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## Honorable Mention

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By Editorial Staff      Wed, Sep 4, 2024

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*Top news items: GAO investigators go 'undercover' to study conflicts of interest; SEC charges six major ratings agencies with record-keeping lapses; How the commercial real estate bust could affect US life insurers; Prudential expands its reinsurance strategy; Voya tops \$100bn across multiple employer solutions; Nassau issues new FIA with 18% bonus; American Life & Security launches new FIA.*

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### GAO investigators go 'undercover' to study conflicts of interest

Over the course of several months, 102 financial professionals in the U.S. received phone calls from General Accounting Office researchers posing as a fictitious 60-year-old who wanted advice about what to do with about \$600,000 in IRA and 401(k) accounts.

Acting more as mystery shoppers than as sting operators, the GAO investigators documented 75 completed encounters in which the “financial professionals described their role and the nature of the relationship with the client and discussed the client’s financial profile.”

Here’s how the GAO, in a [report](#) published in July and released last week, described what its researchers did:

We steered the conversations toward subjects that would help us learn about potential conflicts of interest that might exist in the relationship. We brought up subjects conversationally, without using uniform language. In most cases, we explicitly asked about conflicts of interest, because regulators suggest doing so.

In most cases, we discussed the term fiduciary, because it helped establish the nature of the relationship, facilitated a discussion of the investor protection standards that would be applicable, and because the definition of a fiduciary was the subject of DOL’s 2016 rule regarding conflicts of interest...

We discussed variable compensation to financial professionals, because earning more from recommending one product, service, or company over another can be a source of conflicts of interest... We analyzed call transcripts for information obtained about conflicts of interest, including responses to questions about conflicts of interest, fiduciary protections, and variable compensation.

GAO’s undercover calls revealed that when investors ask professionals about conflicts of

interest, their questions “may not always produce helpful information.” While “firms’ disclosures of conflicts are available to investors... investors may not review or understand these documents.” In other discoveries:

- “In 18 of our undercover conversations, financial professionals described ways that other financial professionals are compensated, such as through sales and fees that can lead to conflicts of interest. Twelve financial professionals recommended ways retirement investors can protect themselves from conflicts of interest or made statements about general products or firm types to avoid.
- “Four of those discussed product types to pay attention to with regards to conflicts of interest. For example, financial professionals discussed avoiding certain investment products because of the compensation a financial professional would receive for selling them, including annuities, load mutual funds, and proprietary products.<sup>95</sup> Six of the 12 financial professionals discussed compensation models a retirement investor should pay attention to for conflicts of interest.”
- “Fifteen financial professionals told us that recommending insurance products, such as annuities, would constitute fiduciary advice, and three financial professionals told us that recommending insurance products would not constitute fiduciary advice. One financial professional explained that with the purchase of an annuity, our 60-year-old retirement investor would not be exiting the fiduciary relationship but would potentially be exiting a fee-based relationship. Another financial professional said he could not act as a fiduciary when recommending an annuity because he could earn commission from that product.
- As of September 2023, 83% of non-wealthy RIA clients were with firms that were registered as or affiliated with a type of broker-dealer and 63% were clients of investment advisers who were also doing business as an insurance broker or agent or affiliated with an insurance company or agency. Financial professionals may provide one recommendation as an RIA and another as a broker-dealer or insurance agent, which may not be apparent or meaningful to a retirement investor.
- Our undercover investigation found that financial professionals often used the term “best interest” when describing “fiduciary” duties. Of the 70 financial professionals who we talked to about the term “fiduciary,” 41 said it meant acting in the client’s “best interest.” One financial professional was reportedly a fiduciary under FINRA.<sup>84</sup> Another said a financial professional has a fiduciary responsibility to make sure he is selling the right products.

The GAO concluded:

Whether a fiduciary standard applies can vary based on context. As a result, it may not always be apparent whether a financial professional has a fiduciary obligation to the retirement investor or not. Financial professionals can have multiple roles, such as

registered representative of a broker-dealer of securities and insurance agent, and retirement investors may not fully understand the conflicts associated with each role.<sup>85</sup> Most financial professionals we spoke to (49 of 75) were both. registered representatives of broker-dealers and investment adviser representatives, which meant they could act in either capacity.

Based on our disclosure review and our undercover phone calls, conflicts can be numerous, complex, and dynamic, which can make it challenging to completely convey them all, and their implications, through a real time conversation with a retirement investor. Retirement investors have a stake in understanding conflicts of interest in their relationships with their firm and financial professional because conflicts of interest may be associated with lower investment returns.

