

Suitability and Disclosure Developments in Annuity Sales in Texas¹

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Regulators and Legislators have recently been focusing on the burgeoning sales in annuities, focusing on whether high commissions, rather than investor suitability, drive sales. This has resulted in recent major developments in Texas and nationally. First, the SEC recently approved FINRA's (formerly the NASD) new rules relating to variable annuity suitability and the supervision of variable annuity sales. Second, a recent statute passed by the Texas Legislature effective January 1, 2008 applies suitability requirements to all individually recommended annuity sales and requires specific disclosures in annuity sales.

But first, some background is needed. A fixed annuity pays out a defined return on investment for an indefinite period, usually the life of the insured and is not based on the performance of any investments. A variable annuity pays a return on investment based on the performance of subaccounts managed by investment advisers and has multiple other features and benefits. An equity-indexed annuity pays a defined return on investment, but may provide a limited upside based on the performance of an investment index. It has no subaccounts and no selected investments. Variable and equity-indexed annuities are complex contracts that typically require long holding periods for liquidation without penalties. They can also carry higher costs and higher commissions than other investments. Annuities carry tax deferral benefits.

According to the Insurance Information Institute, in 2006 insurers sold \$160.6 billion of variable annuities and \$75.6 billion of fixed annuities. Variable annuities now hold almost \$1.4 trillion in assets. Since 2002 variable annuity sales are up 37.74% and fixed annuity sales are down 26.82%. Equity-indexed annuities have also been growing. In 2006, the ten largest producers of this product sold almost \$21 billion of equity-indexed annuities.

The regulation of the sale of annuities may fall into both securities and insurance regulatory regimes, which are vastly different. Securities regulatory regimes traditionally have imposed investor suitability requirements over the distribution channel and insurance regulatory regimes generally have not had suitability requirements. Further, under federal law, variable annuity sales have fallen under securities regulation while fixed annuity sales have fallen under state insurance regulators. Finally, arguments persist about the appropriate regulatory regime for equity-indexed annuities, and the SEC has not made a final decision about its general jurisdiction over the sale of equity-indexed annuities. First, FINRA asked the SEC to evaluate whether equity-indexed annuities are securities. Second, SEC Rule 151 may provide a safe harbor from

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securities registration for the sale of equity-indexed annuities. That rule exempts from securities regulation those annuities that are 1) registered with a state insurance administrator; 2) have the insurer assume the investment risk; and 3) not primarily marketed as investments. Third, at least one court has ruled that equity-indexed annuities are not securities (*Malone v. Addison Insurance Marketing, Inc., et al.* 225 F. Supp. 743 (W.D.Ky 2002)). Finally, equity-indexed annuities sold by a registered securities broker-dealer would still be subject to suitability evaluations under broker-dealer rules.

One particular suitability concern for annuities involves switching, in which a salesman switches the customer's annuity, gets another large commission, and may cause the customer to pay early liquidation penalties. A second suitability concern involves placing annuities in tax-deferred accounts such as individual retirement accounts. In that case, the annuity's tax deferral benefit would generally be meaningless. Other suitability concerns involve carrying costs, holding periods, and allocations in variable annuity subaccounts.

For Texas brokers, 2 major developments in annuity sales have recently occurred. First, after three years of gestation, the SEC has approved FINRA's new sales and supervisory rules for the sale of variable annuities. These rules will be effective August 4, 2008. Second, last session the Texas Legislature for the first time passed suitability rules for all annuity sales. Those laws are effective January 1, 2007.

FINRA's New Annuity Sales and Supervision Rules

FINRA's new variable annuity sales rule, Rule 2821, goes into effect on August 4, 2008. Rule 2821 has multiple provisions. It will create new suitability obligations, principal review and approval requirements, and supervisory and training requirements tailored specifically to variable annuity transactions that will be in addition to other NASD general rules on these topics.

Rule 2821 applies to the purchase or exchange of variable annuities and the customer's initial subaccount allocations. It will not generally apply to reallocations or subsequent premium payments, or when the purchase or exchange occurs within a tax-qualified employer-sponsored retirement or benefit plan. But, Rule 2821 will apply if a broker recommends a variable annuity to an individual plan participant.

