STATE OF NEW YORK
SUPREME COURT COUNTY OF ALBANY

In the Matter of the Application of

THE INDEPENDENT INSURANCE AGENTS AND BROKERS OF NEW YORK, INC. , THE INDEPENDENT INSURANCE AGENTS AND BROKERS OF NEW YORK, PROFESSIONAL INSURANCE AGENTS OF NEW YORK STATE, INC., TESTA BROTHERS, LTD., and GARY SLAVIN,

Petitioners,

For Judgment Pursuant to CPLR Article 78

ORIGINAL

-against-

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

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 capacity as Superintendent of the New York State Department of Financial Services,

Defendants-Respondents.

All Purpose Term
Hon. Henry F. Zwack, Acting Supreme Court Justice Presiding
RJI: 01-18-ST9984 Index No. 907005-18

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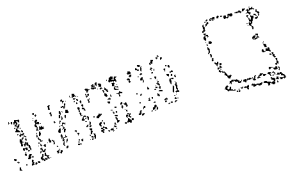

Appearances: Keidel, Weldon & Cunningham, LLP
Howard S. Kronenberg
Attorney for Petitioners
Independent Insurance Agents and Brokers of New York, Inc., Professional Insurance Agents of New York State, Inc., Testa Brothers, Ltd., and Gary Slavin
925 Westchester Avenue, Suite 400
White Plains, New York 10604

O'Melveny & Myers, LLP
Gary Svirsky, Esq., of counsel
Attorneys for Plaintiffs-Petitioners
The National Association of Insurance and Financial Advisors and Donald Damick
7 Times Square
New York, New York 10036

Hon. Letitia James
New York State Attorney General
Attorney for Defendants-Respondents
C. Harris Dague, Esq., of counsel
The Capital
Albany, New York 12224-0341

DECISION/ORDER

Zwack, J:

Before the Court are two applications, the first denominated as the "Independent Action", commenced by the petitioners The Independent Insurance Agents and Brokers of New York, Inc., The Independent Insurance Agents and Brokers of New York, Professional Insurance Agents of New York State, Inc., Testa Brothers, LTD, and Gary Slavin (collectively "Independent or Independent Petitioners"); and the second denominated as the "NAIFA Action", commenced by the plaintiffs-petitioners The National Association of Insurance and Financial Advisors-New York State, Inc., and Donald Damick (collectively "NAIFA or NAIFA Petitioners"), each against the defendants-respondents New York State Department of Financial Services ("DFS") and Maria T. Vullo ("Superintendent"). On March 15, 2019 the Court granted consolidation and a briefing schedule was completed. Both petitioners challenge the DFS' First Amendment to Regulation 187, 11 NYCRR 224.0 et seq. ("Amendment"). The defendants-respondents oppose and have cross moved to dismiss the NAIFA petition.

The Independent Action

The challenged Amendment is also titled "Suitability and Best Interests in Life Insurance and Annuity Transactions," and was issued by DFS on July 17, 2018. The Amendment adopts a uniform standard of care which must be met by agents and brokers, which the regulation identifies as "producers," said standard being that all financial professionals who provide retirement planning and investment advice, both insurers and brokers dealing with annuities and life insurance, must act in the best interest of their clients. The Amendment applies to any transaction or recommendation with respect to a proposed or in-force policy. Prior to the adoption of the Amendment, this standard of care existed for financial professionals with regard to annuity contracts only. The best interest standard charges producers with exercising "care, skill, prudence and diligence," and requires, among other things, they consider "suitability information" for consumers, some 9 factors for life insurance sales and 14 for annuity contracts.

Independent argues that the Amendment must be annulled for several reasons; including that it conflicts with the governing statutory scheme and is beyond the respondent's authority to impose; constitutes improper regulatory policymaking; violates the State Administrative Procedures Act

("SAPA"); is unreasonable, arbitrary and capricious and lacks a rational basis; is unconstitutionally vague; and the Amendment improperly extends the agent/broker relationship. The petitioners also point out that the Amendment mirrors a fiduciary rule enacted by the United State Department of Labor and subsequently invalidated by the federal court.