Conflicts of interest are a common part of many financial transactions involving products recommended to retirement investors. The mechanisms in place to help identify or explain conflicts of interest, such as required disclosures and discussions with financial professionals, may not fully explain the risk and challenges posed by conflicts of interests. Despite obligations to mitigate and eliminate certain conflicts, conflicts of interest persist and can negatively impact retirement investors.

### **SEC charges six major ratings agencies with record-keeping lapses**

The Securities and Exchange Commission has charged six nationally recognized statistical rating organizations, or NRSROs, for significant failures by the firms and their personnel to maintain and preserve electronic communications.

The firms admitted the facts set forth in their respective SEC orders, an SEC release said. They “acknowledged that their conduct violated recordkeeping provisions of the federal securities laws; agreed to pay combined civil penalties of more than \$49 million, as detailed below; and have begun implementing improvements to their compliance policies and procedures to address these violations.”

- Moody’s Investors Service, Inc. agreed to pay a \$20 million civil penalty;
- S&P Global Ratings agreed to pay a \$20 million civil penalty;
- Fitch Ratings, Inc. agreed to pay an \$8 million civil penalty;
- HR Ratings de México, S.A. de C.V. agreed to pay a \$250,000 civil penalty;
- A.M. Best Rating Services, Inc. agreed to pay a \$1 million civil penalty; and
- Demotech, Inc. agreed to pay a \$100,000 civil penalty.

Each of the credit rating agencies, with the exception of A.M. Best and Demotech, is also required to retain a compliance consultant.

A.M. Best and Demotech engaged in significant efforts to comply with the recordkeeping requirements relatively early as registered credit rating agencies and otherwise cooperated with the SEC's investigations, and, as a result, they will not be required to retain a compliance consultant under the terms of their settlements.

"We have seen repeatedly that failures to maintain and preserve required records can hinder the staff's ability to ensure that firms are complying with their obligations and the Commission's ability to hold accountable those that fall short of those obligations, often at the expense of investors," said Sanjay Wadhwa, Deputy Director of the SEC's Division of Enforcement. "In today's actions, the Commission once again makes clear that there are tangible benefits to firms that make significant efforts to comply and otherwise cooperate with the staff's investigations."

Each of the six firms was charged with violating Section 17(a)(1) of the Securities Exchange Act of 1934 and Rule 17g-2(b)(7) thereunder. In addition to significant financial penalties, each credit rating agency was ordered to cease and desist from future violations of these provisions and was censured.

The four firms ordered to retain compliance consultants have agreed to, among other things, conduct comprehensive reviews of their policies and procedures relating to the retention of electronic communications found on their personnel's personal devices and their respective frameworks for addressing non-compliance by their personnel with those policies and procedures.

### **How the commercial real estate bust could affect US life insurers**

Recognizing U.S. life insurers' "significant exposure" to commercial real estate (CRE), and "pressure on commercial property values" from "lower demand for office space as well as higher interest rates," at the Chicago Fed recently analyzed "life insurers' CRE exposures and their implications for financial stability."

The Fed's researchers published their findings in [\*\*\*Economic Perspectives, No. 5, August 2024\*\*\*](#). They reported that:

- At \$600 billion (as of 2022:Q4), commercial mortgages were the third-largest asset calls in life insurers' portfolios, accounting for about 16% of the insurers' total

investments and about 14% of general account assets.

- Life insurers are also exposed to CRE through their \$170 billion CMBS holdings. About 80% of life insurers' CMBS holdings are senior (AAA-rated) tranches; life insurers rarely invest in below investment-grade CMBS tranches.
- Given their significant CRE exposures, life insurers could potentially experience significant losses if CRE prices deteriorate.
- Despite investing in highly rated CMBS tranches, life insurers could potentially incur losses from their CMBS holdings.
- Current and at-origination loan-to-value (LTV) ratios are low for CRE mortgages compared to those for residential mortgages.
- Life insurers would suffer a \$10 billion loss from their commercial mortgage portfolios. The average loss is about 1.1% of capital, with more than one quarter of life insurers experiencing no losses. With few exceptions, insurers' losses are less than 10% of their capital.
- We do not find evidence that exposure to CRE affected life insurers' stock returns in two periods of heightened concerns about CRE.
- In a severe shock, five large insurers—insurers with \$10 billion assets or more—could experience losses of more than 20% of their adjusted capital, and several insurers may face heightened regulatory scrutiny and have to raise capital.
- Most insurers with large estimated losses have only a small share of runnable liabilities, mitigating concerns about potential runs triggered by CRE-related losses.
- The life insurance sector as a whole could face combined losses of about \$36.3 billion from direct and indirect exposures to CRE.
- Some individual large life insurers face significant losses of up to 34% of their capital. However, the largest losses are concentrated in life insurers with limited run risk.
- Stocks of publicly traded life insurers with large CRE exposure did not exhibit abnormal negative returns after the failure of SVB or the earnings announcement of NYCB, suggesting that market participants did not anticipate life insurers experiencing outsized losses related to CRE.

