

# The annuity landscape

Five trends to watch for in 2013 and 2014



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## Our editor and our authors:



**Christopher Raham**  
*Editor and Principal*  
Ernst & Young LLP  
christopher.raham@ey.com  
+1 212 773 9064



**Gerry Murtagh**  
*Assistant Director*  
Ernst & Young LLP  
gerry.murtagh@ey.com  
+1 212 773 5667



**James Collingwood**  
*Manager*  
Ernst & Young LLP  
james.collingwood@ey.com  
+1 312 879 6306



**Doug French**  
*Principal*  
Ernst & Young LLP  
doug.french@ey.com  
+1 212 773 4120



**Ben Yahr**  
*Manager*  
Ernst & Young LLP  
ben.yahr@ey.com  
+1 215 841 0577



**Jacqueline Boersema**  
*Executive Director*  
Ernst & Young LLP  
jacqueline.boersema@ey.com  
+1 704 331 1867



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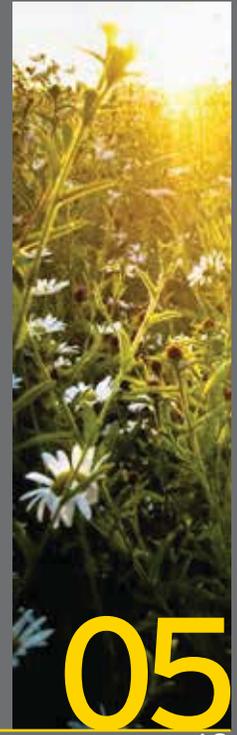
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# Top 5 trends in the annuity industry in 2013

Against a backdrop of improving economic conditions in the US and the stock market reaching an all-time high, insurers continue to reposition and reinvent their products, strategies and services. These changes enable insurers to offer advisors and investors a broad range of products despite the challenges of the continuing low interest rate environment. For advisors, staying up-to-date with the changes in the market and the characteristics of the products currently available is critical to serving the needs of your clients.

In recent months we have seen John Hancock exit the annuity business altogether, while other companies have limited the amount of annuity business they accept to help actively manage their risk. Some companies have even offered to buy out the guarantees in exchange for adding a lump-sum to the client's account value. On the other hand, a few companies have made the strategic decision to add variable annuities (VAs), fixed indexed annuities or fixed annuities to their platforms. These companies hope to take advantage of the unmet marketplace needs for higher rates of return and guaranteed income.

At EY, we continuously monitor the product and solution landscape to help organizations and advisors keep abreast of the ever-changing market. We have identified five trends that will influence the annuity marketplace in 2013.

## **1. The reshaping of the VA market: opportunities remain for advisors who can navigate the new landscape**

Record low interest rates and the costly price of hedging are causing insurers to continually evaluate whether they want to remain in the VA business. Several companies will continue to curtail sales of VAs by lowering the benefits, while others will manage sales volumes by no longer accepting 1035 exchanges. Additionally, insurers will continue to drop aggressive investment options on their VAs and move customers into funds that are less volatile. It remains to be seen if additional buyout offers to contract owners will be made or expanded to other GMXB benefits.

## **2. Hybrid products – good for clients, good for advisors?**

Companies have started to file and introduce products that are hybrids of VAs and fixed products. These products have an upside for both the company and the client due to the lower capital requirements for the company and the downside protection offered to the contract owner. As with any new offering, it is yet to be seen how these products will be received and how product designs will evolve. However, the initial designs appear to provide an attractive option for customers. At the same time, though, potential regulatory headwinds exist.



### 3. Can new entrants fill the gap?

Even though several companies have exited the annuity business, other carriers are adding annuities to their platforms. In some cases, when exiting a line of business or market, the books of business, operations and distribution are often available for sale. This availability enables aggressive entrants to quickly build operational scale and capacity, and ultimately market share. Acceptance by channel and product will likely vary, with fixed annuities by independent marketing organizations (IMOs), broker-dealers and bank platforms leading the way.