Rule 2821 will require that a broker have a reasonable basis to believe that the transaction is suitable for the customer in order to recommend a variable annuity purchase or exchange. It will also require principal review and approval before transmitting to the insurer within seven business days of the sale, and require training specifically tailored to variable annuity sales. Finally, the SEC made a technical change to the Net Capital Rule, Rule 15c3-1 which states that during the time the broker-dealer is holding a customer check for a variable annuity purchase pending principal approval and transmission, it will not be deemed to be holding customer funds for the purpose of the net capital rule.

The rule will require that broker-dealers generate a great amount of paperwork for each variable annuity sale and the detailed list of suitability review requirements will provide fodder

for claimant attorneys in arbitrations. The broker-dealer and the insurer will undoubtedly require that all the required information be thoroughly documented and it will likely take many pages. Also, broker-dealers will need to provide extensive training to their sales force to make sure that brokers understand the new rule and the broker-dealers procedures used to comply with the rule.

Rule 2821 is an add-on suitability determination rule. The general suitability requirements of Rule 2310 still apply.

Rule 2821 Broker Requirements

First, Rule 2821 requires that brokers make reasonable efforts to obtain, at a minimum, the following information from the prospective customer before recommending a variable annuity:

- Age;
- Annual Income;
- Financial Situation and Needs;
- Investment experience;
- Investment objectives;
- Intended use of the variable annuity;
- Investment time horizon;
- Existing assets (including investment and life insurance holdings);
- Liquidity needs;
- Liquid net worth;
- Risk Tolerance;
- Tax status; and
- Such other information reasonably used or considered in recommending annuities to customers.

Because brokers will need to be able to demonstrate, often years later, to principals, FINRA and SEC examiners, and arbitration panels that there was a reasonable basis for the recommendation, brokers will need to obtain this information in writing and in great detail. Some of these items may include checking boxes, but other items, such as existing assets, use of a variable annuity, and liquidity needs will likely need more detailed written explanation. Also, there is a new provision of the Texas Insurance Code (further explained below) which will require that the broker obtain a detailed list of all of the customers' other life insurance policies and annuities.

What does "reasonable efforts" mean? It means get it in writing. Principals and compliance departments face personal supervisory liability from FINRA for approving annuity sales and are unlikely to sign off on these sales based on assertion that the customer did not want to provide the requested information but still wanted to purchase an annuity.

Once this required information has been obtained, the broker must start making disclosures about the recommended product. Under Rule 2821 the broker and the broker-dealer

must have a reasonable basis to believe that the customer has been informed, in general terms, of variable annuities various features, including:

- Potential surrender period;
- Potential surrender charge;
- Potential tax penalty if customers sell or redeem variable annuities before reaching age 59 ½;
- Mortality and expense fees;
- Investment advisory fees;
- Potential charges for and features of riders;
- The insurance and investment components of variable annuities; and
- Market risks.

This disclosure requirement combines both general annuity issues and items that are variable depending on the particular annuity recommended. This means that broker-dealers should create their own general annuity features disclosure document and also provide the insurer's disclosure summary. The broker will also need to be able to document that these disclosures were actually delivered with time enough for the customer to review. There will be a recital of these disclosure agreements signed by the customers, but it may also be wise to provide a copy of these disclosures during the initial meeting when the customer information is gathered. Broker dealers should also expect SEC and FINRA examiners to focus on policies and proof relating to delivery of these required variable annuity disclosures.

After gathering information and providing disclosure, the broker is only one step away from being able to recommend a variable annuity. But, it is a big step. The broker must run all the customer's needs and the features of the various products through the suitability prism using a detailed list of factors provided by Rule 2821. The general suitability requirements of Rule 2310 also remain in effect. Rule 2821 requires the broker to evaluate if the customer would benefit from at least some of the annuity features, including:

- tax deferred growth;
- annuitization; or
- a death or living benefit.

The reference to tax deferred growth means that brokers should be cautious about recommending variable annuities for qualified accounts.

The next step in the suitability determination is to review the subaccount allocations, riders, and product enhancements to determine if all of these items are consistent with the customers needs as stated in the information gathered from the customer.

Finally, variable annuity exchanges have additional requirements and will be a hot button item for regulators and claimant arbitration attorneys for the next several years. If the transaction is an annuity exchange, the suitability determination will take into consideration whether:

- The customer would incur a surrender charge;
- The customer would be subject to commencing a new surrender period;
- The customer would lose existing benefits, such as mortality and expense fees, or charges for riders and similar product enhancements;
- The customer would benefit from the product enhancements and improvements; and
- The customer's account had another variable annuity exchange within the preceding 36 months.

