



State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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Attachments

Office of the Commissioner of Insurance Annuity Sales Supervision Advisory Committee

Minutes January 22, 2008

Council members present: Roberta Riportella, PhD, University of Wisconsin; Connie O'Connell, Parrett & O'Connell; DuWayne Mews, FIC, Financial Strategies; Mary Jan Rosenak, representing Representative Lasee; John Hendrick, Coalition of Wisconsin Aging Groups (CWAG); Martha Kendler, Northwestern Mutual Life; John Wheeler, John Patrick Planning Group; Carla Strauch, Thrivent Financial; Kathleen Rivera; and Patricia Struck, Department of Financial Institutions (DFI).

OCI representatives present: Deputy Commissioner Kimberly Shaul; Jennifer Stegall; Jean Terry; Guenther Ruch; Mike Honeck; Kevin Zwart; and Sue Ezalarab.

Others present: Patrick Nelson, Allianz; Paul Kohls, Allianz; Angela Hollan, Allianz; Rochelle Tourneau, Ameriprise; Terry Tiede, AVIA; John Gerni, ACLI; Bill Toman, Quarles & Brady; Wanda Wegner, CUNA Mutual; John Hammer, Penn Life; Rob Rusch, CUNA Mutual; Lucas Brunmeier, Penn Life; Susan Cellere, Northwestern Mutual; Sharon Brosnan; Thrivent Financial; and Brian Casey, Thrivent Financial.

Deputy Commissioner Kim Shaul chaired the meeting that began at 10:00 a.m. in Conference Room 227, 125 South Webster Street, Madison, Wisconsin.

I. Opening Remarks

Deputy Commissioner Kim Shaul said that this meeting like the September meeting will be about education. The Committee will be looking at models and sharing information in order to begin the rulemaking process. OCI has issued a Statement of Scope relating to the supervision systems addressing compliance with the law in the sales of annuities. The charge of the committee is to produce a work product that will be considered in formalizing an administrative rule setting forth the minimum supervisory requirements that annuity writers need to meet in order to sell annuity products in the state of Wisconsin.

II. Introductions

Deputy Commissioner Kim Shaul announced that Betsey Abramson, public member, has resigned from the Committee. OCI will be discussing whether or not to appoint another consumer representative. Senator Roger Breske is no longer the chair of the Senate Committee that deals with insurance and will no longer be a member of this Committee. Senator Jon Erpenbach who now chairs the Senate Committee on insurance has declined to serve on this Committee.

III. Approval of Minutes from September 11, 2007 Meeting

The minutes from the September 11, 2007, meeting were approved.

IV. OCI Policy Form Filing Presentation

Mike Honeck said that at the last meeting the Committee asked for an overview of the annuity policy forms approval process. Mike said that OCI has a form filing checklist that is intended as a guide for insurers to use when submitting various policy forms. The checklists are summaries and are not intended as an OCI directive nor to interpret or address technical legal questions. Mike gave an overview of the general filing requirements for individual annuity policy forms.

Interstate Compact

Mike Honeck said that legislation has been introduced that would enable Wisconsin to become part of an interstate compact. Wisconsin would join 30 other states that are part of the compact. Products that will be filed with the compact include annuity, life insurance, disability income, and long-term care insurance. The pending legislation will change Wisconsin's form filing approach to file and use. Under current Wisconsin law, with a few exceptions, no insurance policy or group certificate form may be used unless it has been filed with and approved by OCI before they can be used. Any form that has not been disapproved in 30 days in filing is approved. OCI will no longer approve many forms but will still review policy forms through market conduct examinations. By joining the compact the policy form would be submitted to the compact – a single point-of-filing for product review. OCI is trying to get the legislation passed before the end of the session.

Connie O'Connell said that the interstate compact bill, Assembly Bill 542 will be voted on in the Assembly on January 23.

V. Presentation: "Basic Annuity Basics"

John Wheeler, an agent with the John Patrick Planning Group gave a presentation on annuities.

An annuity is defined as "a specified income payable at stated intervals for a fixed or a contingent period, often for the recipient's life, in consideration of a stipulated premium paid either in prior installment payments or in a single payment."

There are two basic types of annuities:

- Immediate annuity — income stream begins immediately upon payment of the first premium.
- Deferred annuity — income stream begins later (or not at all, at the owner's discretion). There are three basic types of deferred annuities: fixed annuities; fixed index annuities; variable annuities.

Things that are common to all annuities include: current income is tax deferred, issued by life insurance companies, provides "income you cannot outlive provisions" and treated similar to IRA's for tax purposes.