### 4. Top products for an advisor platform

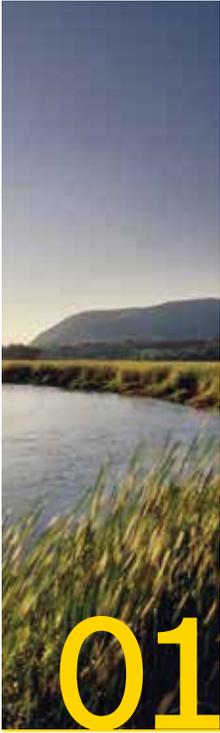
Over the past two years, many companies have introduced VA products targeted to registered investment advisors (RIAs) with features that offer guaranteed lifetime income. However, the growth in the RIA VA marketplace has been slower than anticipated and significant obstacles exist that will limit future growth in this space. Given that many RIAs may have a preference for other methods of generating retirement income, it is likely that placement rates will remain low for some time. New products and features will attempt to break out of this cycle.

### 5. Meeting suitability and other sales practice requirements

We are now starting to see some effects of the FINRA's new suitability and know-your-customer (KYC) rules that took effect in July 2012. In response to the new regulations, many firms have established procedures for gathering client information, record-keeping and product training to help advisors understand their new KYC and suitability obligations. Challenges include capturing the right data; asking for more information, if necessary; and proper documentation. Firms are trying to anticipate regulators' inquiries and challenges and are setting up internal governance structures. Many firms are setting up structures to regularly monitor third-party distributors.

#### Conclusion

Annuities offer clients predictability and security in any market, so we will continue to see the insurance industry focus on them. Manufacturers will look to diversify their product lines, products and features so they are not too concentrated in any one area. The industry will seek to achieve the optimal balance of what is best for the client, advisor and shareholder. Within this publication, we will explore each of these trends in more detail so you can maintain your competitive edge.



# The reshaping of the variable annuity market: opportunities remain for advisors who can navigate the new landscape

by  
Gerry Murtagh

Major changes continue to reshape the variable annuity (VA) market, and the rate of change has intensified in recent years. With major players exiting the space, benefits being cut and fees increasing, advisors are challenged to keep up with rapidly changing product offerings and find solutions that meet client needs. The good news is that clients remain interested in VA products; therefore, advisors willing to invest the time and effort to understand the new landscape can continue to find opportunity and create value.

Over the past few years, major VA players – including Genworth, ING, Sun Life, The Hartford and John Hancock – exited the VA business. For advisors, greater market concentration means potentially fewer products and riders to offer clients. Given the number and rate of changes insurers are making to the VA products, having fewer companies to keep up with might be a good thing for advisors. On the other hand, there is less competition, so advisors and clients might find themselves getting less and paying more for it.

The ongoing low interest rate environment and the high cost of hedging are leading to adjustments in benefits and fees. Benefits are decreasing, while fees are increasing. In addition, companies are managing sales volumes by refusing to accept 1035 exchanges and limiting additional premium payments.

These trends most likely will continue. As they seek to slow the growth of new contracts with living benefits, companies will restructure living benefits, particularly in the area of guaranteed lifetime withdrawal benefits (GLWBs). With GLWBs, insurers are decreasing the withdrawal percentage (the amount of the income base a contract owner can withdraw each year) and bonuses, while increasing charges or restricting investment options. Prudential and other companies have introduced new, less-competitive benefits and pulled richer ones from the market.

Market snapshot	Q1 2012	Q2 2012	Q3 2012	Q4 2012	Q1 2013
No. of new VA products	4	7	4	1	2
No. of new living benefits	5	6	14	1	6
No. of VA product changes	9	7	1	2	2
No. of living benefits with changes	7	9	8	11	9
No. of VA products pulled	0	9	3	8	3
No. of living benefits pulled	7	5	6	6	8



Insurers continue to drop aggressive investment options on their VAs and move clients into less volatile funds. For instance, AXA Equitable Life Insurance Company (AXA) is dropping 26 investment options from one of its VAs and moving money to more conservative funds. Many of these replacement funds feature a volatility management strategy. Nationwide Financial is adding four new managed-volatility fund options to its VAs, and Prudential is adding six new asset allocation funds to its Highest Daily Lifetime Income Benefit. For advisors, these embedded portfolios offer more stability around account value for their clients, and the insurance companies are more comfortable with the guarantees, thanks to the increased fees.