If there was another variable annuity exchange within the previous 3 years, FINRA and SEC examiners will undoubtedly view those transactions as red flags and seek excruciatingly exact details about them. As is standard at many firms today, from a compliance perspective exchanges will require a written acknowledgement of these issues by the customer. Detailed broker notes about the various discussions of these issues will also be a crucial part of the record.

Rule 2821 Principal Requirements

So, after going through all these requirements, the broker finally hands the transaction off to his or her principal. Rule 2821 now requires a principal to review and approve the transaction before sending the variable annuity paperwork to the insurer for processing no later than seven business days after the customer signs the application. In December 2007 FINRA announced that it is reconsidering the required timing of the principal review, so annuity principal review time limits have yet to be finally determined. Rule 2821 also requires that the principal only approve the transaction "if there is a reasonable basis that the transaction would be suitable based on the factors" listed above. This standard appears to require that the principal conduct a new suitability review for the customer and not just a review of the broker's suitability analysis. Rule 2821 places principals squarely in the line of fire. Reliance on what the broker told them does not appear to be much of a mitigating factor if the variable annuity was subsequently determined to be unsuitable. Rule 2821 also requires that the principals sign their approvals or disapprovals and that the broker-dealer document these reviews.

If the principal disapproves the transaction, Rule 2821 allows for the customer to be informed of the reason for disapproval. If the fully-informed customer still wants to pursue the variable annuity transaction despite being educated about the reasons for principal disapproval and affirms that to the principal, the principal may authorize the processing of the transaction as a not recommended transaction.

Rule 2821 Broker-Dealer Supervisory Requirements

Rule 2821 requires that broker-dealers have supervisory procedures specific to the rule beyond the general supervisory procedures required by Rules 3010, 3012, 3013, and 3110. First, Rule 2821 requires a special statistical review of variable annuity exchanges by broker. Broker-dealers will be required to implement systems where exchanges can be easily tracked by

broker, and probably by office code. The rule requires broker-dealers to have “surveillance procedures” to discover if each of its brokers have levels or frequencies of variable annuity exchanges that “raise for review whether such rates of exchanges evidence conduct inconsistent with the applicable provisions of this Rule, other applicable rules, or of the federal laws.” Second, Rule 2821 requires broker-dealers that their policies and procedures to include corrective measures to address inappropriate exchanges and broker conduct in connection with those inappropriate exchanges.

Finally, Rule 2821 requires that broker-dealers “develop and document specific training policies and programs” for the brokers and principals involved in recommending and approving variable annuity transactions to comply with this rule. Fundamentally this means that broker-dealers should provide mandatory training to these persons on Rule 2821 and its new suitability requirements and procedures before the effective date of the Rule on August 4, 2008. If the broker or principal does not complete that training by August 4, 2008, then the broker-dealer should bar the broker or principal from engaging in or approving variable annuity transactions until they have completed the training.

Exception to Net Capital and Prompt Transmittal Rules

The seven-day principal review period in Rule 2821 caused the NASD and SEC to provide exceptions to several other rules. NASD Rule 2330 prohibits improper use of customer funds and NASD Rule 2820 requires the prompt transmittal of the variable annuity application and purchase payment. Consequently, Rule 2821 creates an exception to these rules. A broker-dealer may now hold an variable annuity application and a non-negotiated customer check for up to seven business days while completing its Rule 2821 review without violating Rule 2330’s use of customer funds requirements or Rule 2820’s prompt transmittal requirement. Because FINRA is reconsidering the seven-day period in Rule 2821, the details may change in the future.

The SEC also amended the net capital rule, Rule 15c3-1 for those broker-dealers who do not carry customer funds or securities (i.e. those firms with less than a \$250,000 mandatory net capital.) Rules 15c3-1 and 15c3-3 provides that a firm need not create a customer reserve account if it “promptly transmits” checks or securities to third parties which means that the transmission or delivery of the check needs to be made by noon of the next business day after the receipt of those funds or securities. The SEC has amended its rules to exempt Rule 2821’s principal review period from its “promptly transmits” requirements. The SEC has required that the broker-dealer transmit the check no later than noon of the day following the date that the registered principal completed the review of the variable annuity transaction. The broker-dealer must also keep copies of the check and record the date the check was received and when it was transmitted to the insurance company or returned to the customer.

