

Insurers to Invest Big in ‘Regtech’ as Web of Best Interest Rules Grows

By Warren S. Hersch April 28, 2021

Insurers and their distributors will soon be plowing a lot more money into tools and services to help them navigate an increasingly complex regulatory landscape.

The global market for “regtech” is forecast to grow to \$33.1 billion by 2026 from just \$5.3 billion in 2019, representing an annual growth rate of 21%, according to a February report from the research firm Facts and Factors. Compliance and risk management are fueling much of the increase in regulatory software and services.

Carriers have good reason for devoting more resources to compliance technologies: A widening array of best interest and revised suitability rules, often varying from state to state, are raising the bar on what’s required to protect investors. That’s increasing the risks that carriers and distributors face for failing to meet higher standards of care.

The rules are forcing companies to monitor employees, reinvestment recommendations, transactions and accounts for suitability and undue risks. Mandated disclosure must also be properly communicated.

“If you weren’t focused on it before, you really need to be focused on this area of client best interest,” says Lee Garf, head of compliance at Nice Actimize, a provider of regulatory compliance software. “The regulators are coming — that’s what we hear loud and clear.”

At the Securities and Exchange Commission, a key focus is ensuring compliance with its best interest regulation, a 2019 rule that requires broker-dealers to recommend only products in the client’s best interest and identify conflicts of interest and financial incentives in product sales.



Lee Garf, head of compliance at Nice Actimize

The Financial Industry Regulatory Authority, a private organization that reports to the SEC, is conducting exams to ensure compliance with the regulation and two Finra rules that bear on the suitability of product recommendations.

The self-regulator has “expanded its scope from what we might have been looking at before — reviews and testing on a more comprehensive basis of procedures, policies, practices,” Finra CEO Robert Cook said during an April 14 session of the Insured Retirement Institute’s 20 in 21 conference.

At the state level, insurers are contending with a growing number of best interest rules. David Altmaier, Florida’s insurance commissioner and the president of the National Association of Insurance Commissioners, noted at the conference that 10 states have adopted an NAIC model law on an annuity suitability and best interest standard. Proposals are pending in 10 other states.

There’s also New York’s Regulation 187, a particularly stringent rule covering sales practices, disclosures and documentation for annuities and life insurance.

Running afoul of regulators can lead to significant penalties, corrective action plans and even remediation, warns **Kathy Donovan**, a senior compliance counsel for Wolters Kluwer’s compliance program management business. The company is a provider of software for the risk, compliance and regulatory sectors.



Kathy Donovan, a senior compliance counsel at Wolters Kluwer

“Unfortunately, the industry has seen a number of highly publicized examples in recent years showcasing these failures,” she says.

The Delaware Department of Insurance’s market conduct examinations yielded, for example, nearly \$700,000 in fines during 2019 from more than a dozen companies found to have violated the state insurance code or related regulations, the department reported in January of last year.

Also in 2019, New York’s Department of Financial Services fined six insurers operating in the state for ill-advised swaps of deferred for immediate annuities. The companies — among them New York Life, Companion Life, Guardian, Northwestern Mutual, Prudential and United States Life — had to reimburse \$1.15 million to New York customers and pay \$673,000 in penalties, the state reported.

A risk that insurers and distributors face in the pandemic’s wake, notes Garf, is showing how they improved their compliance programs and heightened standards of care. That entails illustrating the challenges faced, remedial measures taken, lessons learned and

how they intend to ensure compliance in a “future work from anywhere environment,” he says.

Meeting Product Demand

Third-party software that helps insurers and distributors comply with various rules is generally sophisticated at comparing product features and costs, guiding client discussions, crafting recommendations and supervising sales agents, George Hanley, a managing director with Deloitte’s risk and financial advisory unit, says in an interview.



*Deloitte risk and financial
advisory managing director
George Hanley.*

The challenge for carriers adopting the tools, he says, is figuring out how to make their products illustrate attractively when comparing them to competitors’ offerings.

Wolters Kluwer has a web-based tool, NILS State Filing, which formats regulatory information and transmittal forms for ease of use. A separate online product, NILS Insource, lets users monitor regulatory materials and assess the compliance ramifications of insurance obligations. Other tools in the NILS suite manage best interest compliance risks and assign regulatory changes a priority ranking accompanied by recommended requirements.

“A differentiating feature of our data feed,” says Donovan, referencing Insource, “includes expert summaries and regulatory updates that are tagged with lines of business and insurer operational functions so insurers can route these developments to the proper areas—and develop the proper controls accordingly.”

Nice Actimize earlier this month unveiled an artificial intelligence-powered product, Surveil-X Suitability. Among other features, the tool lets insurers flag suitability and best interest breaches related to life insurance, annuities, account rollovers and loans on insurance policies using risk detection models.

Garf says other products can segment best interest rules by state, correlate trades and communications in one system, and provide natural language processing and machine learning so risky behavior and gaps in compliance can be quickly spotted.

However good the tools, fulfilling requirements of the various federal and state rules could prove challenging because what best interest looks like in practice isn’t yet clear, Garf cautions.

“Ultimately it will likely come down to information and consistency — having the data to support your compliance story, and having the ability to show a reliable, uniform approach to compliance across the organization,” he says.