AMENDED IN SENATE APRIL 4, 2011

SENATE BILL No. 715

Introduced by ~~Committee on Insurance (Senators Calderon (Chair), Anderson, Corbett, Correa, Gaines, Lowenthal, Price, and Wyland)~~ *Senator Calderon*
(Coauthors: Senators Anderson, Correa, Gaines, and Wyland)

February 18, 2011

An act to add Article 9 (commencing with Section 10509.910) to Chapter 5 of Part 2 of Division 2 of the Insurance Code, relating to annuity transactions.

LEGISLATIVE COUNSEL'S DIGEST

SB 715, as amended, ~~Committee on Insurance~~ *Calderon*. Annuity transactions.

Existing law requires agents and insurers to fulfill certain requirements with regard to the replacement of existing life insurance policies and annuities.

This bill would require insurers and insurance producers, as defined, to comply with specified requirements regarding the purchase, exchange, or replacement of an annuity recommended to a consumer, including, but not limited to, having reasonable grounds for the insurance producer believing the annuity transaction would be suitable for the consumer, as provided. The bill would also prohibit an insurance producer from selling annuities unless he or she has received Insurance Commissioner-approved training, and would authorize the commissioner to require certain actions by, and impose sanctions and penalties on, insurers and their agents for a violation of the *bill's* provisions ~~of the act~~.

Vote: majority. Appropriation: no. Fiscal committee: yes. State-mandated local program: no.

The people of the State of California do enact as follows:

SECTION 1. Article 9 (commencing with Section 10509.910) is added to Chapter 5 of Part 2 of Division 2 of the Insurance Code, to read:

Article 9. Suitability Requirements for Annuity Transactions

10509.910. The Legislature finds and declares all of the following:

(a) The Legislature finds and declares that in 2010 the National Association of Insurance Commissioners (NAIC) adopted a significantly revised Suitability in Annuity Transactions Model Regulation.

(b) The Legislature also finds that the revised Suitability in Annuity Transactions Model was adopted by the NAIC to set standards and procedures for suitable annuity recommendations and to require insurers to establish a system to supervise recommendations so that the insurance needs and financial objectives of consumers are appropriately addressed.

(c) The Legislature finds that the revised NAIC Suitability in Annuity Transactions Model establishes a regulatory framework that holds insurers responsible for ensuring that annuity transactions are suitable, whether or not the insurer contracts with a third party to supervise or monitor the recommendations made in the marketing and sale of annuities.

(d) The Legislature also finds that the 2010 revisions to the NAIC Suitability in Annuity Transactions Model require that producers be trained on the provisions of annuities in general, and the specific products they are selling.

(e) The Legislature finds that the adoption last year of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Public Law 111-203) provides, under Title IX, Subtitle I, Section 989A, relating to senior investment protections, that a state's adherence to the NAIC's Suitability in Annuity Transactions Model is required for a state or other eligible entities to participate in a

program of grants to support enhanced protections of seniors against misleading marketing practices.

(f) Finally, the Legislature finds that adoption in this state of the NAIC Suitability in Annuity Transactions Model affects California's continued jurisdiction over indexed securities under Title IX, Subtitle I, Section 989J of the Dodd-Frank Act.

~~10509.910. (a)~~

10509.911. The purpose of this article is to require insurers to establish a system to supervise recommendations and to set forth standards and procedures for recommendations to consumers that result in transactions involving annuity products so that the insurance needs and financial objectives of consumers at the time of the transaction are appropriately addressed.

~~(b) Nothing in this article shall be construed to create or imply a private cause of action for a violation of this article.~~

~~10509.911. Notwithstanding any other provision of law, this~~

10509.912. This article shall apply to any recommendation to purchase, exchange, or replace an annuity made to a consumer by an insurance producer, or an insurer where no insurance producer is involved, that results in the purchase, exchange, or replacement recommended.

~~10509.912.~~

10509.913. Unless otherwise specifically included, this article shall not apply to transactions involving any of the following:

(a) Direct response solicitations where there is no recommendation based on information collected from the consumer pursuant to this article.

(b) Contracts used to fund any of the following:

(1) An employee pension or welfare benefit plan that is covered by the Employee Retirement and Income Security Act (ERISA) (29 U.S.C. Sec. 1001 et seq.).

(2) A plan described by Section 401(a), 401(k), 403(b), 408(k), or 408(p) of the Internal Revenue Code, if established or maintained by an employer.

(3) A government or church plan defined in Section 414 of the Internal Revenue Code, a government or church welfare benefit plan, or a deferred compensation plan of a state or local government or tax exempt organization under Section 457 of the Internal Revenue Code.

