Case No. 530047

New York Supreme Court
Appellate Division—Third Department

In the Matter of the Application of
INDEPENDENT INSURANCE AGENTS AND BROKERS OF NEW YORK, INC., and TESTA BROTHERS, LTD.,

Petitioners-Appellants,

– and –

PROFESSIONAL INSURANCE AGENTS OF NEW YORK STATE, INC., and GARY SLAVIN,

Petitioners,

For judgment pursuant to CPLR Article 78

– against –

THE NEW YORK STATE DEPARTMENT OF FINANCIAL SERVICES and MARIA T. VULLO, in her official capacity as Superintendent of the New York State Department of Financial Services,

Respondents-Respondents.

In the Matter of the Application of
THE NATIONAL ASSOCIATION OF INSURANCE AND FINANCIAL ADVISORS – NEW YORK STATE, INC., and DONALD DAMICK,

Plaintiffs-Respondents,

– against –

THE NEW YORK STATE DEPARTMENT OF FINANCIAL SERVICES and MARIA T. VULLO, in her official capacity as Superintendent of the New York State Department of Financial Services,

Defendants-Respondents.

BRIEF OF *AMICI CURIAE* AARP & AARP FOUNDATION IN SUPPORT OF RESPONDENTS-RESPONDENTS

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INTERESTS OF AMICI CURIAE

AARP is the nation's largest nonprofit, nonpartisan organization dedicated to empowering Americans 50 and older to choose how they live as they age. With nearly 38 million members and offices in every state, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands, AARP works to strengthen communities and advocate for what matters most to families, with a focus on financial stability, health security, and personal fulfillment. AARP's charitable affiliate, AARP Foundation, works to end senior poverty by helping vulnerable older adults build economic opportunity and social connectedness.

AARP's and AARP Foundation's efforts to increase the security and adequacy of older individuals' retirement savings include litigation and participation as amici curiae in state and federal courts. Amici participated in the litigation regarding the U.S. Department of Labor's 2016 Fiduciary Rule, seeking intervention in *Chamber of Commerce v. U.S. Department of Labor*, 885 F.3d 360 (5th Cir. 2018), and urge this Court to uphold the consumer and investor protections in the New York Department of Financial Services' Suitability and Best Interest Rule to level the playing field for older Americans. These individuals include approximately 2.5 million AARP members in New York, who deserve the best advice possible to assure their retirement security.

INTRODUCTION AND SUMMARY OF THE ARGUMENT

America today is in the throes of a full-blown retirement crisis. As of March 2019, twenty percent of American adults had no savings whatsoever. Amanda Dixon, *Survey: 21% of Working Americans Aren't Saving Anything at All*, BANKRATE (Mar. 14, 2019), https://bit.ly/33Ayj9g. Twenty percent of Americans save only five percent or less of their annual income, and less than a third save at least eleven percent of their annual income. *Id.* The pandemic has accelerated this crisis dramatically, decimating individual retirement accounts, pensions, and payments into the Social Security system. It is estimated that a staggering seventy-five percent of adults who have lost their jobs during the pandemic will not be able to retire securely—a twenty percent increase in only four months. *See* Alicia H. Munnell, Anqi Chen, & Wenliang Hou, Ctr. for Ret. Research at Bos. Coll., *How Widespread Unemployment Might Affect Retirement Security* 4 (2020), https://bit.ly/3khCqNo. These unprecedented circumstances only underscore why the New York Department of Financial Services' ("DFS") Suitability and Best Interest Rule (the "Rule") must be upheld.