## **Prudential expands its reinsurance strategy**

Prudential Financial, Inc., has agreed to reinsure a portion of its guaranteed universal life block with Wilton Re, resulting in approximately \$350 million of expected proceeds, post-closing, according to a release last month.

Wilton Re will reinsure ~\$11 billions of reserves backing guaranteed universal life policies issued by Pruco Life Insurance Company Arizona (PLAZ) and Pruco Life Insurance Company of New Jersey (PLNJ). The deal covers policies written through 2019 and represents ~40% of Prudential's remaining guaranteed universal life statutory reserves.

In March 2024, Prudential reinsured a \$12.5 billion guaranteed universal life block with Somerset Re. Upon closing, Prudential will have achieved an approximately 60% reduction in its exposure to guaranteed universal life.

PGIM Portfolio Advisory, PGIM's multi-asset solutions affiliate, will manage all the assets supporting the block and will also receive additional assets to manage from Wilton Re. After two years, Prismic, the Bermuda-based reinsurance company created by Prudential and Warburg Pincus, will have an option to reinsure 30% of the block from Wilton Re on substantially similar terms.

Prismic (not to be confused with the web development software company) was created by Prudential and Warburg Pincus last September, with an additional group of investors agreeing to make equity investments in it. At that time, Prudential expected to reinsure to Prismic a block of structured settlement annuity contracts with reserves of ~\$10 billion. Prudential's obligations to the holders of these annuities will remain unchanged following the reinsurance arrangement and Prudential will continue to administer the contracts.

Prudential aims for Prismic to be a strategic reinsurance partner with the ambition to grow their reinsurance relationship materially in years to come. PGIM and Warburg Pincus will provide asset management services to Prismic. Through expanded reinsurance capacity, Prudential expects Prismic will allow the company to provide more people with access to its life and annuity products.

The group of global investors that has agreed to make equity investments in Prismic, alongside Prudential and Warburg Pincus, will give Prismic a combined initial equity investment of \$1 billion from Prudential, Warburg Pincus and a group of global investors.

Prudential and Warburg Pincus will initially own 20% and 15% of the equity in Prismic, respectively. Prismic's board will include two independent directors. Prudential, Warburg Pincus, and the group of investors will each nominate one director.

- Prismic will leverage PGIM's and Warburg Pincus' global investment management capabilities across public and private markets, including public fixed income, private credit, private real estate, and private equity. Prismic will become a client of PGIM Portfolio Advisory, a newly established affiliate within PGIM that combines asset-liability management expertise with portfolio strategy and asset allocation to deliver integrated solutions across public and private asset classes. The Wilton Re reinsurance transaction is structured on an "indemnity coinsurance basis" and contains significant structural protections, including over-collateralization and investment guidelines, the

release said.

Prismic is led by Amy Kessler, a 30-year financial services industry veteran, who will serve as CEO. Kessler was the founding leader of Prudential's international reinsurance business.

Upon closing of the Wilton Re deal, Prudential anticipates a decrease in total after-tax annual adjusted operating income of ~\$35 million. The earnings impact will be finalized at closing. Prudential expects to incur one-time transaction expenses of ~\$25 million in the quarter of closing, primarily due to the extinguishment of certain financing facilities and other closing costs.

### **Nassau issues new FIA with 18% bonus**

Nassau Financial Group has introduced Nassau Bonus Annuity Plus, a bonus fixed indexed annuity designed to give people confidence that they can reach their retirement goals.

Issued by Nassau Life and Annuity Company, Nassau Bonus Annuity Plus is a single premium accumulation-focused fixed indexed annuity that helps increase retirement savings with an up-front premium bonus as well as total accumulation potential from powerful growth options and enhanced control over contract value.

Nassau Bonus Annuity Plus includes several enhanced features, including Nassau's highest premium bonus of up to 18%, a free withdrawal rollover feature, and an early return of premium surrender benefit. These features are made possible by an enhanced benefit fee applied during the surrender charge period, which is 10 contract years in most states.

