AMERICANS FOR ANNUITY PROTECTION
Advocacy in Action. Prosperity for All.

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AAP On DOL - The Better, The Bad and the Ugly!

Despite the widespread reporting that the final Rule made significant concessions to "industry," Americans for Annuity Protection maintains the real effect will obstruct Americans ability to move their qualified money to easily and cost-effectively to annuities. Access and affordability must be maintained and the final Rule does little to help American annuity savers.

While the ***1023 pages*** of the Final Department of Labor Fiduciary Rule are still being digested, we have some high level information about the final Rule and its implications on annuities.

We are pleased that many of the suggestions made by Americans for Annuity Protection throughout this process were addressed including:

1. Disclosure requirements are too complicated and confusing for consumers;
2. Fixed annuities (unfortunately this does not include FIAs) should enjoy an insurance exemption because they protect savings from market losses, provide reliable growth and promise guaranteed income you cannot outlive;
3. Record keeping requirements are overly prescriptive and burdensome and only benefit lawyers and regulators; not consumers; and,
4. A short 8-month implementation period demonstrates a lack of understanding of the comprehensive and firmly established annuity marketplace and will harm consumers.

Unfortunately, there are still considerable problems with the Rule that will disrupt the annuity marketplace for consumers seeking the insurance guarantees of annuities and create more costs for consumers with less access to advice.

As we dig into the pages, many more details and interpretations will continue to flow, but here is what we know today.

With apologies to Clint Eastwood the Better, The Bad and the Ugly with the DOL's final proposal.

The Better

Fixed Rate Annuities

Fixed rate annuities (the agents/brokers who sell them) are treated as Insurance Products, but **fixed indexed annuities (FIAs) have been carved out and treated like variable annuities**.

The DOL says it considers an annuity a fixed annuity under PTE 84-24 only if it offered benefits that "do not vary, in part or in whole, based on the investment experience of a separate account or accounts maintained by the insurer or the investment experience of an index or investment model."

This determination appears to be contrary to the US District Court of Appeals ruling that stipulated "FIAs are not akin to variable annuities, not securities, and not subject to regulation under SEC proposed regulation 151A."

Implementation Period

The Department extended the first phase of implementation to one year after publication of the final rule which means **April 10th 2017**. That means annuity professionals may sell all existing products until April 9th, 2015 and those product sales will be grandfathered - see below.

The full BIC and PTE disclosure provisions, the policies and procedures requirements, and the contract requirement go into full effect on **January 1, 2018**.

Disclosure

The disclosure requirements in the final Best Interest Contract Exemption are significantly streamlined.

Requirements to include projections (1,5 and 10 year) and the annual disclosure requirement, have been entirely eliminated.

The WEB disclosure requirement was also streamlined and individualized information about advisors is not required.

Data Retention

The Department has removed the burdensome and unnecessary record-keeping requirements and the final Rule requires that firms only need to retain the records that show they complied with the BIC or other exemption.

Grandfather Relief

New grandfathering provision allows for additional compensation based on investments made prior to the Applicability Date.

It includes compensation from recommendations to hold, as well as systematic purchase agreements, but requires that post-Applicability Date, additional advice must satisfy basic best interest and reasonable compensation requirements.

Proprietary Products

Advisors may continue to sell proprietary products as long as they disclose they only represent certain products. In addition, ***if there is another product they don't offer that does meet the client's best interest***, they do not recommend their product and understand if they do, they would violate the BIC.

Call Center "Advisory" Activity

The contract is between the firm and the client and a new contract will not be required for each interaction with a different employee of the same firm.

The Bad

Education

The Department also revised the final rule to allow asset allocation models and interactive investment materials to identify specific investment alternatives under **ERISA-covered** and other plans if certain conditions are met.

However, references to specific investment alternatives for IRAs are not treated as education under the education provision in the final rule.

So the ERISA plan is exempt but IRAs are not.

Reasonable Compensation & Prohibited Compensation

Reasonable compensation is still not defined or clarified, leaving any determination to court actions or individual players.

Prohibited compensation does not appear to be any more clarified. Given the fact that prohibited compensation makes the entire transaction prohibited, is a huge concern and exposure to lawsuits and excise taxation.

Both areas need more clarification to help firms comply with the Rule and not be exposed inadvertently and without intent to a prohibited transaction.

The Ugly

Fiduciary requirement

Under ERISA law, which is different than the Uniform Security law, the definition of a fiduciary is he or she must act in the prudent and **SOLE INTEREST OF THE CLIENT**. This makes the annuity insurance sale particularly difficult and legally conflicted because the annuity advisor is also under the laws of Agency which require the annuity professional to have a contractual duty to the insurance company. How can an agent act in someone's SOLE interest if they are also legally bound by contract to another party? As our good friend Jim Mumford, former Iowa Deputy Commissioner often quoted, the law can't serve two masters.