Prudential, MetLife and AXA are among the insurers barring contract owners from making additional premium payments on some existing contracts. Most of the affected contracts are those with a generous living benefit or death benefit. In the past, insurers rarely, if ever, exercised this contract provision.

More insurers are also offering buyouts to contract owners. The Hartford is the latest company to offer some of its contract owners the opportunity to exchange a living benefit for an increase in account value. Earlier, AXA and Transamerica offered contract owners the option to drop certain riders in exchange for an enhanced cash value. It remains to be seen if additional offers to buy out contract owners will be made or expanded to other guaranteed minimum withdrawal benefits (GMWBs).

Despite these extensive product changes, consumers remain interested in VAs. In fact, today's VA products are much more rational due to the large-scale changes that have been made to the base products and living benefits. Companies are no longer trying to gain market share, but rather, aiming to balance their own needs and objectives with those of clients and advisors. For advisors, staying up to date with all the changes in the market and the characteristics of the products currently available is critical to serving the needs of clients.



## Hybrid products: good for clients, good for advisors?

by  
*James  
Collingwood*

Recently, insurers have begun to develop annuity products that are hybrids between fixed indexed annuities and structured products. These hybrids are designed to offer consumers downside protection (at the expense of upside limits) while also protecting insurance companies from the market risk that comes with traditional variable annuity (VA) product designs. To date, only two companies, AXA and MetLife, have begun to offer these products for sale, with Allianz also having filed a similar product with the Securities and Exchange Commission (SEC). As more companies begin to file these products, there is likely to be some evolution in product design, but it is not completely clear what future iterations may look like and how advisors will respond. Finally, regulators have begun to give these products some consideration and will likely continue to do so as these products increase in size.

AXA was the first insurer to offer these hybrid products, having introduced its Structured Capital Strategies VA product in 2010. Over the past two years, AXA has sold more than US\$2 billion of this product. MetLife is the most recent entrant into the market, introducing its Shield Level Selector single-premium deferred annuity for sale in early May. Allianz represents the other potential market participant, having filed a VA contract prospectus with the SEC.

A key difference between these products and many variable and fixed indexed annuity products on the market is that these products are designed as

accumulation vehicles, not as income products. Neither the AXA product nor the MetLife product has any guaranteed living benefits, and only the MetLife product has an optional death benefit of the greater of account value or premiums, less withdrawals.

At their hearts, these products function like traditional fixed indexed annuities without guaranteed living benefits. To support the product, the insurer will invest most of the premium in bonds and use the remainder to buy equity index options to support the interest credited rate that is based on the performance of an underlying equity index. However, the key difference between these products and traditional fixed indexed annuities is that investors can lose money on these products, whereas traditional fixed indexed annuities guarantee that investors will never lose money.

Similar to traditional fixed indexed annuities, these products allow investors to invest indirectly in the performance of an index and share in a portion of the index return. This differs from VA products, which allow investors to invest directly in separate accounts that closely track index returns through a mutual fund-like structure. The products from AXA and MetLife offer a choice among many traditional equity index options (e.g., S&P 500, Russell 2000, MSCI EAFE) and some commodity-based indices. Additionally, the products offer different maturities for index returns, with AXA offering one-, three- and five-year buckets and MetLife offering one-, three- and six-year buckets.



One of the key final choices investors have to make is how much of the downside risk are they willing to take. The AXA product offers three different “buffer” levels, whereby they will absorb the first 10%, 20% or 30% of any loss, while the MetLife product offers four different levels (10%, 15%, 25%, 100%). The amount of loss the investor elects to have the insurance company shoulder impacts the crediting rate terms. As more of the loss is assigned to the insurance company, the credited rate terms and index options become more restrictive to the investor and vice versa. In other words, the higher the buffer levels chosen by investors, the less they will share in any upside market performance.