More specifically, Independent argues that the Amendment improperly makes agents and brokers "producers," without distinction, and imposes upon them a uniform standard of care, that being that they must act in the consumer's "best interest." Independent points out that producers in fact have a narrow and simple duty, which is to procure coverage. This expanded duty, they argue, is at odds with both common law — insurance law is not governed by a fiduciary standard — and statutory construct. The petitioners argue that DFS has overreached it's administrative duty into the legislative realm.

Independent further argues that an amendment was enacted in 1997 which establishes consumer protections to ensure life insurance purchasers receive accurate information on the cost and benefits of an insurance policy or annuity before the policy is purchased. It is also argued that is incumbent upon the Legislature, not DFS, which has no special expertise in this industry, to come up with a standard to regulate non-fiduciaries.

Independent also asserts that the respondents violated SAPA 202-a(3)(c)(iv), in that DFS could not provide a best estimate of the cost for implementation and compliance, or the methodology by which it intends to estimate the same. The lack of a best estimate, Independent argues, demonstrates that the respondents did not consider the cost of implementation, compliance and associated potential costs, determining only that "..producers subject to this amendment likely will incur costs because of this amendment, " and improperly concluding that the costs would be minimal. Independent claims that DFS did not conduct its own analysis of how a best interest standard will affect life insurance sales, it relied on a previous examination conducted by the United States Department of Labor in support of its promulgation of a fiduciary standard for products sold in relation to ERISA retirement plans.[1] Independent argues that the respondents have dismissed questions regarding the cost of compliance and adverse effects on the marketplace. Independent asserts, importantly, that DFS failed to consider the impact of the regulation on small businesses, with limited support and resources, who may choose to leave the market rather than bear costs associated with the

[1]The fiduciary rule was struck down by the District Court in *Chamber of Commerce of the United States of America v United States Department of Labor* (885 F.3d 360 [2018]).

Amendment.

Independent also argues that the Amendment is arbitrary and capricious, lacking any reasonable basis or an adequate record of documented, empirical assessment and evaluation. Independent characterizes DFS's reasoning as "rhetoric without substance" and devoid of any specific context. Further, by implementing this new standard, Independent asserts that litigation will ensue over what the highly subjective "best interest" standard entails, and that the risks and liabilities for failing to meet this undefined standard were not considered. According to the petitioners, the term "best interest" is not only vague and subjective, a question arises as to whose best interest is to be protected; and while the regulation gives examples of "best interests," they are merely examples and not defining criteria. It is also argued that the Amendment creates a fiduciary duty, and makes the producer to an insurance contract a guarantor.

Independent asserts that the term "recommendation" is likewise unconstitutionally vague, because any communication or information given by a producer could be considered a recommendation or advice; and that is not clear what information the producer must compile in order to make a suitable recommendation — financial situation and needs, financial time

line, financial objective — as none of these terms as used in the Amendment are defined. It also argues the "best interest" standard will likely result in lawsuits against insurance producers when a customer suffers an uninsured loss. It also notes insurance is a contract between the insured and the insurer, but the Amendment would place a continuing duty on the producer, who is not a party to the contract. According to Independent, the broker is a legal stranger to the contract, and prior to the Amendment, owed no duty, with the limited exception of when the insured makes a specific request for coverage, once the contract is signed. It is also asserted the Amendment is inconsistent with a primary tenet of insurance law (as recognized by all four New York Appellate Divisions) that one who signs an insurance contract is tasked with having read the same, absent fraud or wrongful conduct. Independent also argues that it is unreasonable for a broker to go line by line through a policy and "insure" the consumer fully understands the policy.

NAIFA Action/Article 78 and Declaratory Judgment

Each of the substantive arguments raised by Independent are also set forth in the NAIFA Verified Petition. NAIFA adds that its' association of

licensed professional insurance agents have a Code of Ethics which already embodies most of the requirements of the amendment. According to the Verified Petition, at paragraph 19, "Providing recommendations and performing services to clients that are always in the client's best interest comes second nature to NAIFA-NYS members. In fact, the NAIFA Code of Ethics, to which NAIFA-NYS's members subscribe, embodies some of the very principles contained in the proposed regulatory amendment."