As traditional pensions dwindle, Americans increasingly depend on non-traditional retirement vehicles like insurance products. Yet, the market for insurance products is complex, and insurance agents and brokers have a financial incentive to sell products that allow them to recoup a quick commission but may

not be beneficial for buyers. As the high lapse rate in the life insurance market demonstrates bad advice that benefits only sellers is more than a hypothetical possibility—it is a current market breakdown with disastrous consequences. The Suitability and Best Interest Rule provides an important tool for combatting this problem. By ensuring that insurance producers' recommendations are in consumers' best interests, the Rule both protects individuals and helps sustain the social safety net by preventing buyers from having to draw more heavily on public benefits to avoid poverty, saving New York alone billions of dollars over the next decade. William Shiflett & Catherine Harvey, AARP Pub. Policy Inst., *The US Could Save $33 Billion by Helping People Save for their Own Retirement* (2018), https://bit.ly/30uQgo1. And, now, after the Fifth Circuit's decision in *Chamber of Commerce*, 885 F.3d 360 (5th Cir. 2018), striking down the Department of Labor's 2016 Fiduciary Rule, states are the only entities able to provide this protection.

For these reasons, it is essential that the Court affirm the decision below upholding DFS' Suitability and Best Interest Rule.

ARGUMENT

I. New York's Suitability And Best Interest Rule Is Necessary To Protect Consumers, Who Increasingly Must Rely On The Recommendations Of Insurance Producers To Save For Retirement.

A. The Shifting Retirement Landscape Has Caused Consumers To Rely More Heavily On Financial Professionals, Including Insurance Producers, For Retirement Savings Recommendations.

Older Americans are retiring at record rates. As the Baby Boomer generation ages, approximately 10,000 individuals retire each day. Univ. of Mich. Health & Ret. Study, *Aging in the 21st Century: Challenges and Opportunities for Americans* 8 (2017). By 2030, twenty percent of the U.S. population will be of retirement age. *See id*. Additionally, due to improved life expectancy, individuals are now spending more time in retirement than ever before. Anne Obersteadt et al, Nat'l Ass'n of Ins. Comm'rs and the Ctr. for Ins. Policy & Research, *State of the Life Insurance Industry: Implications of Industry Trends* 53, 75 (2013), https://bit.ly/3i3jgJs (hereinafter "State of the Life Insurance Industry"). This increased longevity poses new challenges for many Americans, who must now amass enough savings to navigate a lengthy retirement.

These challenges have been exacerbated by the dramatic shift in how Americans prepare and save for retirement. Over the past several decades, the onus for retirement savings has shifted from the employer to the employee. In 1990, eighty-four percent of full-time workers employed by large and medium employers

were enrolled in defined benefit plans—i.e., traditional pension plans in which the employer guarantees the payment of a specific benefit in retirement. *Id.* at 50. By 2019, only twenty-six percent of all civilian workers had access to a defined benefit plan. U.S. Dep't of Labor, Bureau of Labor Statistics, Bulletin No. 2791, *National Compensation Survey: Employee Benefits In the United States,* March 2019 3 tbl.2 (2019), https://bit.ly/3greC7A.

While some employers now offer defined contribution plans—plans where employees contribute a fixed amount from their paychecks to an employer-sponsored retirement plan—a significant number of employers, particularly small businesses, offer no retirement savings plan whatsoever. *See generally* U.S. Gov't Accountability Office, GAO-13-748T, *Retirement Security, Challenges and Prospects for Employees of Small Businesses* (2013), https://bit.ly/3a28oJ8; Sarah Max, *Many Small Business Don't Offer Retirement Plans. Some States are Trying to Fix That*, Barron's: Retirement (Jan. 31, 2020), https://bit.ly/2Ptngqs. An estimated fifty-one to seventy-one percent of employees of small businesses lack access to even a defined contribution plan. U.S. Gov't Accountability Office, *supra* at 1. Indeed, 40 million American households with working-age adults do not have a traditional retirement account. Fed. Ins. Office, U.S. Dep't of the Treasury, *Report on Protection of Insurance Consumers and Access to Insurance* 36, (2016),

https://bit.ly/2C1wsiH (hereinafter "Report on Protection of Insurance Consumers and Access to Insurance.")

