
Financial Institutions & Insurance Committee

ESSB 5671

Brief Description: Determining the suitability of annuities sold in Washington.

Sponsors: Senate Committee on Financial Institutions, Housing & Insurance (originally sponsored by Senators Berkey, Franklin, Shin and Haugen; by request of Insurance Commissioner).

<p style="text-align: center;">Brief Summary of Engrossed Substitute Bill</p> <ul style="list-style-type: none">• Requires insurers and insurance producers to meet suitability standards when recommending the purchase or exchange of an annuity to a consumer.• Grants the Insurance Commissioner rule-making authority.

Hearing Date: 3/10/09

Staff: Jon Hedegard (786-7127)

Background:

The Insurance Commissioner (Commissioner) and the federal and state security regulators all have a role in regulating the sale of annuities in this state.

The Commissioner oversees insurers and insurance producers and the market practices of those persons and entities in this state. This includes the sale of fixed and variable annuities.

The Federal Securities Act of 1933 addresses securities regulation which includes annuities that are classified as securities. The Securities and Exchange Commission (SEC) oversees the Securities Act of 1933 and currently requires registration of variable and indexed (but not fixed) annuities as securities. The Department of Financial Institutions (DFI) also oversees the sale of securities in this state. A security is defined to include annuities but specifically excludes "any insurance or endowment policy or annuity contract under which an insurance company promises

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

to pay a fixed sum of money either in a lump sum or periodically for life or some other specified period."

The DFI has a number of requirements for broker-dealers, salespersons, investment advisers, and investment adviser representatives (licensees). One legal requirement is the suitability of a security recommendation made by a licensee. Prior to making a transaction, a licensee must make reasonable efforts to obtain information concerning:

- the customer's financial status;
- the customer's tax status;
- the customer's investment objectives; and
- other information used or considered to be reasonable in making recommendations to the customer.

The licensee must have reasonable grounds for believing that the recommendation is suitable for the customer upon the basis of the facts, if any, disclosed by the customer as to his or her other security holdings and as to his or her financial situation and needs.

Both the Insurance Code (Title 48 RCW) and the Securities Act of Washington (chapter 21.20 RCW) recognize this overlap.

The Financial Industry Regulatory Authority (FINRA) is the largest non-governmental regulator for securities firms in the United States. The FINRA was established in 2007 in a merger between the National Association of Securities Dealers and portions of the New York Stock Exchange. As a self-regulatory organization, FINRA must be registered with the Securities and Exchange Commission (SEC). The FINRA rules must be reviewed and approved by the SEC. The FINRA has rules regarding suitability, including the suitability of annuities.

Summary of Bill:

Before the execution of a purchase or exchange of an annuity resulting from a recommendation, an insurer or insurance producer must make reasonable efforts to obtain information concerning a consumer's financial background, investment goals, and other information used or considered to be reasonable in making recommendations to the consumer. Insurers and insurance producers must have reasonable grounds for believing that the recommendation is suitable for the consumer on the basis of the facts disclosed by the consumer. A recommendation must be reasonable under all circumstances actually known to the insurer or insurance producer at the time.

An insurer or insurance producer does not have an obligation to a consumer if the consumer:

- refuses to provide relevant background;
- fails to provide complete or accurate information; or
- decides to enter into an insurance transaction that is not recommended by the insurer or insurance producer.

Compliance with FINRA suitability rules satisfies the requirements for the recommendation of annuities registered under the Securities Act of 1933. This does not limit the Commissioner's ability to take enforcement action.

An insurer must establish and maintain a system to supervise recommendations that is reasonably designed to achieve compliance with the suitability requirements. The system must include written procedures and a periodic review of records that are reasonably designed to assist in detecting and preventing violations. An insurer may contract with a third party to establish and maintain the system of supervision. Compliance with specific standards satisfies the insurer's obligations when contracting with a third party.

The Commissioner may order reasonably appropriate corrective action to address any consumer harmed by the insurer's or insurance producer's violation. Any applicable penalty may be reduced or eliminated by the Commissioner if corrective action for the consumer was taken promptly after a violation was discovered.

Insurers and insurance producers must be able to make records regarding the information collected from the consumer and other information used in making the recommendations available to the Commissioner. These records must be available for five years after the insurance transaction or for five years after the annuity begins paying benefits, whichever is longer.

The Commissioner may adopt rules to implement and administer this section.

Exemptions are created for annuity recommendations involving specific factual situations.

This act does not impact the application of chapter 21.20, the State Securities Act.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill takes effect 90 days after adjournment of the session in which the bill is passed.