(4) A nonqualified deferred compensation arrangement established or maintained by an employer or plan sponsor.

(5) Settlements of or assumptions of liabilities associated with personal injury litigation or any dispute or claim resolution process.

(6) Formal prepaid funeral contracts.

~~10509.913.~~

10509.914. For the purposes of this article, the following terms have the following definitions:

(a) “Annuity” means an annuity that is an insurance product under state law that is individually solicited, whether the product is classified as an individual or group annuity.

~~(b) “Continuing education credits” or “CE credits” means continuing education credit from a continuing education course approved by the commissioner.~~

~~(c) “Continuing education provider” or “CE provider” means an individual or entity that is approved by the commissioner to offer continuing education courses.~~

(b) “Commissioner” means the Insurance Commissioner.

(c) “Continuing education credit” or “CE credit” means one continuing education credit hour as defined in Section 2188.2(i) of Title 10 of the California Code of Regulations.

(d) “Continuing education provider” or “CE provider” means an individual or entity that is certified to offer continuing education courses pursuant to Section 2186.1(b) and Section 2188 of Title 10 of the California Code of Regulations.

~~(d)~~

(e) “FINRA” means the Financial Industry Regulatory Authority or a succeeding agency.

~~(e)~~

(f) “Insurance producer” means a person required to be licensed under the laws of this state to sell, solicit, or negotiate insurance, including annuities.

~~(f) “Insurer” means a company required to be licensed under the laws of this state to provide insurance products, including annuities.~~

(g) “Insurer” means a company required to be licensed or to hold a certificate of authority, or both, under California law to provide insurance products, including annuities.

~~(g)~~

(h) “Recommendation” means advice provided by an insurance producer, or an insurer where no insurance producer is involved, to an individual consumer that results in a purchase, exchange, or replacement of an annuity in accordance with that advice.

~~(h)~~

(i) “Replacement” has the same definition as in Section 10509.2.

~~(i)~~

(j) “Suitability information” means information that is reasonably appropriate to determine the suitability of a recommendation, including all of the following:

(1) Age.

(2) Annual income.

(3) Financial situation and needs, including the financial resources used for the funding of the annuity.

(4) Financial experience.

(5) Financial objectives.

(6) Intended use of the annuity.

(7) Financial time horizon.

(8) Existing assets, including investment and life insurance holdings.

(9) Liquidity needs.

(10) Liquid net worth.

(11) Risk tolerance.

(12) Tax status.

~~10509.914.~~

10509.915. (a) In recommending to a consumer the purchase of an annuity or the exchange of an annuity that results in another insurance transaction or series of insurance transactions, the insurance producer, or the insurer where no insurance producer is involved, shall have reasonable grounds for believing that the recommendation is suitable for the consumer on the basis of the facts disclosed by the consumer as to his or her investments and other insurance products and as to his or her financial situation and needs, including the consumer’s suitability information, and that there is a reasonable basis to believe all of the following:

(1) The consumer has been reasonably informed of various features of the annuity, such as the potential surrender period and surrender charge, potential tax penalty if the consumer sells, exchanges, surrenders, or annuitizes the annuity, mortality and expense fees, investment advisory fees, potential charges for and

features of riders, limitations on interest returns, insurance and investment components, and market risk.

(2) The consumer would benefit from certain features of the annuity, such as tax-deferred growth, annuitization, or death or living benefit.

(3) The particular annuity as a whole, the underlying subaccounts to which funds are allocated at the time of purchase or exchange of the annuity, and riders and similar product enhancements, if any, are suitable, and in the case of an exchange or replacement, the transaction as a whole is suitable, for the particular consumer, based on his or her suitability information.

(4) In the case of an exchange or replacement of an annuity, the exchange or replacement is suitable, including taking into consideration whether any of the following are applicable:

(A) The consumer will incur a surrender charge, be subject to the commencement of a new surrender period, lose existing benefits, such as death, living, or other contractual benefits, or be subject to increased fees, investment advisory fees, or charges for riders and similar product enhancements.

(B) The consumer would benefit from product enhancements and improvements.

(C) The consumer has had another annuity exchange or replacement and, in particular, an exchange or replacement within the preceding 36 months.

(D) The exchange or replacement of that annuity would not be an "unnecessary replacement" as that term is used in subdivision (b) of Section 10509.8.

(b) Prior to the execution of a purchase, exchange, or replacement of an annuity resulting from a recommendation, an insurance producer, or an insurer where no insurance producer is involved, shall make reasonable efforts to obtain the consumer's suitability information.

(c) Except as permitted pursuant to subdivision (d), an insurer shall not issue an annuity recommended to a consumer unless there is a reasonable basis to believe the annuity is suitable based on the consumer's suitability information *and applicable California law*.