New York has not escaped the consequences of this crisis: as of 2015, fifty-two percent of New Yorkers employed in private sector positions worked for an employer who did not offer any retirement plan. David John & Gary Koenig, AARP Pub. Policy Inst., *Workplace Retirement Plans Will Help Workers Build Economic Security* 1 (Aug. 2015), https://bit.ly/2DF5kpT. Seventy-six percent of New Yorkers without a high school degree worked for employers who did not offer any retirement plans. *Id.*

In the absence of a defined-benefit plan or other employer-sponsored retirement plan, many Americans must themselves traverse a complicated landscape of financial products in order to adequately save for retirement. Among those products are life insurance and annuities, which are increasingly critical for obtaining financial security in retirement. Report on Protection of Insurance Consumers and Access to Insurance, *supra* at 36-38. These products can be particularly well-suited to insure against "longevity risk," or the risk that one will outlive their retirement cash-flow, because they guarantee future income streams. State of the Life Insurance Industry, *supra* at 3, 44-50. Indeed, nearly 75 million American families rely on life insurance products for financial security, and the annuity market is growing substantially. *Id.* at 74. In 2019, annuity sales reached

$241.7 billion—the highest rate in 11 years. LIMRA, *Secure Retirement Institute: 2019 Total Annuity Sales Reach Highest Level Since 2008* (Feb. 18, 2020), https://bit.ly/2DkXuSA.[1]

While life insurance and annuities can help ensure financial security in retirement, they are extremely complicated products. Consumers looking to purchase a life insurance policy or an annuity face a dizzying array of options. Life insurance can be term or permanent. *See Life Insurance FAQs*, Forbes, https://bit.ly/3icfqh7 (last visited Aug. 4, 2020). Permanent life insurance can be universal or whole. *Id*. Universal life insurance can be fixed, variable, or indexed. *Id*. Annuities can be immediate or deferred. *See What Are the Different Types of Annuities?*, AnnuityFYI, https://bit.ly/31maAqH (last visited Aug. 4, 2020). Deferred annuities can be multi-year guarantee annuities, deferred income, indexed, or variable. *See id.* Various iterations of each product are available, each with its own advantages and disadvantages for individuals in any given set of circumstances.

Faced with this complex web of products, consumers must increasingly rely on the recommendations of insurance agents and brokers. See U.S. Dep't of Labor,

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[1] In recent months, the market for annuities has declined as a direct result of the Covid-19 pandemic. However, forecasters project that the market will rebound as the pandemic eases. *See* LIMRA, *Secure Retirement Institute Forecasts Rebound for Most Annuity Products by 2021* (June 17, 2020), https://bit.ly/3gzgGdG.

Regulating Advice Markets: Definition of the Term "Fiduciary" Conflicts of Interest - Retirement Investment Advice Regulatory Impact Analysis For Final Rule and Exemptions 3 (2016), https://bit.ly/3guAX4k (hereinafter DOL 2016 Fiduciary Rule Administrative Record). Older adults—and especially women, lower-income older adults, and minority older adults—rely on this advice even more heavily than the general population because they more frequently have limited financial literacy. *See generally*, Annamaria Lusardi et al., *Financial Literacy and Financial Sophistication in the Older Population*, 13 J. Pension Econ. & Fin. 347 (2014), https://bit.ly/3kb6OcB. As reliance on insurance producers intensifies, the need for consumer protections, like those found in the Suitability and Best Interest Rule, are increasingly necessary.

B. The Suitability And Best Interests Rule Is Necessary Because Producers Have An Incentive To Act In Their Own Interest, Rather Than The Best Interest of Consumers.

While consumers increasingly rely on insurance producers for product recommendations, the insurance industry incentivizes producers to sell products that may not be in a consumer's best interest but allow the producer to recoup large commissions. Producers receive lucrative payouts for the sale of a life insurance or annuity products. In New York, producers can, under certain circumstances, recoup up to 99% of the first-year premium payment for life insurance products and up to 8.5% of the deposit amount on an annuity. *See* N.Y. Ins. Law § 4228(5)

(McKinney 2002). Because the initial sale generates a large commission for the producers, they have an incentive to steer consumers towards pricier products. Moreover, the insurance producer recoups the majority of the commission within the first four years of a sale, giving producers little impetus to ensure that a recommended product is a lifelong fit for a consumer. *See* J.A. at 682.