These products allow investors exposure to equity markets, while minimizing their downside risk exposure and preserving principal. Additionally, the different buffer levels allow investors to choose the risk/return tradeoff that best suits their risk tolerance and financial situation. For insurance companies, these products provide an opportunity to remain active in the annuity space, but lessen their exposure to the market swings that come with VA product lines. Additionally, the lack of guaranteed living benefits on these products shields the insurer from the additional financial volatility these riders bring.

While AXA has had success selling this hybrid product over the past few years, the product’s overall slice of the annuity market pie is still small. The product design, which builds on the already complicated design of fixed indexed annuity products, is complex and may take some time for investors and advisors to understand with regard

to product functionality and value. Additionally, the lack of guaranteed living benefits that have helped drive sales in the VA and fixed index annuity space may be seen as a drawback by some advisors looking for more income-centric products. However, these hybrids may, ultimately, have a place in investors’ portfolios as a complement to, rather than a replacement of, more income-centric variable and fixed indexed annuity products.

Finally, these products have begun to catch the attention of regulators. At the Life Actuarial Task Force session during the most recent National Association of Insurance Commissioners (NAIC) national meeting in April, a regulatory actuary expressed concern about the filing of these hybrid products as VA contracts due to potential conflicts with the NAIC Variable Annuity Model Regulation, and suggested that the NAIC further review the VA regulatory framework to assess its appropriateness for the products. There has been no further discussion of this issue publicly to date, but this is likely to be something regulators will begin to consider further.

While the evolution of these hybrid products is yet to be seen, they offer potential benefits for investors and insurance companies and could become a popular annuity product offerings in the future.



## Can new annuity entrants fill the gap?

by  
*Doug French*

Since the global financial crisis, many of the largest insurers in the United States have exited the annuity market entirely, or have limited production due to capital constraints and the ongoing impact of the low interest rate environment. Throughout 2012 and the first part of 2013, advisors have continued to cope with these changes in the annuity landscape. While some companies have added variations of annuities to their platforms in an effort to fill the void left by the exodus of the traditional annuity manufacturers, the overwhelming trend has been fewer choices and uncertainty for advisors as they try to meet their clients' growing demand for retirement solutions. As demographics and memories of market volatility continue to drive baby boomers' needs for stable accumulation and guaranteed income provided by this product segment, the question remains, "How will the product provider gap be filled?"

### **Rise of the new entrant**

Over the past 12 months, we have observed a trend worth watching closely. The acquisition by "new entrants" of unencumbered product development functions, new business operations and distribution relationships from existing insurers is creating new launching pads for the next generation of annuity manufacturers. These new entrants have reacted to and leveraged lessons learned by prior players and are positioning themselves to quickly capitalize on traditional providers' changes in strategic

direction. New entrant management teams and their partners recognize the value of distribution relationships, operational scale and intellectual capital that accompany these acquisitions. Their actions today will allow them to quickly build product and operational scale, while providing capacity to market.

Some new entrants are piloting their new capabilities and products in a few states, affording them an opportunity to work with existing advisor networks and marketing organizations to get everything right – before their products are introduced nationally. In the majority of these cases, platform acceptance is not an issue; advisors are already familiar with the benefits of annuities and thus require less training. The new offering is an additional option for advisors to offer their clients.

### **Old providers – new capacity**

The increased pace of private equity-backed acquisitions in the annuity industry is a trend we believe will also have a beneficial impact on the new product availability, albeit on a longer timescale. As existing back books of business move off the balance sheets of traditional annuity providers and create some "headroom" in capital availability for annuities, the stage will be set for new designs from traditional providers. Burned by recent experiences, however, the return will be gradual and slow in nature, driven by "sustainable manufacturing



approaches," particularly in the variable annuity (VA) marketplace. Simpler or non-traditional offers supported by those with big name recognition are the dominant approaches we see emerging under this model. Those with access and acceptability on bank platforms have the advantage of being able to build on their existing relationships and attractively position annuities as alternative investments to clients in the current low interest rate environment.

### Focus on new areas

At the most basic end of the scale, selected new entrants are offering very simple, low-cost annuities focused on investment flexibility and tax advantages to capture 1035 exchanges or as alternatives to individual retirement account (IRA) rollover vehicles.