Traditional Fixed Deferred Annuities and Fixed Deferred Index Annuities

How traditional fixed deferred annuities work: principal guaranteed by the insurer; a minimum interest rate (2-3%) is guaranteed; interest crediting methods differ among products; and some are CD-like annuities taken for a fixed term of years.

How fixed deferred index annuities work: the penalty period may last from 5-20 years; the principal may be only partially guaranteed; costs are higher and more complex than for traditional fixed deferred annuities; penalties are assessed for exceeding the "free out" amount; utilizing the "free out" amount usually destroys any index return; multiple crediting methods (annual reset, point to point, high water mark, any of which may include monthly averaging); in addition to surrender charges additional costs generally apply.

Practice applications for traditional fixed deferred and fixed deferred index annuities: long term investing where liquidity is a minor factor; as part of the bond component in an asset allocation program; for a risk averse client who wants an opportunity for higher returns in a low interest rate environment.

Suitability red flags for fixed index annuities: putting most or all of a clients' money in a fixed index annuity; "free out" portion of the index annuity normally loses the index gain if withdrawn, making it a poor choice to meet liquidity needs; unreasonably long surrender periods or liquidity requirements.

Variable Annuities

Variable annuities are a security; money is invested in market based subaccounts; has more risk than a fixed annuity and surrender charges are similar to fixed annuities. Producers that sell variable annuities are licensed by the Financial Industry Regulatory Authority (FINRA) and by OCI.

The risks may be managed by purchasing income guarantees; features a death benefit that may pay more than the annuity's market value; generally will outperform fixed annuities over long periods of time.

Practice applications for variable annuities: excellent alternative to non-deductible IRA's; better long term choice than a fixed annuity; can provide higher income for a client who had not done a good job saving; good choice for wealth transfer for an uninsurable client.

Suitability issues for variable annuities; can and probably will lose value at some point, making it unsuitable for a risk averse client; is expensive, making it unsuitable for a client investing solely in low risk subaccounts (fixed annuity would be a better choice).

Annuitization

Annuitization is the act of converting a deferred annuity to an income stream of some kind. Immediate annuities are "annuitized" at issue. It's like "buying a pension."

Practice applications for annuitization: reducing or eliminating social security taxation, lowering taxable income to allow for Roth IRA conversions or funding life insurance premiums for tax favored wealth transfer.

The presentation also included examples of annuity payouts, alternatives to annuitization, and case studies. The key to a suitable annuity sale is to know your customer, always consider liquidity needs, consider whether there is a better solution and do the right thing for your client.

John will send a copy of the PowerPoint presentation "Basic Annuity Basics" to Jennifer Stegall for distribution to Committee members and to the interested parties list.

Discussion on Annuity Presentation

Roberta Riportella said that she is concerned about agents selling annuities to consumers who have only \$30,000 in assets. DuWayne Mews said he thought variable annuities appear to be a problem because of the lack of disclosure on fees. Most people receive but do not review or understand the lengthy prospectus that is given to them. John Henderick said the most vulnerable people are the senior consumers. We need to be concerned about senior consumers who may have been good with handling money, accumulated a lot of money during their lifetime and then became impaired or senior consumers who are the surviving spouse of a person who was good with handling money.

VI. Allianz Presentation

Paul Kohls, Vice President Government Relations, said that the Allianz presentation would consist of what Allianz is doing today and what the company has done in the recent past. For the last 15-20 years annuities were used for accumulation not for annuitization. Allianz's annuity products include fixed, indexed, variable and immediate annuities. Their products are sold through independent agents, banks registered representatives and wirehouses. The evolution of suitability at Allianz began in the mid-1990's through the introduction of the Statement of Understanding (point of sale disclosure document) in all states. In 2000 the Statement of Understanding was now required in all states. In October 2004 after the adoption of the National Association of Insurance Commissioners' (NAIC) Model Suitability Law the suitability program was implemented in four states, including Wisconsin. In July 2005 program enhancements including no "opt outs" and analysis of surrender charges incurred with replacements. In the spring of 2008 additional enhancements will include recalibration of thresholds for elevated review and calls being made to seniors 75 and older.

Pat Nelson, Chief Suitability Officer said that the new product suitability form facilitates collection of data necessary for Allianz to assess suitability. The disclosure statement is required with each application signed by the agent and applicant. The disclosure statement provides the consumer with a clear explanation of the specifics of the product such as product features, benefits, costs and risks.