As a result, producers often recommend products that may ensure a return for the producer but are ultimately unsuitable for the consumer. The high lapse rates for insurance products is one indicator of the negative impacts of these conflicted recommendations. Lapse rates track the percentage of insurance policies that terminate due to non-payment of a premium. Lapse rates are indicative of the suitability of insurance recommendations, with lower lapse rates indicating products are generally suitable for consumers, and higher lapse rates indicating higher proportions of unsuitable recommendations. High lapse rates may indicate that a product was either too pricey for the consumer or of inappropriate duration. A recent study by the Society of Actuaries and LIMRA International found that within five years, one-third of individual life insurance policies lapsed. Within ten years, just under one-half of all policies lapsed. *See* Cathy Ho & Nancy S. Muise, *U.S. Individual Life Insurance Persistency: A Joint Study Sponsored by Society of Actuaries and LIMRA* 13 (2012), https://bit.ly/3ftHw5B. Lapse rates have a particularly pernicious impact on older adults, who forfeit $112 billion annually in

lapsed or surrendered life insurance policies. Life Ins. Settlement Ass'n, *American Seniors Forfeit $112 Billion Annually Due to Lapsed or Surrendered Insurance Policies, According to Research Presented at* LISA Institutional Investor Conference, Global Newswire (Feb. 24, 2015 9:11 EST), https://bit.ly/33uXxWE. And, while consumers can reinstate lapsed policies, it often comes at a cost. Reinstating lapsed coverage generally requires new underwriting, which can substantially increase premiums if the consumer has aged or has new health conditions. Allen Wastler, *How Lapses in Life Insurance Policies Hurt You*, MassMutual: Blog (Nov. 19, 2019), https://bit.ly/33tyZ0h.

C. Individuals' Lack of Retirement Security In The Modern Market Threatens The Stability Of The Social Safety Net.

In addition to helping individuals with retirement security, regulations like the Suitability and Best Interest Rule are a key component in avoiding disastrous economic consequences to states themselves, as well as the federal government. Traditionally, Americans expected to rely on a "three-legged stool" for retirement security: pensions, personal savings, and Social Security. Barclay Palmer, *What is the Three-Legged Stool?*, Investopedia (Oct. 28, 2019), https://bit.ly/3fCPmu4. When individuals without pensions—that is, most people—also have insufficient retirement savings from investment in insurance products and other assets, they have no choice but to lean heavily on public benefits. Indeed, lower- and middle-income retirees have long depended on public benefits for the majority of their

incomes. Elizabeth Bell, Adam Carasso, & C. Eugene Steuerle, Urban Inst., *Strengthening Sources of Retirement Savings for Low-Income Families* 1 (2005) https://urbn.is/30spah8. A recent study showed that 40.2% of older Americans rely *solely* on Social Security, putting tremendous pressure on the retirement security stool's remaining leg and putting it at risk of breaking. Press Release, *Nat'l Inst. on Ret. Sec., New Report: 40% of Older Americans Rely Solely on Social Security for Retirement Income* (Jan. 13, 2020), https://bit.ly/31fr43O. Helping low-income retirees save enough to increase their retirement income by even $1,000 per year would save public benefits $33 billion nationwide, and $4 billion in New York alone, by 2032. Shiflett & Harvey, *supra*.

DFS proposed the Suitability and Best Interest Rule with this precarious landscape in mind. The Rule effectively levels the playing field for consumers and producers by requiring producers to take affirmative steps and collect certain information to ensure that a recommendation is in the best interest of the consumer. While producers are still free to recoup commissions, they can no longer do so to the detriment of the consumer. The Rule makes sense because anything short of requiring affirmative steps to ensure a recommendation is in the best interest of a consumer would likely be inadequate. Rules requiring mere disclosure of conflicts of interest with no duty of care, for example, have largely been found ineffective at mitigating conflicts, and often leave consumers even

more confused. DOL 2016 Fiduciary Rule Administrative Record, *supra* at 9. Accordingly, a strong rule, like the Suitability and Best Interest Rule, is necessary to protect consumers and safeguard their retirement savings in an increasingly complex financial market, and to help stabilize the public benefits system in New York and throughout the United States.