NAIFA also asserts the Amendment improperly ignores the important distinction between an "agent and a "producer," and the resultant loyalties. It also argues that the "best interest standard" imposes upon producers a fiduciary responsibility, and requires the producer to go beyond the statutory standard of truthfully and accurately representing the terms and provisions of the policy. NAIFA also points out that the Amendment is irrational, as it inexplicably exempts direct sales (those solicited by mail, phone, and online) from the "best interest standard."

In his affidavit in support of the NAIFA petition, Donald Damick, a licensed insurance broker, details how by making a recommendation based upon the consumer's best interest, and no other interest, he could potentially violate his contract with the insurer — because, as he explains, he must place the consumer's interest over the interest of the insurer

without any consideration of his own compensation and any consideration for his principal. He also argues that putting the consumer first makes him a fiduciary. Mr. Damick also asserts the Amendment adds a "significant layer of obligations" on him, in additional to an "already ample consumer protective scheme governing the sale of life insurance and annuity products."

Department of Financial Services

In its Verified Answer, DFS asserts ten defenses, including that the Amendment comports with statutory powers delegated to DFS, is constitutional as it satisfies due process, was validly promulgated, and is rational and not arbitrary and capricious. DFS's other defenses are that the petitioners' claims are barred by SAPA 205, the petition fails to state a cause of action, petitioners failed to exhaust their administrative remedies, and the claims are barred by the applicable statute of limitations.

DFS points out that it has broad supervisory power over the banking, insurance and financial services markets, and has a duty is to protect consumers of financial products, including insurance — as it already licenses all producers and companies, as well as approves all forms,

disclosures and the rates charged by insurers, and investigates consumer complaints. Annuities are further regulated under the present Regulation 187, enacted in 1997, "applying to any recommendation to purchase or replace an annuity contract by an insurance producer," and which requires disclosure and a suitability analysis.

In support of the motion to dismiss the petition, DFS produced the affidavit of Deputy Superintendent for Life Insurance at DFS, James Regalbuto. Mr. Regalbuto pointed out that the Amendment was the result of DFS concerns regarding the increasing complexity of life insurance and annuity products, which in turn has caused consumers to rely more heavily on the recommendations of producers. Life insurance is increasingly being marketed as an "investment product" and the structure of compensation for the sale of life and annuity products creates incentives for producers not to act in their customer's best interest. Mr. Regalbuto also cited the high "lapse rate" in which consumers stop paying premiums and their policies lapse, and DFS's concerns with complaints it has verified regarding producer conduct. Loss of premiums and possibly a surrender penalty negatively affects consumers. Mr. Regalbuto opined that the large early year lapse rates for products intended to provide long term coverage — one third of which will lapse within 5 years — indicated a systematic

problem of unsuitable life insurance recommendations and sales. According to Mr. Regabulto, there have also been a "significant number of verified complaints" and "rampant abuse in the sale of certain life insurance products" particularly involving the sale or replacement of annuities replacing deferred annuities with immediate annuities, which netted the producer a new commission, but may have been disadvantageous to the consumer whose old annuity might have a higher rate of return or higher potential income. These problems were not unique to annuities, according to Mr. Regabulto, and he offered the conclusion that producers were not giving the disclosures which were sufficient to afford consumers meaningful opportunity to identify problematic producer behavior. He asserts consumers are receiving conflicting advice, namely advice not driven by their needs but rather by the producer's need for compensation. He further argued that producers should be required to act in the best interest of the consumer, rather than primarily in the producer's own financial interest.

DFS argues that the growing complexity of insurance products, which requires consumers to rely more on producer recommendations, as well as changes in marketing strategy and producer compensation practices (the overwhelming majority of compensation being paid in the first four years after purchase of a policy) points to the likelihood of producers selling

higher premium products without consideration of the consumer's wants, needs and ability to pay. Further, according to DFS, the four-year retention rate for insurance is only 20%, which as a consequence creates a likelihood that a producer who sold the policy will not remain to service it, making it an "orphan policy" which when assigned a new producer may result in uninformed recommendations regarding an in-force policy or policy lapse or replacement.