(d) (1) Except as provided pursuant of paragraph (2), neither an insurance producer, nor an insurer, shall have any obligation to a consumer pursuant to subdivision (a) or (c) related to any annuity transaction if any of the following occur:

(A) No recommendation is made.

(B) A recommendation was made and was later found to have been prepared based on ~~inaccurate material~~ *materially inaccurate* information provided by the consumer.

(C) A consumer refuses to provide relevant suitability information and the annuity transaction is not recommended.

(D) A consumer decides to enter into an annuity transaction that is not based on a recommendation of the insurer or the insurance producer.

(2) An insurer's issuance of an annuity subject to paragraph (1) shall be reasonable under all the circumstances actually known to the insurer at the time the annuity is issued.

(e) An insurance producer or, where no insurance producer is involved, the responsible insurer representative, shall at the time of sale do all of the following:

(1) Make a record of any recommendation subject to subdivision (a) of this section.

(2) Obtain a customer signed statement documenting a customer's refusal to provide suitability information, if any.

(3) Obtain a customer signed statement acknowledging that an annuity transaction is not recommended if a customer decides to enter into an annuity transaction that is not based on the insurance producer's or insurer's recommendation.

(f) (1) An insurer shall establish a supervision system that is reasonably designed to achieve the insurer's and its insurance producers' compliance with this article, including, but not limited to, all of the following:

(A) The insurer shall maintain reasonable procedures to inform its insurance producers of the requirements of this article and shall incorporate the requirements of this article into relevant insurance producer training manuals.

(B) The insurer shall establish standards for insurance producer product training and shall maintain reasonable procedures to require its insurance producers to comply with the requirements of Section ~~10509.915~~ *10509.916*.

(C) The insurer shall provide product-specific training and training materials that explain all material features of its annuity products to its insurance producers.

(D) The insurer shall maintain procedures for review of each recommendation, prior to issuance of an annuity, that are designed to ensure that there is a reasonable basis to determine that a recommendation is suitable. The 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. 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 maintain reasonable procedures to detect recommendations that are not suitable. This may include, but is not limited to, confirmation of consumer suitability information, systematic customer surveys, interviews, confirmation letters, and programs of internal monitoring. Nothing in this subparagraph prevents an insurer from complying with this subparagraph by applying sampling procedures, or by confirming suitability information after issuance or delivery of the annuity.

(F) The insurer shall annually provide a 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.

(2) (A) Nothing in this subdivision restricts an insurer from contracting for performance of a function, including maintenance of procedures, required under paragraph (1). An insurer is responsible for taking appropriate corrective action and may be subject to sanctions and penalties pursuant to Section ~~10509.916~~ *10509.917* regardless of whether the insurer contracts for performance of a function and regardless of the insurer's compliance with subparagraph (B).

(B) An insurer's supervision system under paragraph (1) shall include supervision of contractual performance under this subdivision. This includes, but is not limited to, both of the following:

(i) Monitoring and, as appropriate, conducting audits to assure that the contracted function is properly performed.

(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.

(3) An insurer is not required to include in its system of supervision an insurance producer's recommendations to consumers of products other than the annuities offered by the insurer.

(g) An insurance producer shall not dissuade, or attempt to dissuade, a consumer from any of the following:

(1) Truthfully responding to an insurer's request for confirmation of suitability information.

(2) Filing a complaint.

(3) Cooperating with the investigation of a complaint.

(h) (1) Sales made in compliance with FINRA requirements pertaining to suitability and supervision of annuity transactions shall satisfy the requirements under this article. This subdivision applies to FINRA broker-dealer sales of variable annuities and fixed annuities if the suitability and supervision is similar to those applied to variable annuity sales. However, nothing in this subdivision shall limit the commissioner's ability to enforce, including conducting investigations related to, the provisions of this article.

(2) For paragraph (1) to apply, an insurer shall do both of the following:

(A) Monitor the FINRA member broker-dealer using information collected in the normal course of an insurer's business.

(B) Provide to the FINRA member broker-dealer information and reports that are reasonably appropriate to assist the FINRA member broker-dealer to maintain its supervision system.

~~10509.915.~~

10509.916. (a) An insurance producer shall not solicit the sale of an annuity product unless the insurance producer has adequate knowledge of the product to recommend the annuity, and the insurance producer is in compliance with the insurer's standards for product training. An insurance producer may rely on insurer-provided product-specific training standards and materials to comply with this subdivision.