The enhanced premium bonus of up to 18% creates a larger base to help contract holders grow their retirement savings and increase accumulation potential over the long term.<sup>1</sup>

Contract holders also receive enhanced liquidity features, with the ability to withdraw up to 5% penalty-free annually or roll over the withdrawal option for up to five contract years to receive up to 25%<sup>2</sup>. Also, with the early return of premium surrender benefit, after the fifth contract year contract holders can receive a cash surrender value of at least their single premium less prior gross withdrawals and enhanced benefit fees.

Nassau Bonus Annuity Plus provides powerful, tax-deferred growth potential to help contract holders catch up or get a head start on their nest eggs, all while protecting the principal from market downturns<sup>3</sup>. It offers indexed accounts linked to indices like the S&P

500® and Nasdaq-100®.

<sup>1</sup>Bonus is not available for immediate withdrawal and the bonus amount and associated earnings are subject to a vesting schedule. The bonus amount may vary by age and state and is not intended to meet short-term financial goals.

<sup>2</sup>Withdrawals of any kind (including Required Minimum Distributions) will cause the free withdrawal amount to revert back to 5% on the next contract anniversary. Withdrawals exceeding the free withdrawal amount may be subject to surrender charges, recovery of non-vested premium bonus amounts, Market Value Adjustment, and pro-rated fees. See the Product Summary and Product Disclosure for more information.

<sup>3</sup>The principal is protected against market losses and guaranteed under the base contract. Applicable fees will be deducted from the contract value, and this could potentially result in a loss of principal if the contract has had interest credits less than the fees.

Nassau was founded in 2015 and has grown to \$24.3 billion in assets under management, \$1.5 billion in total adjusted capital, and about 374,000 policies and contracts as of June 30, 2024.

### **Voya tops \$100bn across multiple employer solutions**

Voya Financial, Inc., announced today a milestone growth advancement as the firm surpassed \$100 billion across various multiple employer solutions. Further highlighting Voya's experience and commitment to Multiple Employer Plans (MEPs), Pooled Employer Plans (PEPs), Employer Aggregation Programs and other customized solutions, the firm continues to drive growth in this important market segment, with total assets increasing 15% since the same time period last year.

To support its growth and commitment to the multiple employer plan space, Voya recently announced the addition of newly created positions to support sales growth in this important market segment. These roles, which have been focused on driving growth and engagement with both advisors and plan sponsors, are dedicated to helping facilitate the creation of new solutions and adding adopting employers into existing solutions.

Voya's growth across the abundance of multiple employer arrangements has been driven by flexible programs designed to provide optimal support for clients of all sizes. As a result, Voya has experienced significant growth specifically within its Wealth Solutions business, with 34% of total employer-sponsored DC plans participating in a multiple employer plan



solution.

Last year, Voya also announced it is serving as the recordkeeper for first 403(b) Pooled Employer Plan following the SECURE Act 2.0 legislation. The PEP is designed to provide a pooled plan option for 501(c)(3) nonprofit organizations and health care related entities, expanding retirement plan access for employees in these industries.

#### **American Life & Security launches new FIA**

American Life & Security Corp., a six-year-old, Nebraska-based insurer (B++ by AM Best), has launched the American Life MaxGrowth 10 Fixed Indexed Annuity (FIA). MaxGrowth has a contract term of 10 years with annual point-to-point, monthly sum, and “performance-triggered” options. The annuity allows for additional premium contributions within the first 6 months and offers a 5×5 Annuitization option for accessing the full Contract Value over 5 years after 5 years.\*

The contract offers these crediting strategies:

- The S&P Market Agility 10 Index (S&P Market Agility 10 TCA 0.5% Decrement Index): The S&P Market Agility 10 Index is an equity-bond index that measures the performance of equity and fixed income component indices that each take long or short positions based on momentum and volatility indicators in response to changing market conditions. RBC Capital Markets is the hedging partner for the index.
- The Schroders Global Compass Index: The Schroders Global Compass Index is a global multi-asset index that uses a dynamic allocation to seek positive return opportunities amid changing market conditions. The Index uses a rules-based approach to allocate across multiple asset classes, including global equities, government bonds, and energy commodities.

MaxGrowth is Distributed through American Life’s IMO partners, MaxGrowth is currently available in Arizona, Colorado, Florida, Georgia, Illinois, Iowa, Kansas, Kentucky, Michigan, Nebraska, Nevada, New Mexico, North Dakota, Oklahoma, South Dakota, Utah, and the District of Columbia.

\*5×5 Annuitization is only available if no withdrawals other than RMDs have previously been taken. Additionally, MaxGrowth includes a Nursing Home Benefit rider for those who may need nursing home care.