commissioner’s approved Annuity Buyer’s Guide.
- B. **“Charitable gift annuity”** means a transfer of cash or other property by a donor to a charitable organization in return for an annuity payable over one or two lives, under which the actuarial value of the annuity is less than the value of the cash or other property transferred and the difference in value constitutes a charitable deduction for federal tax purposes, but does not include a charitable remainder trust or a charitable lead trust or other similar arrangement where the charitable organization does not issue an annuity and incur a financial obligation to guarantee annuity payments.]
- C. **“Contract owner”** means the owner named in the annuity contract or certificate holder in the case of a group annuity contract.
- D. **“Determinable elements”** means elements that are derived from processes or methods that are guaranteed at issue and not subject to company discretion, but where the values or amounts cannot be determined until some point after issue. These elements include the premiums, credited interest rates (including any bonus), benefits, values, non-interest based credits, charges or elements of formulas used to determine any of these. These elements may be described as guaranteed but not determined at issue. An element is considered determinable if it was calculated from underlying determinable elements only, or from both determinable and guaranteed elements.
- E. **“Funding agreement”** means an agreement for an insurer to accept and accumulate funds and to make one or more payments at future dates in amounts that are not based on mortality or morbidity contingencies.] NAIC Model Laws, Regulations, Guidelines and Other Resources—2nd Quarter 2015 © 2015 National Association of Insurance Commissioners 245-3
- F. **“Generic name”** means a short title descriptive of the annuity contract being applied for or illustrated such as “single premium deferred annuity.”
- G. **“Guaranteed elements”** means the premiums, credited interest rates (including any bonus), benefits, values, non-interest based credits, charges or elements of formulas used to determine any of these, that are guaranteed or have determinable elements at issue. An element is considered guaranteed if all of the underlying elements that go into its calculation are guaranteed.
- H. **“Illustration”** means a personalized presentation or depiction prepared for and provided to an individual consumer that includes non-guaranteed elements of an annuity contract over a period of years.
- I. **“Market Value Adjustment”** or “MVA” feature is a positive or negative adjustment that may be applied to the account value and/or cash value of the annuity upon withdrawal, surrender,

contract annuitization or death benefit payment based on either the movement of an external index or on the company's current guaranteed interest rate being offered on new premiums or new rates for renewal periods, if that withdrawal, surrender, contract annuitization or death benefit payment occurs at a time other than on a specified guaranteed benefit date.

J. "Non-guaranteed elements" means the premiums, credited interest rates (including any bonus), benefits, values, dividends, non-interest based credits, charges or elements of formulas used to determine any of these, that are subject to company discretion and are not guaranteed at issue. An element is considered non-guaranteed if any of the underlying non-guaranteed elements are used in its calculation.

K. "Registered product" means an annuity contract or life insurance policy subject to the prospectus delivery requirements of the Securities Act of 1933.

Drafting Note: Registered products include, but are not limited to, contingent deferred annuities.

L. "Structured settlement annuity" means a "qualified funding asset" as defined in section 130(d) of the Internal Revenue Code or an annuity that would be a qualified funding asset under section 130(d) but for the fact that it is not owned by an assignee under a qualified assignment.

B. Best Interest Standard of Conduct

The purpose of this regulation is to protect the consumer by having minimum standards regarding disclosures and ensuring some education regarding the products they are purchasing. The goal is to help the consumer understand what they have and what the costs associated with it are. Not all annuities are covered by this regulation.

This regulation is for retail sales, all group and individual annuity contracts and certificates **except:**

- Annuities with no non-guaranteed elements
- Annuities used to fund
 - An employee pension plan (covered by ERISA)
 - Employer-sponsored plans; 401k, 401a, 403b
 - Governmental plan or church plans sec 414
 - Deferred compensation plans defined under sec 457 of the IRC for state or local governments
 - Non-qualified deferred compensation plans established or maintained by an employer or plan sponsor

- Non-registered variable annuities issued exclusively to an accredited investor or qualified purchaser as those terms are defined by the Securities Act of 1933
 - Variable annuities and other registered products must use a buyer’s guide as required but the disclosures and illustration requirements are met by the requirements from the SEC and FINRA
- The commissioner may require additional disclosures.
- Structured annuity settlements
- Charitable gift annuities
- Funding agreements

<https://www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12164.pdf>

33318 Federal Register / Vol. 84, No. 134 / Friday, July 12, 2019 / Rules and Regulations
SECURITIES AND EXCHANGE COMMISSION 17 CFR Part 240 [Release No. 34–86031; File No. S7–07–18] RIN 3235–AM35 Regulation Best Interest: The Broker-Dealer Standard of Conduct
AGENCY: Securities and Exchange Commission. ACTION: Final rule.