Suitability, Disclosure and Recordkeeping for Annuity and Life Insurance Switches Under New Texas Statutes

Under Texas state law all annuities have been governed by the Texas Department of Insurance. The Texas Securities Act specifically excludes registered annuity contracts, thus depriving the Texas Securities Commissioner and courts enforcing the Texas Securities Act from direct authority over annuities. Section 4.A of the Texas Securities Act specifically excludes from the definition of “security:” “any . . . annuity contract . . . issued by an insurance company subject to the supervision or control of the Texas Department of Insurance when the form of such policy or contract has been duly filed with the Department.”

Last session the Texas Legislature passed two bills impacting the sale of annuity contracts and required suitability in annuity sales for the first time. These bills gave enforcement duties to the Texas Department of Insurance and did not provide private causes of action.

Annuity Suitability – HB 2761

First, HB 2761 creates a suitability requirement in the sale of annuities made after January 1, 2008. It adds Chapter 1115 to the Texas Insurance Code and applies to agent-recommended fixed, variable, and equity-indexed annuities, provided that the annuity was individually solicited. The chapter’s applicability does not depend on whether the annuity was a group or individual annuity. *Texas Insurance Code §§1115.002(2) and 1115.003(a)*. Chapter 1115 exempts advertisements and other direct responses if no information was collected from the customer, contracts used to fund employee benefit or welfare plans covered by ERISA, 401(k) and similar plans, and government and church plans, nonqualified deferred compensation arrangements by the employer or plan sponsor, litigation or claim settlements, and prepaid funeral benefits. *Texas Insurance Code §1115.003(b)*.

Chapter 1115 requires that before executing a recommended annuity purchase, the agent (or the insurer in a direct sale) must make reasonable efforts to obtain the purchaser’s financial status, tax status, investment objectives, and other relevant information. Then the annuity recommended by the agent (or the insurer in a direct sale) must have “reasonable grounds for believing that the recommendation is suitable” for that purchaser based on the purchaser’s other insurance, their investments, and financial situation and needs. *Texas Insurance Code §§1115.051(a) and (b)*. The “reasonable grounds” standard is based on the agent’s (or insurer’s if direct sold) actual knowledge at the time of the recommendation. *Texas Insurance Code §1115.051(d)*. The agent (or the insurer if direct sold) is absolved from responsibility if the purchaser refused to provide the relevant information, provided incomplete or inaccurate information, or entered into a non-recommended annuity transaction. *Texas Insurance Code §§1115.051(c)*. Finally, compliance with FINRA suitability rules will meet Chapter 1115’s requirements for variable annuity recommendations. *Texas Insurance Code §1115.054*. But, compliance with FINRA record-keeping requirements does not necessarily fulfill the Chapter 1115’s record-keeping requirements.

The actual knowledge and reasonable basis provisions will mean that compliance will be process-driven. The gathering of information and the reasonable basis for the recommendation will need to be well-documented. In light of this, Chapter 1115 also requires maintaining a detailed compliance system in connection with recommended annuity sales, including written procedures and periodic reviews of the agents' and insurers' records to detect patterns indicating unsuitable annuity sales. *Texas Insurance Code §§1115.052(a) through (c)*. Agents and insurers may contract with third parties to establish and maintain the compliance system, but must reasonably inquire as to whether the third party is fulfilling its duties and take reasonable actions to enforce the third party's contractual compliance duties. These reasonable inquiries requirement can be fulfilled by an annual certification or periodically selecting other third parties to review the first third party's compliance work. *Texas Insurance Code §1115.052(d)*. The review procedures shall be "reasonable under the circumstances" and do not require the review of all agent-solicited transactions or the extension of these compliance controls beyond recommendations of annuity products. *Texas Insurance Code §§1115.052(e) and (f)*. Insurers can request compliance certifications from their agents. *Texas Insurance Code §1115.053*.

Chapter 1115 requires that agents and insurers maintain records of annuity recommendations and the information used as the basis for the recommendations for five years. *Texas Insurance Code §1115.055*.

Chapter 1115 specifically states that it shall not be construed to create a private cause of action. It can only be enforced by the Texas Department of Insurance which can impose administrative sanctions and penalties and require that insurers and agents take specific corrective actions. *Texas Insurance Code §§1115.101 and 1115.102*. Although there is no private right of action, other states that previously adopted annuity suitability requirements have been aggressive in enforcing these provisions. Minnesota, particularly, has established a track record of annuity suitability actions under insurance law:

- Pacific Life Insurance Company - \$950,000 penalty - April 2005;
- Consec Insurance - \$2.5 million penalty – April 2006;
- Met Life Investors USA Insurance Company - \$250,000 – December 2006; and
- American Investors Life Insurance Company - \$1.4 million – August 2007.