In summary, DFS points out that the Amendment is based on the principle that agents and brokers making recommendations about complex insurance transactions are more informed about market intricacies and potential impacts, and thus should be obligated to provide guidance in the best interests of the customer when making a recommendation.

The Motion to Dismiss by DFS

In the NAIFA proceeding, DFS seeks to have the Verified Petition/Declaratory Judgment dismissed for a number of reasons, arguing that the Amendment is well within the statutory authority granted to it by the Legislature, it comports with the separation of powers, and is not a subject which requires an act of the Legislature; does not violate SAPA; is

not "arbitrary and capricious;" and does not violate the Due Process clause of the Constitution as being "void for vagueness." Further, DFS asserts that Independent's argument that the Amendment improperly extends the common law agent/broker relationship is unfounded.

DFS argues that multiple provisions of the Financial Services Law ("FSL") and Insurance Law authorize it to protect consumers by regulating producer sales practices. Insurance Law Article 24 allows the Superintendent to regulate practices that could mislead or inequitably harm consumers, and that the Amendment is a permissible and reasonable exercise of the broad statutory authority to regulate "fraudulent and collusive insurance practices." It asserts that the Amendment is properly crafted and thus must be accorded deference — with the petitioners having the burden of showing that the Amendment is inconsistent with some specific statutory provision. Here, DFS notes that the Superintendent can investigate and take action against unfair trade practices under FSL 201(b)(5); 301(C); 302. The Superintendent can promulgate standards for conduct, regulate insurance brokers and agents under Insurance Law 2101 (k), and under 2110 can refuse to renew, or revoke or suspend the license of any producer who demonstrates untrustworthiness or incompetence or misrepresents the terms of an insurance contract. It is also argued the FSL

clearly sets out that the Superintendent may proactively take measures designed to educate and protect consumers of financial products and to encourage high standards of honesty, transparency and fair business practices among insurers.

DFS asserts that the Amendment does not, impermissibly, characterize both agent and broker as "producers" and both can be subject to the behavioral requirements set forth, as both are licensed to sell insurance policies and annuities to consumers. Both must meet the statutory and regulatory requirements and behave in an ethical, trustworthy and competent manner toward the consumer, and this does not change simply because of any contractual, fiduciary or common-law relationship between an agent and an insurer or a broker to a principal.

The Superintendent also argues that there is nothing in the Insurance Law that prevents her from imposing duties on insurers or producers to consumers in addition to those imposed under the common law. The Superintendent may, through regulation, impose duties on producers with regard to "recommendations," ensuring that are acting in a trustworthy and ethical manner, and that such regulations have been formulated successfully time and time again. DFS also asserts that treating agents and brokers as producers is not arbitrary, capricious or irrational, as the

petitioners challenge. Agents and brokers recommend and sell insurance products directly to consumers; they have the same function and the exact same legal obligation, which is to provide professional, trustworthy advice. The term best interest does not give rise to any conflict between an agent's duties to a principal and duties to a consumer, as it establishes no duties other than the recommendation of a particular product to a particular consumer. The duty owed to the consumer is a limited one, and attaches only to the recommendations by the producer, or in other words, to the sales advice as to products that are available, and thus requires the giving of advice with the consumer's best interest in mind.