SUMMARY: The Securities and Exchange Commission (the “Commission”) is adopting a new rule under the Securities Exchange Act of 1934 (“Exchange Act”), establishing a standard of conduct for broker-dealers and natural persons who are associated persons of a broker-dealer (unless otherwise indicated, together referred to as “broker-dealer”) when they make a recommendation to a retail customer of any securities transaction or investment strategy involving securities (“Regulation Best Interest”). Regulation Best Interest enhances the broker-dealer standard of conduct beyond existing suitability obligations, and aligns the standard of conduct with retail customers’ reasonable expectations by requiring broker-dealers, among other things, to: Act in the best interest of the retail customer at the time the recommendation is made, without placing the financial or other interest of the broker-dealer ahead of the interests of the retail customer; and address conflicts of interest by establishing, maintaining, and enforcing policies and procedures reasonably designed to identify and fully and fairly disclose material facts about conflicts of interest, and in instances where we have determined that disclosure is insufficient to reasonably address the conflict, to mitigate or, in certain instances, eliminate the conflict. The standard of conduct established by Regulation Best Interest cannot be satisfied through disclosure alone. The standard of conduct draws from key principles underlying fiduciary obligations, including those that apply to investment advisers under the Investment Advisers Act of 1940 (“Advisers Act”). Importantly, regardless of whether a retail investor chooses a broker-dealer or an investment adviser (or both), the retail investor will be entitled to a recommendation (from a broker-dealer) or advice (from an investment adviser) that is in the best interest of the retail investor and that does not place the interests of the firm or the financial professional ahead of the interests of the retail investor.

1. Recommendations that fall under the best interest standard of conduct.

Best Interest regulation applies to recommendations to natural persons who Use the recommendation primarily for personal, family, or household purposes.

Reg BI only applies to recommendations to “retail customers.” Reg BI defines a “retail customer” as a natural person, or the legal representative of such person, who:

- (a) receives a recommendation of any securities transaction or investment strategy involving securities from a BD or AP; and
- (b) uses the recommendation primarily for personal, family or household purposes.

“Uses” means when, as a result of the recommendation:

- the retail customer opens a brokerage account with the BD, regardless of whether the BD receives compensation;
- the retail customer has an existing account with the BD and receives a recommendation from the BD, regardless of whether the BD receives or will receive compensation, directly or indirectly, as a result of the recommendation; or
- the BD receives or will receive compensation, directly or indirectly, as a result of that recommendation, even if that retail customer does not have an account at the firm.

The phrase “primarily for personal, family, or household purposes” covers any recommendation to a natural person for his or her account, other than recommendations to a natural person seeking these services for commercial or business purposes.

The standards are for all types of investment recommendations, from a standard savings in an annuity to an IRA. Different investment products have many fees and expenses, penalties for early withdrawals, penalties for late withdrawals (an IRA may have a required minimum distribution). These are a few of the items to be considered and explained.

C. Care Obligation

https://www.sec.gov/info/smallbus/secg/regulation-best-interest#Care_Obligation

Under the Care Obligation, you must exercise **reasonable diligence, care, and skill** when making a recommendation to a retail customer to:

- understand potential risks, rewards, and costs associated with recommendation, and have a reasonable basis to believe that the recommendation could be in the best interest of at least some retail customers;
- have a reasonable basis to believe the recommendation is in the best interest of a particular retail customer based on that retail customer’s investment profile and the potential risks, rewards, and costs associated with the recommendation and does not

place the interest of the broker-dealer ahead of the interest of the retail customer;
and

- have a reasonable basis to believe that a series of recommended transactions, even if in the retail customer's best interest when viewed in isolation, is not excessive and is in the retail customer's best interest when taken together in light of the retail customer's investment profile.