~~(b) (1) (A) An insurance producer who engages in the sale of annuity products shall complete a one-time four credit-hour training course approved by the commissioner and provided by a commissioner-approved education provider.~~

(b) (1) (A) An insurance producer who is otherwise entitled to engage in the sale of annuity products shall complete a one-time

eight-credit-hour annuity training course approved by the commissioner and provided by a commissioner-approved education provider, prior to commencing the transaction of annuities, pursuant to subdivision (a) of Section 1749.8.

(B) In addition to the requirement set forth in subparagraph (1), every producer who engages in this state in the sale of annuity products shall satisfactorily complete four continuing education credits prior to license renewal every two years, pursuant to subdivision (b) of Section 1749.8.

~~(B)~~

(C) Insurance producers who hold a life insurance line of authority on the effective date of this article and who desire to sell annuities shall complete the requirements of this subdivision within six months after the effective date of this article. Individuals who obtain a life insurance line of authority on or after the effective date of this article may not engage in the sale of annuities until the annuity training course required under this subdivision has been completed.

~~(2) The minimum length of the training required under this subdivision shall be sufficient to qualify for at least four CE credit-hours, but may be longer.~~

~~(3)~~

(2) The training required under this subdivision shall include information on all of the following topics:

(A) The types of annuities and various classifications of annuities.

(B) Identification of the parties to an annuity.

(C) How fixed, variable, and indexed annuity contract provisions affect consumers.

(D) The application of income taxation of qualified and nonqualified annuities.

(E) The primary uses of annuities.

(F) Appropriate sales practices, replacement, and disclosure requirements.

(G) Other topics required for training in selling annuities under subdivision (c) of Section 1749.8.

~~(4)~~

(3) Providers of courses intended to comply with this subdivision shall cover all topics listed in the prescribed outline and shall not present any marketing information or provide training on sales

techniques or provide specific information about a particular insurer's products. Additional topics may be offered in conjunction with and in addition to the required outline.

~~(5) A provider of an annuity training course intended to comply with this subdivision shall register as a CE provider in this state and comply with the rules and guidelines applicable to insurance producer continuing education courses as set forth in _____.~~

~~(6) Annuity training courses may be conducted and completed by classroom or self-study methods in accordance with _____.~~

~~(7) Providers of annuity training shall comply with the reporting requirements and shall issue certificates of completion in accordance with ____.~~

(4) A provider of an annuity training course intended to comply with this section shall register as a CE provider in this state and comply with the rules and guidelines applicable to insurance producer continuing education courses as set forth in Section 1749.8, in subdivisions (d) and (e) of Section 1749.1, and in Sections 2188, 2188.1, 2188.2, 2188.3, 2188.4, 2188.6, 2188.7, 2188.8, 2188.50 and 2188.9 of Title 10 of the California Code of Regulations.

(5) Annuity training courses may be conducted and completed by classroom or self-study methods in accordance with Sections 2188.2 and 2188.3 of Title 10 of the California Code of Regulations.

(6) Providers of annuity training shall comply with the reporting requirements and shall issue certificates of completion in accordance with Section 2188.8 of Title 10 of the California Code of Regulations.

~~(8)~~

(7) The satisfaction of the training requirements of another state that are substantially similar to the provisions of this subdivision shall be deemed to satisfy the training requirements of this subdivision in this state.

~~(9)~~

(8) An insurer shall verify that an insurance producer has completed the annuity training course required under this subdivision before allowing the insurance producer to sell an annuity product for that insurer. An insurer may satisfy its responsibility under this subdivision by obtaining certificates of completion of the training course or obtaining reports provided by

commissioner-sponsored database systems or vendors or from a reasonably reliable commercial database vendor that has a reporting arrangement with approved insurance education providers.

~~10509.916.~~

10509.917. (a) An insurer is responsible for compliance with this article. If a violation occurs, either because of the action or inaction of the insurer or its insurance producer, the commissioner may order any of the following:

(1) An insurer to take reasonably appropriate corrective action for any consumer harmed by the insurer's, or by its insurance producer's, violation of this article.

(2) A general insurance agency, independent agency, or the insurance producer to take reasonably appropriate corrective action for any consumer harmed by the insurance producer's violation of this article.

(3) Penalties and sanctions pursuant to Section 10509.9.

(b) Any applicable penalty under Section 10509.9 for a violation of this article may be reduced or eliminated if corrective action for the consumer was taken promptly after a violation was discovered or the violation was not part of a pattern or practice.

~~10509.917.~~

10509.918. (a) Insurers, general agents, independent insurance agencies, and insurance producers shall maintain or be able to make available to the commissioner records of the information collected from the consumer and other information used in making the recommendations that were the basis for insurance transactions for five 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 an insurance producer.

(b) Records required to be maintained by this article may be maintained in paper, photographic, microprocessing, magnetic, mechanical, or electronic media or by any process that accurately reproduces the actual document.

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