Although Chapter 1115 authorizes no private right of action, the new recordkeeping requirements for the sale of each recommended annuity may provide fodder for litigators seeking other insurance-related causes of action, including damages actions for "an unfair or deceptive act or practice in the business of insurance." *Texas Insurance Code §541.151*.

Annuity Disclosures – HB 2762

Second, HB 2762 adds Chapter 1114 to the Texas Insurance Code. Chapter 1114 generally provides that insurance agents and companies produce detailed compliance and disclosure paperwork to customers considering paying for a new annuity or life insurance policy with financing or proceeds from a previous annuity or life insurance policy. These switching transactions have been a special concern for regulators.

Chapter 1114 is a detailed disclosure-based, not a suitability-based regime. It provides that agents must submit a statement signed by both the agent and the applicant as to whether the proposed insured has existing policies or contracts as part of the application for a new life insurance policy or annuity. If the applicant states that there are existing policies or contracts, the agent must present the applicant with a required notice approved by the Insurance Commissioner that lists all the life insurance policies and annuities the applicant proposes replacing, the name of the insured or annuitant, and whether that policy will be used as a financing source for the new policy or contract. The applicant and agent both must sign the notice and attest that the notice was read aloud to the applicant or the applicant waived reading. The notice must be left with the applicant. If the notice is presented to the applicant via the Internet, the insurer must mail the applicant a copy of the notice within three business days of receiving the application. The agent must also leave with the applicant all sales materials used in presenting the new life insurance policy or annuity. *Texas Insurance Code §1114.051*.

On December 27, 2007, the Texas Insurance Commissioner issued new rules mandating that that an insurance customer be read or waive reading a notice about replacing annuities or life insurance policies. *28 TX Admin Code §3.9504*. The Commissioner also issued a mandatory notice for direct response consumer notices. *28 TX Admin Code §3.9505*. Any variations from these notices must be pre-approved by the Texas Department of Insurance. *28 TX Admin Code §3.9506*. These mandatory notices must be in at least 10 point font and are attached at the end of this article.

Chapter 1114 also imposes duties on insurance companies selling the replacement policy or annuity. The selling insurer must:

- Tell its agents about the Chapter 1114 notice and disclosure requirements and incorporate these requirements into all relevant training manuals;
- Provide each agent with a written statement on the whether and under what circumstances it will accept applications for replacement policies;
- Review the “appropriateness” of each replacement policy;
- Implement procedures to ensure that the insurer meets these provisions;
- Implement procedures to detect replacement transactions involving policies or annuities issued by that insurer in considering new applications, regardless of whether the agent or applicant has disclosed the existence of that previous policy. *Texas Insurance Code §1114.052(a) – (c)*; and
- Provide notice of the proposed replacement to the original life insurer. *Texas Insurance Code 1114.053(c)*.

The Texas Department of Insurance has yet to issue regulations defining terms such as “appropriateness.” But, that term may lead to something similar to a suitability review requirement. However, the statute provides a large loophole to the “appropriateness” determination. If the agent tells the insurer that the replacement transaction is consistent with the insurer’s written statement on the circumstances under which it will accept applications for replacement policies, then the insurer need not review the “appropriateness” of the transaction.

The statute appears to say that the insurer can rely entirely upon the agent's representation. But, the Texas Department of Insurance may require something more than taking the agent's blanket representation at face value.

Chapter 1114 also requires insurers to generally monitor their agents' sales of life insurance policies and annuities and be able to produce records detailing:

- Each agent's life insurance replacements, including financed purchases, as a percentage of the agent's total annual life insurance sales;
- Each agent's number of policy lapses by the agent as a percentage of the agent's total annual life insurance sales;
- Each agent's annuity replacements, including financed purchases, as a percentage of the agent's total annual annuity contract sales;
- Number of transactions that are unreported replacements of existing life insurance policies or annuity contracts detected by the insurer's required monitoring system; and
- Replacement life insurance policies and annuities indexed by agent and previous insurer.