Fixed indexed annuities have evolved significantly from a product development standpoint and appear to be gaining acceptance on bank and broker-dealer channels. New entrants have developed simpler fixed indexed products with shorter surrender-charge schedules to counter the criticism that these annuities are complicated because of complex crediting strategies and sizeable surrender charges. Advisors are aware of more transparent products in the market that their clients can understand more easily. Of course, complex strategies wrapped with guaranteed income benefits remain popular.

VAs are more sustainable than ever, driven by the many large-scale changes that have been made to the base products and living benefits. The embedded portfolios on VAs with particular living benefits offer more stability around account value to clients, and insurance companies are more comfortable managing the guarantees as a result. In some cases, features of fixed indexed guarantees, including participation rates, are appearing in this lineup.



### **Stay the course**

Most certainly, there are challenges new entrants must face to gain both producer and client acceptance, build share in their chosen space and successfully fill the gap. Similarly, traditional providers who plan a return to the space “at the right time” or enter the fixed indexed annuity market in lieu of participating in the VA market will face challenges driven by the historical “in, out and back in again” approach to managing risk at the expense of continuity in the minds of advisors and customers. In either case, manufacturers must adopt a management approach that will allow it to stay the course when its books are tested by the persistent conditions of a slowly recovering economy and the potential for future severe market events. Whether that means practicing consistent, prudent risk management or finding a balance of business to avoid the historical lessons of over-concentration in any one feature, product or product line, steady as she goes must be a management imperative. Companies must work together with advisor and customer groups to develop and offer valuable products based on reasonable expectations of all parties.

### **Partner with advisors and channels**

It is our belief that advisors should have a clear understanding of the value of these benefits to their clients, given the market over the last few years, and understand the value of having their partner companies continue to offer annuities. We believe advisors will become increasingly important collaborators to positively influence product design and distribution models supported by rationale, valuable guarantees and appropriate compensation. Filling the gap successfully in a sustainable way depends on it. New annuity entrants would be wise to pursue this approach as differentiators.

**Annuities offer clients predictability and security in any market, and we will continue to see the insurance industry focus on them.**



# Top products for an advisor platform

by  
Ben Yahr

In the recent past, insurers have viewed stronger relationships with registered investment advisors (RIAs) as a critical element of their growth strategies. Compared with other types of asset managers, RIAs have seen their asset bases expand – a trend many in the industry expect to continue. To capture market share in the RIA channel, variable annuity (VA) writers have introduced customized versions of their core offerings targeted to RIAs. In fact, 18 of the top 20 VA insurers offer RIA VAs, according to 2012 sales data from LIMRA, but the expected VA growth in the RIA distribution channel hasn't yet materialized, leaving many insurers perplexed as to why.

We will briefly discuss what we believe are some of the factors that have limited insurers' ability to capture market share through RIAs and suggest a range of strategies and tactics that insurance companies can adopt to improve growth in this channel.

## 1. Overcome negative advisor bias

In our experience, many fee-based RIAs seem to be biased against annuities. In some cases, their views are based on an educated analysis of VA products; in others, their views are based on a bad past experience with a company representative, or an uncomfortable client experience with a complex VA contract. In addition, fiduciary duties toward clients and standard compensation structures also impact the RIAs' perceptions of VAs. Whatever the case, many advisors are not fully convinced these financial instruments are a good fit for clients. Thus, they are reluctant to recommend VAs. As a mentor in the business would say, "A sale is first made in the advisor's mind." Whatever the reasons for the bias, insurance companies face an

education challenge. Specifically, they must improve their communication and storytelling efforts with regard to the merits of VAs and their usefulness (and appropriateness) for different types of investor objectives and how they fit within a client's portfolio. Further, insurers must spend more time with RIAs developing their understanding of the objections and concerns most frequently confronting fee-based advisors. For example, RIAs often want to see some credible analysis with hard numbers showing that VAs are good alternatives. Co-developing credible responses that improve the likelihood of a sale in the advisor's mind can be the solid foundation for a growing relationship.