DFS argues that, consistent with the guidelines set out in *Boreali v Axelrod* (71 NY2d 1 [1987]), the Amendment does not violate separation of powers principles and is an appropriate exercise of its authority. FSL 201 provides that "it is the intent of the legislature that the superintendent shall supervise the business of, and persons providing, financial products..including any person subject to the provisions of the insurance law..." and requires that the "superintendent shall take such actions as the superintendent believes necessary....to encourage high standards of honesty, transparency and fair business practice....[to] eliminate financial fraud, criminal abuse, and unethical conduct in the industry...." DFS also

notes the Insurance Law is replete with examples of how it is charged with safeguarding the ethical standards of the insurance industry, including licensing, prohibition of deceptive practices, and license suspension if the Superintendent determines the licensee has engaged in misleading conduct or is "untrustworthy or incompetent." DFS further argues, as the Superintendent is charged with eliminating financial fraud and unethical conduct, and where such conduct has been noted, that the Amendment has been appropriately designed and that it "operates proactively to prevent consumer harm." In sum, DFS asserts the Amendment was enacted following consideration of whether its benefits to consumers offset its societal costs.

DFS also asserts that the Legislature has not tried to act on the issue addressed by the Amendment, and that a single or few instances where a bill fails to pass the Legislature is not indicative of legislative disapproval. Here, no bill was introduced on this subject, despite the petitioners' insistence that a bill known as the "Investment Transparency Act" was unsuccessfully proposed. DFS notes that the bill was not geared towards "producers" — but rather was actually intended for distinct groups of financial consultants, investment advisors and retirement planners. Further, DFS notes that the Legislature has taken no action regarding

Original Reg. 187, which requires a standard of conduct for annuities, such as is now proposed in the Amendment for all insurance products.

Turning to the last *Boreali* factor, DFS asserts that it is clear that it has a special expertise when it comes to insurance matters. In formulating the Amendment, it relied on its observations of changes in the market, specific and technical trends in the insurance industry, including the growing complexity in life insurance and annuity products, and problem issues it identified, such as high lapse rates.

DFS asserts that it complied with SAPA, and argues, because the Amendment is a principles-based approach (allowing producers and insurers compliance flexibility) that the costs associated with the implementation of the Amendment are de-minimus. DFS also argues, given the noted flexibility, that it is impossible to estimate the costs of compliance. On this issue, DFS also notes that insurers and producers are already gathering information about their consumers (goals, needs, personal finances) and the compliance process under the Amendment requires similar information gathering and a recommendation — with the distinction that the recommendation must be documented and disclosed... which is the "why" of the Amendment.

DFS asserts that the petitioners are unable to meet the heavy burden

attendant with their challenge to the regulation as arbitrary and capricious (that the Amendment is so lacking in reason as to be essentially arbitrary) as opposed to DFS's required showing of only that Amendment is not in conflict with a positive provision of the insurance law. DFS also argues there is no requirement that it must provide evidence to a certain threshold of harm to consumers before it can regulate.

DFS asserts the Amendment cannot be considered "void for vagueness" and therefore unconstitutional under the due process clause. DFS notes that the petitioners facing this new regulatory requirement had the opportunity to seek guidance from DFS on whatever terms they now challenge, and which afforded them a reasonable opportunity to obtain guidance from DFS on what is permitted or prohibited by the Amendment — thus satisfying due process. Particularly, the petitioners, throughout the regulatory process, had a sufficient opportunity to satisfy their questions regarding the meaning of the words they now challenge. For example, the petitioners question whose interests are served, which is clearly the consumer, defined under the Amendment as the "owner or prospective purchaser of the property." The Amendment also specifically defines "recommendation" as "advice" which will "result in the consumer entering into or refraining from a transaction." The Amendment also defines what a

recommendation is not. Likewise, the best interest standard is not vague, but rather requires the producer to access relevant suitability information in a manner which "reflects the care, skill, prudence and diligence of a prudent person acting in a like capacity and familiar with such matters would use under the prevailing circumstances." The Amendment requires that licensed producers be "competent" and "trustworthy." It is an objective, not subjective, standard.

DFS argues the Amendment does not, as the petitioners argue, extend the agent broker relationship in conflict with common law, noting the Insurance Law is comprised of literally hundreds of regulations that go beyond the scope of common law to protect consumers. The Amendment does not superimpose a "continuing duty" nor is it retroactive. While the Amendment requires a producer act in the consumer's best interest, it does not guarantee or warrant an outcome, and if the information as to suitability is not provided, no recommendation need be made, as would also be the case if there were no suitable product available from the producer. Therefore, under no circumstances does the Amendment make a producer a guarantor, as petitioners argue. DFS notes that it is well settled law that producers do not owe any duty to the insured to recommend the best or the most appropriate coverage, and asserts that the Amendment does not in any

way allow an insured to sue a producer pursuant to its terms, as the Amendment may only be enforced by the Superintendent.