Chapter 1114 requires that insurers maintain these records for at least five years. *Texas Insurance Code §1114.052(d)*. The new statute also requires that insurers "ascertain" that the sales materials and illustrations used in replacement life insurance policy and annuity sales are "complete and accurate for the proposed policy or contract" and that the insurer maintain these records for five years. *Texas Insurance Code §1114.052(g) and (h)*. The insurer has some further compliance requirements for customers who come from "direct response solicitations" which include endorsers or sponsors and all forms of advertising. *Texas Insurance Code §§1114.002(2) and 1114.055*.

Finally, Chapter 1114 imposes certain duties on the insurers who issued the policies or annuities being replaced. Upon receipt of a notice of replacement by the insurer issuing the replacement life insurance policy or annuity, the previous insurer must provide a notice to the policy or contract owner about the owner's right to receive information about the existing policy and contract values. The notice must include an in force illustration or a policy summary. *Texas Insurance Code §1114.054(c)*. The previous insurer must also provide the customer with a notice stating that "the release of policy values may affect the guaranteed elements, nonguaranteed elements, face amount, or surrender value of the policy from which the values are released." *Texas Insurance Code §1114.054(d)*. These previous insurers must also preserve for five years all received replacement notifications received from the insurers issuing the replacement life insurance policies or annuities. *Texas Insurance Code §1114.054(b)*.

Chapter 1114 provides that the failure of insurers and agents to comply with its provisions "constitutes a violation of Chapter 541 and is subject to sanctions and penalties as provided by that chapter." *Texas Insurance Code §1114.101(a)*. Note that this language omits the word "damages." Chapter 541 of the Texas Insurance Code provides that the Texas Department of Insurance can bring administrative actions for violations of the Texas Insurance

Code's provisions that can lead to sanctions and penalties. It also provides for a private cause of action for "damages." *Texas Insurance Code §541.151*. This means that the Chapter 1114 does not create any claims for general damages by reference to Chapter 541. But, in litigation a plaintiff's attorney could well argue an insurer's failure to comply with Chapter 1114's notice requirements is generally indicative of an "unfair method of competition or an unfair or deceptive act or practice in the business of insurance." *Texas Insurance Code §541.151*.

Chapter 1114 also provided that "if it is determined that the requirements of this chapter have not been met," the insurer issuing the new life insurance policy or annuity shall provide the policy owner an in force illustration, policy summary, or available disclosure document and the required notice regarding replacements. *Texas Insurance Code §1114.001(c)*. The statute did not say who was required to make that determination. In any event, the only remedy provided for that violation to the policy owner is the requirement that the policy owner receive the required disclosures and notice.

The Texas Department of Insurance may seek extensive administrative remedies for violations of Chapter 1114. In addition to the penalty and sanction provisions of Chapter 541, the Texas Department of Insurance can seek to revoke or suspend an agent's license or certificate of authority and forfeit commissions or other compensation paid to an agent. *Texas Insurance Code §1114.102(a)*. Violations that were material to the sale may also lead to an order requiring payment of restitution, restoration of the policy or contract values, and interest payments. *Texas Insurance Code §1114.102(b)*.

In connection with both recommended annuities and life insurance policy and annuity switches, it should be noted that if these activities are done by a FINRA-registered broker-dealer, the purchaser may have claims to enforce under FINRA suitability rules applicable to the broker-dealer and these new record-keeping requirements could provide ammunition for such claims.

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Texas Required Notice for Life Insurance or Annuity Replacements

IMPORTANT NOTICE: REPLACEMENT OF LIFE INSURANCE OR ANNUITIES

This document must be signed by the applicant and the producer, if there is one, and a copy left with the applicant.

You are contemplating the purchase of a life insurance policy or annuity contract. In some cases this purchase may involve discontinuing or changing an existing policy or contract. If so, a replacement is occurring. Financed purchases are also considered replacements.

A replacement occurs when a new policy or contract is purchased and, in connection with the sale, you discontinue making premium payments on the existing policy or contract, or an existing policy or contract is surrendered, forfeited, assigned to the replacing insurer, or otherwise terminated or used in a financed purchase.

A financed purchase occurs when the purchase of a new life insurance policy involves the use of funds obtained by the withdrawal or surrender of or by borrowing some or all of the policy values, including accumulated dividends, of an existing policy to pay all or part of any premium or payment due on the new policy. A financed purchase is a replacement.