Whether you have complied with the Care Obligation will be evaluated as of the time of the recommendation (and not in hindsight).

What does the first component of the Care Obligation require?

You must exercise reasonable diligence, care, and skill to understand the potential risks, rewards, and costs associated with the recommendation.

What would constitute reasonable diligence, care, and skill will vary depending on, among other things, the complexity of and risks associated with the recommended security or investment strategy and the broker-dealer's familiarity with the recommended security or investment strategy.

While every inquiry will be specific to the particular broker-dealer and the recommended security or investment strategy, you generally should consider **important factors** such as:

- the security's or investment strategy's:
 - investment objectives;
 - characteristics (including any special or unusual features);
 - liquidity;
 - volatility; and
 - likely performance in a variety of market and economic conditions;
- the expected return of the security or investment strategy; and
- any financial incentives to recommend the security or investment strategy.

Together, this inquiry should allow you to develop a sufficient understanding of the security or investment strategy and to be able to reasonably believe that it could be in the best interest of at least some retail customers.

What does the second component of the Care Obligation require?

You must consider the risks, rewards, and costs in light of the retail customer's investment profile and have a reasonable basis to believe that the recommendation is in that particular customer's best interest and does not place the broker-dealer's interest ahead of the customer's interest.

The **retail customer's investment profile** is defined to include, but is not limited to the retail customer's:

- age;
- other investments;
- investment time horizon;
- liquidity needs;

- financial situation and needs;
- tax status;
- investment objectives;
- investment experience;
- risk tolerance; and
- any other information the retail customer may disclose to the broker in connection with a recommendation

What does the third component of the Care Obligation require?

When recommending a series of transactions, you must have a reasonable basis to believe that the transactions taken together are not excessive, even if each is in your customer's best interest when viewed in isolation. The requirement applies irrespective of whether you exercise actual or *de facto* control over a customer's account.

What would constitute a "series" of recommended transactions would depend on the facts and circumstances, and would need to be evaluated with respect to a particular retail customer.

D. Disclosure Obligation

In financial planning, disclosure is critical to both parties. The insurance company providing the annuity does not want to take advantage of clients and must relate both the risks and fees up front as well as the benefits so the client knows what they are buying. The client needs to understand annuities are fantastic products, but not necessarily for everyone. There are fees involved in the product, early withdrawal penalties, as well as the fact that if a person has chosen a life option they cannot surrender the contract.

1. Insurance Producer Disclosure for Annuities form

The Disclosure Obligation requires a form is signed by the client - prior to the sale - with basic information about the producer, insurer, types of products they can sell, and if the client asks, the commissions and non cash compensation earned on this sale. See appendix A

E. Conflict of Interest Obligation

<https://content.naic.org/sites/default/files/inline-files/MDL-275.pdf>

Conflict of interest obligation. A producer shall identify and avoid or reasonably manage and disclose material conflicts of interest, including material conflicts of interest related to an ownership interest.

https://www.sec.gov/info/smallbus/secg/regulation-best-interest#Care_Obligation

The Conflict of Interest Obligation (and the Compliance Obligation discussed below), applies solely to the broker-dealer entity, and not to the associated persons of a broker-dealer. For purposes of discussing the Conflict of Interest Obligation, the term “broker-dealer” or “you” refers only to the broker-dealer entity, and not to such individuals.

Under the Conflict of Interest Obligation, a broker-dealer must establish, maintain, and enforce written policies and procedures reasonably designed to address conflicts of interest associated with its recommendations to retail customers.

Specifically, the **written policies and procedures** must be reasonably designed to:

Identify and at a minimum disclose, pursuant to the Disclosure Obligation, or eliminate all conflicts of interest associated with such recommendations;

Identify and mitigate any conflicts of interest associated with such recommendations that create an incentive for the broker-dealer’s associated persons to place their interest or the interest of the broker-dealer ahead of the retail customer’s interest;

Identify and disclose any material limitations, such as **a limited product menu** or **offering only proprietary products**, placed on the securities or investment strategies involving securities that may be recommended to a retail customer and any conflicts of interest associated with such limitations, and prevent such limitations and associated conflicts of interest from causing the broker-dealer or the associated person to place the interest of the broker-dealer or the associated person ahead of the retail customer’s interest; and

Identify and eliminate sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sale of specific securities or specific types of securities within a limited period of time.

