



## **WRNewswire**

An AALU Washington Report

**Think New York’s Best Interest Rule 187 Can’t Apply to You?  
You Might Be Surprised: What Producers and Intermediaries Need to Know  
About the Potentially Broad Reach of Rule 187**

Unless you’re a New York producer recommending an annuity or life insurance policy to a New York resident, you don’t need to worry about New York’s new Best Interest regulation (“Rule 187”), right? Wrong. The very broad language in Rule 187 could cause it to apply to other producers, including intermediaries, who are working with a New York producer, even if they never have direct contact with the client. In this Alert, we’re going to take a look at how Rule 187, which will apply to life insurance recommendations on February 1, could apply to producers and intermediaries who may not expect it.

### **Expansive but Undefined Language**

One of the frustrating things about New York’s Rule 187 is that some of the most important terms are not defined. As a result, producers, intermediaries, and carriers are making tough decisions about how broadly some of the Rule’s provisions should be read. This is not an easy task, and it carries with it real compliance risks as there is no guarantee the New York Department of Financial Services (“NYDFS”) will agree with these good faith interpretations in later enforcement actions.

NYDFS has issued some guidance on implementing and interpreting Rule 187, which we summarized in an Alert [here](#). AALU and other organizations are actively engaging with NYDFS to request additional guidance needed to assist producers, intermediaries, and carriers in complying with the Rule, including the issues discussed below. While it is possible that NYDFS may issue additional guidance addressing these concerns, it has not been provided as of this writing.

Here are some of the major ambiguities that could cause Rule 187 to apply to producers and intermediaries who think they could not be subject to the Rule.

- **Material Participation—What Is It and Why Does it Matter?**

One of the biggest issues is whether a producer has “materially participated” in another producer’s recommendation. Here’s what the Rule provides:

“Any requirement applicable to a producer pursuant to this Part shall apply to every producer who materially participated in the making of a recommendation and received compensation as a result of the sales transaction, regardless of whether the producer has had any direct contact with the consumer, provided that product wholesaling or product support based on generic client information, or the provision of education or marketing material, does not constitute participating in the making of a recommendation. [emphasis added]”<sup>1</sup>

In other words, even though the second producer had no contact with the client, if that second producer “materially participated” in the recommendation made by the client-facing first producer (and was paid as a result of the transaction), Rule 187 would apply to both producers (unless one of the exclusions applies).

The practical effect could be quite significant for the second producer, who would be held to the same requirements under Rule 187 as the first producer. This would include ensuring the proper collection, documentation, and consideration of the required suitability factors; making the required disclosures; and providing, in a reasonable summary format, the favorable and unfavorable factors underlying the recommendation. This puts the second producer at some risk—if Rule 187 applies to the second producer, would the second producer have a Rule 187 compliant process, or is the second producer essentially relying on the first producer and potentially sharing responsibility for compliance failures? To further complicate matters, it may be nearly impossible for the second producer to know whether Rule 187 was followed, such as in an intermediary arrangement where these second producer does not supervise or control the first producer and has no contact with the client.

#### *What Does Material Participation Mean?*

Obviously, then, knowing what constitutes material participation and whether one of the exclusions applies is essential to compliance for those working with New York producers. Unfortunately, we don’t have clear guidelines, and BGAs, FMOs, IMOs, and other intermediaries are reaching different conclusions about whether their services might rise to the level of material participation, or whether they fit into one of the exclusions.

For example, some have concluded that NYDFS intended to prevent a senior producer who hadn’t properly considered the client’s best interest from ordering a junior producer in the same agency to recommend a certain policy to the client. Viewed this way, the material participation provision is intended to hold the second producer accountable for what was, in fact, the “real”

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<sup>1</sup> Rule 187, Sec. 224.4(k).

recommendation to the client. If this more narrow interpretation of the Rule's scope is correct, relatively few intermediaries would be affected.

However, others have concluded the NYDFS intended the material participation provision to cover any other producers or intermediaries who advise the first producer and help shape the recommendation, even if they are separate entities. An example might be where the second producer or intermediary reviews the client's information and recommends a particular carrier or type of policy to the first producer for the client, and the first producer follows this advice in making the final recommendation. If this interpretation is correct, the threshold for material participation could be quite low, and many intermediaries and other second producers could be affected.

- **Product Wholesaling/ Support Exclusion—The Significance of “Generic” Information**

Separate from the material participation issue, there is also the exclusion issue. The good news for many intermediaries is that Rule 187 specifically excludes certain activities, stating that they are not “participation,” material or otherwise, in the first producer's recommendation. These exclusions are for “product wholesaling and product support” and “education or marketing material.”

The education and marketing exclusion is fairly unambiguous, and likely will be useful to many producers who are involved in talking to producers about products. However, the product wholesaling and product support exclusion only applies where these services to the first producer are “...based on generic client information.” This raises a number of important questions about what “generic” client information means, both in terms of technical compliance and in terms of interpreting the scope of material participation.

*Generic Client Information—Administrative Support vs. Recommendations to Particular Clients*

In terms of scope, conditioning the product wholesaling and support exclusion on the use of only “generic” client information could be one way NYDFS is drawing a distinction between administrative support and playing a substantive role in helping the first producer decide what to recommend to a particular client. It suggests that NYDFS may believe that some product wholesaling and support activities could be material participation if they are focused on a particular person.

For example, running illustrations based on client information provided by the first producer may just be support and not material participation—the second producer is not recommending what the first producer should do, but crunching numbers at the first producer's request. On the other hand, the second producer might be using the first producer-provided client information to suggest which carriers or policy types the first producer should consider for this particular client. If this is the distinction NYDFS is drawing, the line between generic and specific client information becomes very important, as the applicability of Rule 187 to the second producer may depend on it.

Unfortunately, this line is not clearly drawn, and it is not clear what is “generic” client information and what isn’t. Probably it is generic client information if all the second producer knows about the prospective client is a few relevant data points and no name. But what if the client’s actual name is also provided? Alternatively, what if nearly every relevant detail about the client is disclosed to the second producer, except the name? In which of these scenarios is the wholesaling and product support based on “generic” information? Unfortunately, we don’t have clear answers to these questions, and producer and intermediaries have to make judgment calls regarding the services they provide to other producers.

### **Conclusion:**

Rule 187 presents a number of compliance challenges to producers, intermediaries, and carriers—all of whom are working in good faith to comply with the new Rule. Some of these challenges are clearly understood, but others result from ambiguity in Rule 187 itself. The regulated community can’t always discern from the text of Rule 187 what NYDFS intended, and this creates compliance risk.

The potentially long reach of the material participation clause in Rule 187 is a less-obvious but real risk facing producers and intermediaries who might reasonably believe that the Rule wouldn’t apply to them. AALU and others in the industry have urged NYDFS to issue guidance narrowly interpreting the scope of material participation and broadly applying the exclusions for product wholesaling and support. Clear guidelines would avoid confusion and risk of unintentional compliance errors. However, until such clarity is provided, producers and intermediaries would be well advised to review the services they provide to client-facing producers to assess whether these could be construed as material participation and whether an exclusion applies. We will provide updates and alerts on Rule 187 issues as we continue working with our members on compliance implementation.