You should carefully consider whether a replacement is in your best interests. You will pay acquisition costs and there may be surrender costs deducted from your policy or contract. You may be able to make changes to your existing policy or contract to meet your insurance needs at less cost. A financed purchase will reduce the value of your existing policy and may reduce the amount paid upon the death of the insured.

We want you to understand the effects of replacements before you make your purchase decision and ask that you answer the following questions and consider the questions on the back of this form.

1. Are you considering discontinuing making premium payments, surrendering, forfeiting, assigning to the insurer, or otherwise terminating your existing policy or contract?
 YES NO

2. Are you considering using funds from your existing policies or contracts to pay premiums due on the new policy or contract? YES NO

If you answered "yes" to either of the above questions, list each existing policy or contract you are contemplating replacing (include the name of the insurer, the insured or annuitant, and the policy or contract number if available) and whether each policy or contract will be replaced or used as a source of financing:

INSURER NAME	CONTRACT OR POLICY #	INSURED OR ANNUITANT	REPLACED (R) OR FINANCING (F)
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- 1.
- 2.
- 3.

Make sure you know the facts. Contact your existing company or its agent for information about the old policy or contract. If you request one, an in force illustration, policy summary or available disclosure documents must be sent to you by the existing insurer. Ask for and retain all sales material used by the agent in the sales presentation. Be sure that you are making an informed decision.

The existing policy or contract is being replaced because

I certify that the responses herein are, to the best of my knowledge, accurate:

Applicant's Signature and Printed Name Date

Producer's Signature and Printed Name Date

I do not want this notice read aloud to me. ____ (Applicants must initial only if they do not want the notice read aloud.)

A replacement may not be in your best interest, or your decision could be a good one. You should make a careful comparison of the costs and benefits of your existing policy or contract and the proposed policy or contract. One way to do this is to ask the company or agent that sold you your existing policy or contract to provide you with information concerning your existing policy or contract. This may include an illustration of how your existing policy or contract is working now and how it would perform in the future based on certain assumptions. Illustrations should not, however, be used as a sole basis to compare policies or contracts. You should discuss the following with your agent to determine whether replacement or financing your purchase makes sense:

PREMIUMS: Are they affordable?
 Could they change?
 You're older—are premiums higher for the proposed new policy?
 How long will you have to pay premiums on the new policy?
 On the old policy?

POLICY VALUES: New policies usually take longer to build cash values and to pay dividends.
Acquisition costs for the old policy may have been paid, you will incur costs for the new one.
What surrender charges do the policies have?
What expense and sales charges will you pay on the new policy?
Does the new policy provide more insurance coverage?

INSURABILITY: If your health has changed since you bought your old policy, the new one could cost you more, or you could be turned down.
You may need a medical exam for a new policy.
Claims on most new policies for up to the first two years can be denied based on inaccurate statements.
Suicide limitations may begin anew on the new coverage.

IF YOU ARE KEEPING THE OLD POLICY AS WELL AS THE NEW POLICY:
How are premiums for both policies being paid?
How will the premiums on your existing policy be affected?
Will a loan be deducted from death benefits?
What values from the old policy are being used to pay premiums?

IF YOU ARE SURRENDERING AN ANNUITY OR INTEREST SENSITIVE LIFE PRODUCT:
Will you pay surrender charges on your old contract?
What are the interest rate guarantees for the new contract?
Have you compared the contract charges or other policy expenses?

OTHER ISSUES TO CONSIDER FOR ALL TRANSACTIONS:
What are the tax consequences of buying the new policy?
Is this a tax free exchange? (See your tax advisor.)
Is there a benefit from favorable “grandfathered” treatment of the old policy under the federal tax code?
Will the existing insurer be willing to modify the old policy?
How does the quality and financial stability of the new company compare with your existing company?

**Texas Required Notice for Direct Response Consumer Notices on
Replacement of Life Insurance and Annuities**

NOTICE REGARDING REPLACEMENT

REPLACING YOUR LIFE INSURANCE POLICY OR ANNUITY?

Are you thinking about buying a new life insurance policy or annuity and discontinuing or changing an existing one? If you are, your decision could be a good one—or a mistake. You will not know for sure unless you make a careful comparison of your existing benefits and the proposed policy or contract's benefits.

Make sure you understand the facts. You should ask the company or agent that sold you your existing policy or contract to give you information about it.

Hear both sides before you decide. This way you can be sure you are making a decision that is in your best interest.