How should you develop policies and procedures to mitigate certain incentives to associated persons?

Your policies and procedures must be reasonably designed to reduce the potential effect such conflicts may have on a recommendation given to a retail customer.

You have flexibility to develop and tailor reasonably designed policies and procedures that include conflict mitigation measures, based on your circumstances, such as your size, retail customer base (for example, the diversity of investment experience and financial needs), and the complexity of the security or investment strategy involving securities that is being recommended, some of which may be weighed more heavily than others.

Policies and procedures may be reasonably designed at the outset, but may later cease to be reasonably designed based on subsequent events or information obtained, for example, through supervision (e.g., exception testing) of associated person recommendations. Your actual experience should be used to revise your measures as appropriate.

1. Cash and non-cash compensation

Non-Cash Compensation Rules

<https://www.finra.org/rules-guidance/key-topics/gifts-gratuities-and-non-cash-compensation>

[FINRA Rules 2310 \(Direct Participation Programs\)](#), [2320 \(Variable Contracts of an Insurance Company\)](#), [2341 \(Investment Company Securities\)](#), [5110 \(Corporate Financing Rule – Underwriting Terms and Arrangements\)](#) (together, the Non-Cash Compensation Rules) impose restrictions on non-cash arrangements that are in connection with the sale and distribution of securities covered by those rules. The Non-Cash Compensation Rules prohibit a member firm or associated person from directly or indirectly accepting or making payments of any non-cash compensation, subject to specified exceptions.

The exceptions permit:

gifts that do not exceed an annual amount per person fixed by the FINRA Board of Governors (currently \$100) and are not preconditioned on achievement of a sales target;

an occasional meal, a ticket to a sporting event or the theater or comparable entertainment which is neither so frequent nor so extensive as to raise any question of propriety and is not preconditioned on achievement of a sales target;

payment or reimbursement by “offerors” (product issuers, advisers, underwriters and their affiliates) in connection with training or education meetings, subject to certain conditions, including meeting location restrictions and not preconditioning attendance on achievement of a sales target; and

internal firm non-cash compensation arrangements that are based on total production and equal weighting of product sales. (Rules 2310 and 5110 do not impose total production and equal weighting requirements on internal non-cash compensation arrangements.)

Effective June 30, 2020, [SEC Regulation Best Interest \(Reg BI\)](#) establishes a standard of conduct for broker-dealers and associated persons when they make a recommendation to a retail customer of any securities transaction or investment strategy involving securities. Reg BI

requires broker-dealers to act in the best interest of the retail customer at the time the recommendation is made, without placing the financial interest of the broker-dealer ahead of the interests of the retail customer.

Reg BI requires broker-dealers to establish, maintain and enforce written policies and procedures reasonably designed to identify and at a minimum disclose, or eliminate, all conflicts associated with such recommendations. Among other things, broker-dealers must identify and eliminate any sales contests, sales quotas, bonuses and non-cash compensation that are based on the sales of specific securities or specific types of securities within a limited period of time. Accordingly, in addition to Non-Cash Compensation Rules' restrictions, any non-cash compensation arrangement must be consistent with the requirements of Reg BI.

2. Ownership interest

<https://www.federalregister.gov/documents/2019/07/12/2019-12164/regulation-best-interest-the-broker-dealer-standard-of-conduct>

Third, under the Conflict of Interest Obligation,^[19] a broker-dealer must establish, maintain, and enforce reasonably designed written policies and procedures addressing conflicts of interest associated with its recommendations to retail customers. These policies and procedures must be reasonably designed to identify all such conflicts and at a minimum disclose or eliminate them. Importantly, the policies and procedures must be reasonably designed to mitigate conflicts of interests that create an incentive for an associated person of the broker-dealer to place its interests or the interest of the firm ahead of the retail customer's interest. Moreover, when a broker-dealer places material limitations on recommendations that may be made to a retail customer (*e.g.*, offering only proprietary or other limited range of products), the policies and procedures must be reasonably designed to disclose the limitations and associated conflicts and to prevent the limitations from causing the associated person or broker-dealer from placing the associated person's or broker-dealer's interests ahead of the customer's interest. Finally, the policies and procedures must be reasonably designed to identify and eliminate sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sale of specific securities or specific types of securities within a limited period of time.