Allianz requires that a suitability form must be filled out for every annuity application submitted. This applies in all states regardless of age. Information taken from the application will be entered into a rules engine that reviews the application for threshold triggers (income too low, liquid assets below \$75,000). If the threshold trigger is exceeded the application receives manual review. An elevated review team with either request more information, offer to accept less money than applied for, offer a different product more suitable or decline to accept the business.

As part of Allianz's agent training program, Partnership for Consumer Trust ("PACT"), an eLearning center has been developed that has modules dealing with suitability, replacements, and disclosure. The PACT agent training program will provide extensive training, sales support and other resources to educate the agent about products and suitability standards and practices to help them make a proper sale. Agent training will be conducted through webinars, workshops and forums.

In addition to suitability training, Allianz uses several tools to monitor agent activity including, the LIMRA Cap survey that is sent to every policyholder within 30 days, FINRA monthly report review to cross check for registered reps who have been disciplined against its appointed agent list, agent oversight initiative to systematically review independent agents based on certain risk characteristics and an agency review process that monitors complaint trends and replacement activity trends.

Discussion on Allianz's Program

Kathy Rivera asked if agent training is required prior to selling annuity products. Allianz tracks which agents complete the training but the training is not required. Patti Struck asked how much of the program was due to the recent Allianz settlement with the Minnesota Attorney General. The program was being developed before the settlement but the settlement did affect the program. The new suitability form is a result of the settlement. Mike Honeck said that companies need to monitor their agents to make sure they are complying with suitability requirements. Agent monitoring is the key.

VII. Other Business

Patti Struck handed out copies of a report entitled "Protecting Senior Investors: Report of Examinations of Securities Firms Providing "Free Lunch" Sales Seminars. In response to concerns about "free lunch" seminars being held for senior investors the Securities and Exchange Commission (SEC), the North American Securities Administrators Association (NASAA) and the Financial Industry Regulatory Authority (FINRA) conducted examinations of broker-dealers, investment advisors and other financial services firms that offered these sales seminars. Examinations were targeted in areas of the country that have large populations of retirees, such as Florida, California, Texas, Arizona, North Carolina, Alabama and South Carolina. There were 110 examinations conducted between April 2006 and June 2007.

Many of these seminars are advertised as "educational," workshops," and "nothing will be sold at this workshop." Many of the advertisements did not mention any investment products. The concern is that seniors attending these "free lunch" seminars are unaware these seminars are a way to obtain new customers and sell investment products. The most commonly discussed products at the seminars were variable annuities, real estate investment trusts, equity indexed annuities, mutual funds, private placements of speculative securities (such as oil and gas interests) and reverse mortgages.

During the examinations regulators identified supervisory best practices that appeared to be effective. Regulators encourage financial services firms to take steps to assure that supervisory procedures with respect to sales seminars are being implemented effectively. Regulators also concluded that ongoing investor education efforts for seniors should provide education with respect to "free lunch" sales

seminars. Investor education should emphasize that investors should take time to research the firm, the financial adviser as well the product being offered before opening an account or making a purchase.

Carla Strauch said that after the last meeting Thrivent went back and looked at its forms for New Account and Suitability Information, the Asset Transfer Disclosure Information documents and the Deferred Variable Annuity Questionnaire and made changes to the forms. The new forms will be distributed to agents starting in May.

Guenther Ruch said that at the April 22 meeting there will be presentations by the Insurance Marketplace Standards Association (IMSA), the Financial Industry Regulatory Authority (FINRA) and the Iowa Insurance Department. OCI staff will be working with Kathy Rivera on an initial draft based on presentations and discussions from the meetings.

VIII. Adjourn Meeting

The meeting adjourned at 2:30 p.m.

Attachments

State of Wisconsin Office of the Commissioner of Insurance
Form Filing Checklist – Individual Annuity (oci.wi.gov/ociforms/indannck.pdf)

2007 National Association of Insurance Commissioners
Life, Accident & Health, Annuity, Credit Transmittal Document
http://www.naic.org/documents/industry_rates_lh_trans.doc

[Basic Annuity Basics PowerPoint Presentation](#)
By John Wheeler, John Patrick Planning Group

Protecting Senior Investors: Report of Examinations of Securities Firms Providing “Free Lunch” Sales Seminars

By the Office of Compliance Inspections and Examinations, Securities and Exchange Commission; North American Securities Administrators Association; Financial Industry Regulatory Authority - September 2007
www.sec.gov/spotlight/seniors/freelunchreport.pdf