The Excise Tax

A prohibited transaction – one that involves unreasonable compensation, prohibited compensation or does not materially disclose a conflict(s) of interest – would be subject to a separate excise tax by the IRS. This can be up to 100% of the "prohibited transaction," which in the annuity world probably means the annuity account value. So, a $100,000 annuity that is deemed a prohibited transaction, can mean the advisor has to pay out of his or her own pocket $100,000 in excise tax; which is **in addition to** returning the annuity value amount to the customer.

The Ugliest

BIC – Best Interest Contract

1. FIAs recommendations that involve commissions or compensation not paid directly by the customer for a level fee or through the customer's assets will require a BIC. This means that FIAs

are treated like VAs under ERISA and ***potentially exposes them to security regulation through re-characterization under ERISA law***.

2. The contract must provide for a private course of action (aka a lawsuit) and ***may not require arbitration***. This creates a boon for lawyers, uncertainty and potentially extra costs for consumers, and extreme liability exposure for insurance companies.

Additionally, the BIC requirement was eliminated for ERISA plans; it only applies to IRAs and other non-ERISA plans. This concession to the 401(k) marketplace creates an un-level playing field between 401(k) advisors and IRA advisors. Favoring the 401(k) advisor at the expense of the private insurance market, limits consumer's ability to move to portable, aggregated and self-owned IRAs.

While we had hoped for so much more from the Department in terms of understanding the insurance nature of annuities and the harmful impact to retirement savers under this Rule, there is a rainbow to be found. In other words, the Sun WILL Come Out Tomorrow – through litigation!

There has been much reporting about the potential of interested parties litigating this Rule. Many were waiting to see the final Rule before determining their litigation strategy, which is reasonable. Americans for Annuity Protection supports litigation efforts because, while the Department appears to have made concessions around the margins, the devastation to the IRA annuity marketplace is still a clear and present danger to the very consumers it has declared to help.

It is obvious that The Rule benefits the 401(k) stakeholders (ERISA plans) at the expense of the IRA marketplace and ignores Americans' desires to aggregate 401(k) savings to better leverage ALL of their savings, to turn their non-portable savings into a personally owned and portable IRA, and to buy better savings options than the limited ones offered through their employer.

The Department never analyzed the impact on the fixed annuity marketplace, including the fixed indexed annuity marketplace. Also, they did the merest cursory review of variable annuities. As a result, they failed in their primary duty to provide a thorough analysis of both costs and benefits of the Rule *of the marketplace(s) it will affect*. The Department used selective and inconclusive analysis and arrived at their predetermined justification ignoring the multibillion dollar marketplace of IRA annuities.

But don't take our word for it. Craig M. Lewis, a finance professor at Vanderbilt's Owen School of Business and formerly the SEC's chief economist., explains it best in a FORBES article.

> *To drum up support for the proposal, the White House and the DOL have repeatedly claimed that conflicted advice from brokers costs investors $17 billion a year — despite a number of significant concerns about the reliability of the estimate and the results-oriented process that produced it.*
>
> *To reach its estimate, CEA asserts that several academic studies show that assets subject to broker commissions underperform similar products sold directly to investors (that is, without a broker and without a sales load) by approximately 1%.*
>
> *You don't have to be an economist [or even a kindergartner] to recognize the Administration's $17 billion talking point significantly overestimates the costs, if any, to investors relying on the "conflicted advice" of brokers. And you don't have to be a regulator to recognize that an*

independent and objective economic analysis should be performed during the public comment process, especially when the regulatory agency making the decision is not a subject matter expert. This is particularly true here given the significant impact that the rulemaking will have on tens of millions of investors.

Read the complete article here

As you recall, the court's final decision in the 151A lawsuit was also predicated on the failure of the SEC to complete its impact analysis.

In this week's column for Insurance News Net we discussed a recent court decision on the government's determination of Met Life's SIFI status. The reasons the judge ruled in the courts favor were strikingly similar to the Department's actions (or lack of actions like their inadequate and prejudiced impact analysis). So the potential for successful litigation is strong. Also, we believe, including the non-security fixed indexed annuity with security products while carving-out their fixed annuity brethren is extremely problematic for the Department and a boon to litigation efforts.

While some folks may be cheering and some making lemonade out of lemons, annuity professionals are severely impacted and must stay engaged.

New legislation was announced today from the House. While getting democrats on board may be tough, we have the story and the numbers to demonstrate that this Rule is harmful to consumers who want to move 401(k) assets or existing IRA assets to the protection and certainty of fixed indexed annuities – the most popular annuity in the market today!

With lifetime income guarantees and protection from market losses, while at the same time maintaining access to your annuity funds -three benefits not available in other financial products - fixed indexed annuities may be the only opportunity Americans have to save for retirement. So stay tuned in, stay engaged and subscribe to Americans for Annuity Protection and make sure you do your part to protect your clients' opportunities for annuities.