The petitioners, in opposing the DFS motion to dismiss, argue that the Amendment is inconsistent with both the governing statutory theme and common law, citing as an example the equating of insurance agents and brokers into one group entitled "producers." "Producers," as used in Article 21, has a very limited statutory meaning according to petitioners. The petitioners also argue that the statutory scheme provides for the separate and disparate treatment of agents and broker, and equating the two, as done by the Amendment, directly contravenes Insurance Law sections 107(a), 2101(a), 2101(c), 2103 and 2104. Agents and brokers are two separate entities, with separate duties and obligations, which are separately defined.

The petitioners also argue that the Amendment exceeds the authority granted to the DFS by the Legislature, and does not meet the test set forth in *Boreali* (71 NY2d at 9). They assert that DFS made value judgments to resolve complex social issues, did not study or properly consider the present and future costs, created it's own set of comprehensive rules where the Legislature has been making efforts, and did so without the unique expertise which such changes would require.

In addition to noting the failure by DFS to comply with SAPA by doing a cost estimate, the petitioners cite to an American Council of Life Insurance estimate that the initial costs to comply with the Amendment will be $208 million and estimated annual costs at $66.6 million. The petitioners argue that the failure by DFS to set forth a best estimate is fatal to the Amendment. They also argue that DFS justification for the need for the Amendment is insufficient under SAPA.

The petitioners also assert that the "best interest" standard as written is a litigator's dream, arguing that insurance agents and brokers are "not legal advisors in a better position to discuss the meaning of insurance policies and their meanings than an ordinary person reading the same policy" (Slavin affidavit at paragraph 10). Consumers will be encouraged to place too much trust in the producer. The petitioners also argue the Amendment will place new duties on agents and brokers and which were rejected under common law. They also assert that the terms "recommendation" and "suitability" are so vague that it makes the compliance with the Amendment impossible and thus unconstitutional.

Discussion

The primary purpose of declaratory judgments is to adjudicate the parties' rights before a "wrong" actually occurs, in the hope that later litigation will be unnecessary (*Klosterman v Cuomo*, 61 NY2d 525 [1984]). SAPA 204, which authorizes declaratory rulings, is to assist the general public by facilitating action by administrative agencies in interpreting statutes and regulations...and determining the applicability of the statutes and regulations to all the various situations which may from time to time be presented (*Power Authority of State of New York v New York State Dept. of Environmental Conservation*, 86 AD2d 57 [3d Dept 1982]). SAPA 204[2][c] provides: "Notwithstanding the inconsistent provisions of the law, a person may submit a petition in the manner provided for in Article 78 of the CPLR without first applying for a declaratory ruling.....a person may concurrently petition the court pursuant to Article 78 and petition the agency pursuant to this subdivision." SAPA 205, provides, in part, as follows: "Nothing in this section shall be construed to grant or deny to any person standing to petition under article seventy-eight of the civil practice law and rules or to bring an action for a declaratory judgment or to prohibit the determination of the validity or applicability of the rule in any other action or proceeding in which its invalidity or inapplicability is properly asserted." Further, it does not necessarily require the issuance of a declaratory ruling prior to the

commencement of an Article 78 petition when exhaustion of administrative remedies would be "an exercise in futility" (*Usen v Sipprell,* 41 AD2d 251, 256 [4th Dept 1973; *Watergate II Apartments v Buffalo Sewer Authority,* 46 NY 2d 52, 57 [1978]).