II. State Action Offers the Most Effective Means To Protect Consumers From Conflicted Advice That Can Destroy Their Retirement Security.

Appellants contend that the Suitability and Best Interest Rule exceeds DFS's authority, in part, based on the Fifth Circuit's decision in *Chamber of Commerce*, 885 F.3d at 376; Appellant Br. 4, 49-50. They argue that the Rule's use of a uniform "best interest" standard creates a fiduciary relationship, which the Fifth Circuit held inapplicable to insurance agents and brokers under a common law standard—a standard, the court said, that ERISA codified. *See id.* at 49.

As a preliminary matter, the Suitability and Best Interest Rule strikes a very different balance than DOL's Fiduciary Rule did. Unlike the DOL's 2016 Fiduciary Rule, the Rule does not define insurance agents and brokers as fiduciaries or create a fiduciary relationship. *See Indep. Ins. Agents & Brokers of N.Y.*, 109 N.Y.S.3d 574, 591 (N.Y. Sup. Ct. 2019) ("Merely because the Amendment requires a producer to recommend to the consumer product which best first the consumer's insurance needs does not impose a 'special relationship' from which liability for fraud or tort can arise . . . [i]t does not necessary entail a

relationship of trust[.]”). In fact, the Suitability and Best Interest Rule helps alleviate confusion by prohibiting non-fiduciary producers from calling themselves “advisors” precisely *because* only advisors have fiduciary duties outside the contractual relationship. *Id.* at 591-92. The Suitability and Best Interest Rule thus creates crucial consumer protections in a very different way than did the former DOL Rule.

More to the point, state protections like the Suitability and Best Interest Rule are both permissible and necessary. As the lower court explained, while foreclosing the DOL from going beyond the common law to protect consumers because of ERISA’s purported boundaries, the *Chamber of Commerce* decision expressly left open the possibility that states could enact appropriate regulations. 109 N.Y.S.3d 574 (citing *Chamber of Commerce*, 885 F.3d 360). The Fifth Circuit explained that its decision did not forbid “other appropriate federal *or state* regulators to act” to protect consumers in financial advisory transactions. *Id.* (emphasis added).

The need for state action is becoming increasingly apparent as federal agencies adopt rules granting lesser protections than those offered by New York. For example, while the Securities and Exchange Commission recently promulgated Regulation Best Interest and attendant guidance, those regulations and guidance rely primarily on disclosure rather than requiring financial professionals to take

affirmative steps to protect the consumer's best interest. *See generally* Regulation Best Interest: The Broker-Dealer Standard of Conduct, 84 Fed. Reg. 33318 (July 12, 2019) (to be codified 17 C.F.R. 24). The SEC rules and guidance also leave blurry lines between salespeople and advisors who are genuinely fiduciaries. *Id.* Likewise, the Department of Labor's new proposed Prohibited Transaction Exemption makes no attempt to protect consumers within the bounds of the Fifth Circuit's decision, relying solely on disclosure and self-regulation. *See* Improving Investment Advice for Workers & Retirees, 85 Fed. Reg. 40834 (July 7, 2020) (to be codified 29 C.F.R. 2550).

Consequently, states are now in the best position to protect consumers from the confusing, misleading, and fraudulent advice pervading a market that incentivizes producers to act in their own best interest, rather than that of the consumer. Fortunately, states are well-positioned to address the unique needs of the market and consumers in their respective jurisdictions, using their expertise to select the approach that best ameliorates the problems they face. New York, the financial and commercial hub of the United States, has appropriately taken a strong protective approach that, while not going as far as the 2016 Fiduciary Rule, significantly improves consumer protections in the insurance market and helps purchasers achieve financial security in retirement.

CONCLUSION

For the forgoing reasons, the Court should affirm the decision below dismissing the Complaints.

August 10, 2020

Respectfully submitted,

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Pursuant to the Uniform Practice Rules of the Appellate Division (22 N.Y.C.R.R.) § 1250.8(j), the foregoing brief was prepared on a computer using Microsoft Word. A proportionally spaced, serif typeface was used, as follows:

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August 10, 2020

/s/ Ali Naini
Ali Naini