F. Documentation Obligation

<https://content.naic.org/sites/default/files/inline-files/MDL-275.pdf>

(4) Documentation obligation. A producer shall at the time of recommendation or sale:

(a) Make a written record of any recommendation and the basis for the recommendation subject to this regulation;

(b) Obtain a consumer signed statement on a form substantially similar to Appendix B documenting:

- (i) A customer's refusal to provide the consumer profile information, if any; and
- (ii) A customer's understanding of the ramifications of not providing his or her consumer profile information or providing insufficient consumer profile information; and

(c) Obtain a consumer signed statement on a form substantially similar to Appendix C acknowledging the annuity transaction is not recommended if a customer decides to enter into an annuity transaction that is not based on the producer's recommendation.

(5) Application of the best interest obligation. Any requirement applicable to a producer under this subsection shall apply to every producer who has exercised material control or influence in the making of a recommendation and has received direct compensation as a result of the recommendation or sale, regardless of whether the producer has had any direct contact with the consumer. Activities such as providing or delivering marketing or educational materials, product wholesaling or other back office product support, and general supervision of a producer do not, in and of themselves, constitute material control or influence.

<https://content.naic.org/sites/default/files/inline-files/MDL-275.pdf>

Recordkeeping

A. Insurers, general agents, independent agencies and producers shall maintain or be able to make available to the commissioner records of the information collected from the consumer, disclosures made to the consumer, including summaries of oral disclosures, and other information used in making the recommendations that were the basis for insurance transactions for [insert number] years after the insurance transaction is completed by the insurer. An insurer is permitted, but shall not be required, to maintain documentation on behalf of a producer. Drafting Note: States should review their current record retention laws and specify a time period that is consistent with those laws. For some states this time period may be five (5) years.

B. Records required to be maintained by this regulation may be maintained in paper, photographic, microprocess, magnetic, mechanical or electronic media or by any process that accurately reproduces the actual document. Drafting Note: This section may be unnecessary in states that have a comprehensive recordkeeping law or regulation.

https://www.sec.gov/info/smallbus/secg/regulation-best-interest#Record_making_and_Recordkeeping
Record-making and Recordkeeping

You must meet new record-making and recordkeeping requirements with respect to certain information collected from or provided to retail customers in connection with Regulation Best Interest. This builds upon existing record-making and recordkeeping obligations.

- For each retail customer to whom a recommendation of any securities transaction or investment strategy involving securities is or will be provided, you must keep a record of all information collected from and provided to the retail customer pursuant to Regulation Best Interest, as well as the identity of each natural person who is an associated person, if any, responsible for the account.
- You must retain all records of the information collected from or provided to each retail customer for at least six years after the earlier of the date the account was closed or the date on which the information was replaced or updated.

G. Supervision System

<https://www.sec.gov/tm/faq-regulation-best-interest>

Compliance Obligation

Q: Are firms required to build new systems of controls and compliance in order to satisfy the Compliance Obligation?

A: The Compliance Obligation requires that firms establish, maintain and enforce, written policies and procedures that are reasonably designed to achieve compliance with Regulation Best Interest. The Commission has stated that these policies and procedures should be reasonably designed to address and be proportionate to the scope, size and risks associated with the operations of the firm and types of business in which the firm engages. In adopting the requirement, the Commission did not mandate specific requirements but provided flexibility to allow broker-dealers to establish compliance policies and procedures that accommodate a broad range of business models.

Broker-dealers are currently subject to supervisory obligations under federal securities laws and regulations, as well as applicable self-regulatory organization rules, and broker-dealers could choose to satisfy the Compliance Obligation by adjusting/building upon their current systems of supervision and compliance, as opposed to creating entirely new systems. (Posted February 11, 2020)

<https://content.naic.org/sites/default/files/inline-files/MDL-275.pdf>

C. Supervision system.

(1) Except as permitted under Subsection B (transactions not based on a recommendation), an insurer may not issue an annuity recommended to a consumer unless there is a reasonable basis to believe the annuity would effectively address the particular consumer's financial

situation, insurance needs and financial objectives based on the consumer's consumer profile information.