## 2. Justify the cost structure

The higher fee structure of VA products (compared with other investments offering a guaranteed source of income) is far and away the top reason clients do not purchase VAs. Higher costs are a big issue for RIAs, who have a well-earned reputation for being hypersensitive to fees. Many RIAs may focus on a total return type of analysis, utilizing tools and materials they currently have in place for evaluating investment options. If insurers are to drive growth through the RIA channel, they must be ready and willing to justify the higher costs of contractual guarantees by clearly demonstrating the superior client outcomes when it comes to income benefits, death benefits or tax benefits. In some circumstances, companies may need to sharpen the pencil on management and administrative expense fees in order to gain acceptance. For example, the combination of a balanced-risk fund and a growth-of-dividends fund is likely to be discussed as a retirement income solution with lower total fees than a typical RIA-channel VA, once



the latter's management and administration fees, mortality expense charges and rider fees are taken into account. An insurer should educate and enable RIAs regarding the cost-value propositions to increase the likelihood of VA sales.

### **3. Enable advisor compensation**

Because of the design of annuities, withdrawing advisor fees from the basic VA contracts can generate negative tax consequences for clients. Similarly, when clients elect an income rider, withdrawn fees can either reduce the guaranteed income available to the client or undermine the rider guarantees. As such, RIAs historically have needed to collect fees from other client accounts under management – something that could be solved through RIA-friendly contracts. A basic objective for insurers should be to educate RIAs on efficient ways to collect fees and enable them with tools or technology to collect fees, even if not collected from the VA. Further, client-friendly materials explaining to clients how such fee withdrawals work would be appreciated by RIAs.

### **4. Adjust for dual registration**

There is one other complicating factor worth mentioning – the growing number of dual-registered agents in the market today. Such agents may find a better value for clients by selling annuities as registered representatives, rather than as RIAs. There are clear benefits of this approach for clients, who ultimately benefit from lower costs. Dual-registered agents are likely to compare both retail and RIA versions and choose whichever is more beneficial – a fact insurers must address in their product design and marketing programs.

### **5. Refine segmentation**

Because VAs are complex flexible financial instruments with a variety of uses, they have suffered from an identity crisis. Is the key benefit income generation or tax deferral? Given the tax rules for annuities, it can't be both. To help RIAs understand appropriate uses for VAs, insurance companies need to clearly articulate the target customer profile and the value proposition. For example, let's assume the target customer is an ultra high-net-worth couple with a small qualified portfolio relative to their overall wealth. It's likely that this couple is in the top income tax bracket and the advisor may be avoiding certain asset classes that would diversify the portfolio because of potentially adverse tax consequences (think hedge fund or other actively managed investment with a high annual turnover). If the client and advisor can elect the desired investment within a low-cost VA, the tax benefits would create a compelling value proposition. Several carriers have designed private placement VA products that are specifically tailored to this market.

None of these five factors is necessarily a deal breaker for insurers seeking to grow their businesses with RIAs. However, they each represent a challenge that must be addressed both strategically and tactically in order to improve adoption. Insurers that can design VA products that meet client needs in specific customer segments and clearly communicate the value proposition have an opportunity to gain a substantial competitive edge in the RIA market.



# Meeting suitability and other sales practices under FINRA 2111

by  
*Jacqueline Boersema*

Over the past few years, insurers have been provided with suitability standards and guidelines with respect to recommending and selling annuity products to clients. This past year, the Financial Industry Regulatory Authority (FINRA) (under rule 2111) provided an expanded list of the type of information an advisor must obtain from a client and analyze prior to making a product recommendation. In addition, insurers have been given a suitability framework under the 2010 Suitability in Annuity Transaction Model Regulation (the Model Regulation) that addresses suitable annuity transaction sales, supervision, monitoring and reporting. Fortunately, the Model Regulation standards were written to be, when feasible, consistent with the suitability standards under FINRA 2111. This article will review the standards under both rules and highlight what companies are doing to comply.

