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Consumer Group Faults Insurance Regulators for Failing to Protect Consumers

NAIC Greenlights Complex, High-Fee, Low-Value “Retirement Income” Product: Contingent Deferred Annuities

Proposed Action Highlights the Need for Department of Labor’s Fiduciary Rule

The Center for Economic Justice (CEJ) criticized state insurance regulators’ failure to protect insurance consumers from a complex, high-fee, low value “retirement income” insurance product – the Contingent Deferred Annuity (CDA). CEJ said the state insurance regulators’ failure highlights the need for the U.S. Department of Labor’s proposed rule requiring those who advise retirement savers to purchase CDAs and other products to put the consumer’s best interest before the seller’s interest – a fiduciary duty.

The National Association of Insurance Commissioners¹ Life Insurance Committee adopted a regulatory guidance manual for CDAs at the organization’s recent meeting, but the guidance manual provides little actual regulatory guidance and omits crucial consumer protections.

CEJ pointed to the NAIC’s definition of a CDA to demonstrate the complexity of the product:

An annuity contract that establishes a life insurer’s obligation to make periodic payments for the annuitant’s lifetime at the time designated investments, which are not owned or held by the insurer, are depleted to a contractually defined amount due to contractually permitted withdrawals, market performance, fees and/or other charges.”

¹ The NAIC describes itself as the U.S. standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia and five U.S. territories. Through the NAIC, state insurance regulators establish standards and best practices, conduct peer review, and coordinate their regulatory oversight. NAIC staff supports these efforts and represents the collective views of state regulators domestically and internationally. NAIC members, together with the central resources of the NAIC, form the national system of state-based insurance regulation in the U.S.

“The so-called regulatory guidance is simply an act by insurance regulators to unleash another complex, low-value ‘retirement income’ product onto consumers without any meaningful consumer protections. The product should not even be allowed in the marketplace since it violates every state’s law that insurance commissioners may not approve products which are misleading. **We commend the insurance regulators in New York, California and Minnesota for refusing to approve CDAs,**” said Birny Birnbaum, Director of CEJ.

Birnbaum continued, “The CDA is a fee harvesting product for insurers with little likelihood of payout to policyholders and a very low benefit-to-fee ratio. The benefit ratio is so low that insurers and insurance regulators refused to disclose it to consumers. It is unlikely that CDAs could be sold if the sale was subject to a consumer best interest standard, but insurance regulators applied the lesser suitability sales standard instead. The promotion of these abusive products by most state insurance commissioners – instead of stopping the products from entering the marketplace – is a vivid demonstration of the need for the Department of Labor to finalize its fiduciary standard rule.”

Among the critical consumer protection omissions from the guidance document are plain-English consumer information and disclosures to enable a consumer to actually understand what benefits the product provides, how the product operates, the likelihood of a consumer ever getting a benefit or the costs of the product.

“Rather than developing and requiring essential consumer information, the insurance regulators simply said no such information need be provided to consumers,” said Birny Birnbaum, Director of CEJ.

The guidance document states that annuity disclosure requirements applicable to other annuities also apply to CDAs, but then states that since no CDA consumer information exists, the annuity disclosure requirements can be ignored for CDAs:

Providing the current buyer’s guide for fixed and variable annuities, which is inapplicable, for CDAs may confuse consumers. **Therefore, the Working Group concluded that the requirement to provide a buyer’s guide would not be appropriate for CDAs.** (Emphasis added)

This is an example of the guidance document concluding that an important consumer protection model doesn’t neatly apply to CDAs, but instead of adjusting the model or developing the missing consumer protection, the guidance document leaves a hole. The NAIC is effectively saying, “We don’t have a regulatory tool that addresses this issue with CDAs, so we will exempt CDAs from this consumer protection.” CEJ provided a template for such critical consumer information, but the CDA subgroup declined to pursue the development of this essential consumer information.

The insurance regulators also failed to protect consumers by denying consumers a “nonforfeiture benefit.” A nonforfeiture benefit is simply a value built up over time as consumers pay premiums and fees for insurance products that accumulate benefits over that time. Despite calls from CEJ and the American Academy of Actuaries that a nonforfeiture benefit was appropriate for CDAs, the insurance regulators failed to include any protection for a consumer who pays into the CDA for decades and then decides to get out of the policy – with nothing to show for it. Instead, the regulators included a “cancellation benefit” providing a variety of options to insurers in the event that the insurer decides to unilaterally change the CDA terms.

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