(2) An insurer shall establish and maintain a supervision system that is reasonably designed to achieve the insurer's and its producers' compliance with this regulation, including, but not limited to, the following:

(a) The insurer shall establish and maintain reasonable procedures to inform its producers of the requirements of this regulation and shall incorporate the requirements of this regulation into relevant producer training manuals;

(b) The insurer shall establish and maintain standards for producer product training and shall establish and maintain reasonable procedures to require its producers to comply with the requirements of Section 7 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 producers; Suitability in Annuity Transactions Model Regulation 275-8 © 2020 National Association of Insurance Commissioners

(d) The insurer shall establish and maintain procedures for the review of each recommendation prior to issuance of an annuity that are designed to ensure there is a reasonable basis to determine that the recommended annuity would effectively address the particular consumer's financial situation, insurance needs and financial objectives. 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 establish and maintain reasonable procedures to detect recommendations that are not in compliance with Subsections A, B, D and E. This may include, but is not limited to, confirmation of the consumer's consumer profile information, systematic customer surveys, producer and consumer interviews, confirmation letters, producer statements or attestations and programs of internal monitoring. Nothing in this subparagraph prevents an insurer from complying with this subparagraph by applying sampling procedures, or by confirming the consumer profile information or other required information under this section after issuance or delivery of the annuity;

(f) The insurer shall establish and maintain reasonable procedures to assess, prior to or upon issuance or delivery of an annuity, whether a producer has provided to the consumer the information required to be provided under this section;

(g) The insurer shall establish and maintain reasonable procedures to identify and address suspicious consumer refusals to provide consumer profile information;

(h) The insurer shall establish and maintain reasonable procedures to identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific annuities within a limited period of time. The requirements of this subparagraph are not intended to prohibit the receipt of health insurance, office rent, office support, retirement benefits or other employee benefits by employees as long as those benefits are not based upon the volume of sales of a specific annuity within a limited period of time; and Drafting Note: The intent of Subparagraph (h) is to prohibit sales contests, sales quotas, bonuses and non-cash compensation based on the sale of a particular product within a limited period of time, but not to prohibit general incentives regarding the sales of a company's products with no emphasis on any particular product.

(i) The insurer shall annually provide a written 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

(3) (a) Nothing in this subsection restricts an insurer from contracting for performance of a function (including maintenance of procedures) required under this subsection. An insurer is responsible for taking appropriate corrective action and may be subject to sanctions and penalties pursuant to Section 8 of this regulation regardless of whether the insurer contracts for performance of a function and regardless of the insurer's compliance with Subparagraph (b) of this paragraph.

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

(i) Monitoring and, as appropriate, conducting audits to assure that the contracted function is properly performed; and NAIC Model Laws, Regulations, Guidelines and Other Resources—Spring 2020 © 2020 National Association of Insurance Commissioners 275-9

(ii) 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.

(4) An insurer is not required to include in its system of supervision:

(a) A producer's recommendations to consumers of products other than the annuities offered by the insurer; or

(b) Consideration of or comparison to options available to the producer or compensation relating to those options other than annuities or other products offered by the insurer.

<https://www.sec.gov/info/smallbus/secg/regulation-best-interest#Introduction>

[1] This guide was prepared by the staff of the U.S. Securities and Exchange Commission as a “small entity compliance guide” under Section 212 of the Small Business Regulatory Enforcement Fairness Act of 1996, as amended. The guide summarizes and explains rules adopted by the SEC, but is not a substitute for any rule itself. Only the rule itself can provide complete and definitive information regarding its requirements.

[2] A dual registrant is an investment adviser solely with respect to those accounts for which a dual registrant provides investment advice or receives compensation that subjects it to the Advisers Act. Although this discussion focuses on the treatment of broker-dealers that are dually registered with the Commission as investment advisers, a broker-dealer should perform the same analysis when it is engaged in other financial services (such as a bank, a commodity trading advisor, or a future commission merchant).

[3] For more information about the “solely incidental” prong, see the Commission Interpretation Regarding the Solely Incidental Prong of the Broker-Dealer Exclusion from the Definition of Investment Adviser.

[4] *Basic, Inc. v. Levinson*, 485 U.S. 224 (1988).