Client suitability under FINRA 2111 states that “a broker-dealer or associated person has a reasonable basis to believe that a recommended transaction or investment strategy involving a security or securities is suitable for the customer.” This past year, the rule was expanded to provide explicit guidance on the type of client information an advisor should obtain and analyze to determine suitability (referred to as the customer investment profile).

The following table reflects the information an advisor must attempt to obtain under FINRA 2111. The additional requirements, which were added under the new rule, are indicated by an asterisk in the customer investment

profile table below (age, investment experience, time horizon, liquidity needs and risk tolerance).

Customer investment profile
1. Age*
2. Investment objectives
3. Other investments
4. Investment experience*
5. Financial situation and need
6. Time horizon*
7. Tax status
8. Liquidity needs*
9. Risk tolerance*
10. Any other information the customer discloses

Although the new rule is specific with respect to client information an advisor must obtain and review before making a product recommendation, it does not provide explicit guidance on documenting evidence of suitability. Instead, the rule suggests that firms take a risk-based approach when documenting suitability determinations, which, most likely, will vary based on the customer’s profile and the complexity, performance and risk of the recommended security.



However, for providing documentation evidence for annuity transaction, there is tangible guidance provided under the Model Regulation:

- ▶ A producer or insurer shall record any recommendation given, including evidence that a reasonable effort was made to obtain the client's suitability information.

And for client discussions that did not result in a recommended product sale, the insurer should obtain:

- ▶ Signed documentation stating the customer refused to provide suitability information

Or

- ▶ Signed documentation that the annuity transaction is not recommended and is not based on the advisor's recommendation

Also, under the Model Regulation, insurers are required to establish a system to supervise recommendations to meet insurance needs and financial objectives of the client. The supervision system typically entails supervising procedures, training and spot checking recommendations. When conducting spot checks, the supervisor must review all supporting information the advisor used or created to establish a reasonable suitability basis for the product recommendation to the client. Hence, the review is of the entire file, which will contain suitability documentation the client provided as well as documentation the advisor created during the product and recommendation discussion with the client.

Thus, documentation of client signatures and that a supervisory review process is in place is good practice to meet minimum requirements under the Model Regulation. However, there are additional steps companies have

taken to have a sound suitability approach in place that will address regulatory inquiries. For instance, companies should consider developing and documenting a suitability approach and process that may contain all or some of the following steps:

### **Satisfying FINRA 2111**

- ▶ Updating existing customer questionnaires (customer investment profiles) to address the new revised FINRA 2111 requirements
- ▶ Creating or updating risk tolerance questionnaires that test and quantify the client's risk tolerance using a weighting or scoring approach
- ▶ Creating risk tolerance profiles (based on the risk tolerance scoring approach) that define the client's risk appetite (conservative, moderate or aggressive)
- ▶ Aligning product offerings to risk tolerance profiles (product risk matching) so the advisor can sell only products that match a client's specific risk profile
- ▶ Developing and conducting training on the firm's suitability approach and process
- ▶ Documenting the firm's suitability approach, process and training so it is readily available to provide to a regulator, if requested



### **Satisfying the Model Regulation:**

- ▶ Developing and conducting specific product training
- ▶ Providing a one-time, minimum four-credit-hour, general annuity training offered by an insurance department-approved education provider
- ▶ Establishing a process to have a supervisor review a product recommendation prior to the issuance of an annuity
- ▶ Producing an annual report to senior management that includes compliance review results (pass/fail rates, exceptions, complaints, sanctions and corrective actions taken)
- ▶ Creating an ongoing (e.g., quarterly) internal suitability compliance review and monitoring following the sale of a product

The Model Regulation does permit companies to hire a third-party provider to establish its systems of supervision, including monitoring and conducting audits on behalf of the company. If a third-party provider does perform this role, the company must obtain an annual certificate stating that the suitability function has been properly performed.

Recent regulations have provided a suitability framework that companies selling investment and insurance products can use to create a suitability approach. The key to satisfying regulatory inquiries is to provide that the approach, process and training are well documented, should the regulators inquire as to how companies are determining, supervising and monitoring that their advisors are selling suitable products to clients.

**The industry will seek to achieve the optimal balance of what is best for the client, advisor and shareholder.**

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