In determining whether an agency has gone over the line into areas reserved for the Legislature, a court may use the four considerations first set forth in *Boreali* (71 NY2d 1). The considerations are "whether (1)the agency did more than balance costs and benefits, but instead made value judgments entailing difficult and complex choices between broad policy goals to resolve social problems; (2) the agency merely filled in details of a broad policy or if it wrote on a clean slate, creating its own comprehensive set of rules without the benefit of legislative guidance; (3) the Legislature has unsuccessfully tried to reach agreement on the issue, which would indicate that the matter is a policy consideration for the elected body to resolve; and (4) the agency used special expertise or competence in the field to develop the challenged regulation...(and) are not mandatory, need not be weighed evenly, and are essentially guidelines for conducting an analysis of an agency's exercise of power" (*Matter of LeadingAge N.Y., Inc. v Shah* 153 AD3d 10, 17-18 [3d Dept 2017] internal quotations and citations omitted).

If, considering the factors under *Boreali* ,the record demonstrates that

DFS acted within its authority and that it has not enacted a regulation which should the premise of the Legislature — in sum that the Amendment is an exercise of discretion by an administrative agency — the Court is mindful that it "cannot interfere unless there is no rational basis for the exercise of discretion or the action complained of is arbitrary and capricious" (*Matter of Pell v Board of Educ. of Union Free School Dist. No.1 of Towns of Scarsdale & Mamaroneck, Westchester County*, 34 NY2d 222, 231 [1974]); and its function as a reviewing court is a very limited one, and if the interpretation given by DFS is not irrational or unreasonable, the Amendment should be upheld (*Matter of Howard v Wyman*, 28 NY2d 434, 438 [1971]).

With certain caveats, including that a regulation is not inconsistent with statutory language and statutory purposes, or that it is policy created "on a clean slate to balance conflicting interests in the absence of legislative guidance" (*Matter of New York State Land Tit. Assn, Inc. v New York Dept. Of Fin. Servs.*, (169 AD3d 18, 33 [1st Dept 2019])[2] the Superintendent may adopt a regulation that goes beyond the text of the Insurance Law. Here, the Court is also mindful that the burden rests with the petitioners to establish that

[2]NAIFA use this case to support the contention that the agency was without legislative authority. Albeit the petition striking the regulation was granted in the lower court, the regulation was upheld on appeal.

the Amendment is inconsistent with some specific statutory provision or that the effect of the Amendment is so severe as to render it arbitrary or irrational (*Oster v Schenck*, 41 NY 2d 782, 785-786 [1977]).

"[T]he determination of an agency acting pursuant to its authority and within its area of expertise is...entitled to judicial deference" (*Matter of Entergy Nuclear Indian Point 2, LLC v NY State Dept. of State*, 130 AD3d 1190, 1192 [3d Dept 2015], citations omitted). This said, the Court is also mindful that its role is not to "second-guess" DFS regarding the efficacy of the Amendment, but rather determine whether the Amendment is a "reasonable exercise" of DFS' "broad power to implement the Insurance Law, and is neither irrational nor unreasonable, neither arbitrary nor capricious" (*Matter of Sullivan Fin. Group, Inc. v Winn*, 94 AD3d 90, 97-98 [3d Dept 2012], internal quotations and citations omitted). All said, if the Amendment is consistent with enabling legislation and is not so lacking in reason for its promulgation that it is essentially arbitrary, it should be upheld (*Matter of New York Land Title Ass'n.*, 168 AD3d at 30).

Under common law, an agent and broker have no fiduciary relationship to the consumer, their only obligation is to obtain coverage that a customer specifically requests or to inform the customer of their inability to do so (*Murphy v Kuhn*, 90 NY2d 266, 269 [1997]), and "have no continuing duty to

advise, guide or direct a client to obtain additional coverage" (*Voss v Netherlands Ins. Co.*, 22 NY3d 728, 734 [2014]). There is no special relationship where there is no delegation by the consumer of his/her insurance decision making responsibility and there is no compensation apart from the payment of premuims (*Hoffend & Sons, Inc., v Rose & Keirnan*, Inc. 7 NY3d 152 [2008]).

A consumer may allege he/she has a special relationship with an insurance agent or broker if any one of "three exceptional situations...(exist)...: (1) the agent receives compensation for consultation apart from the payment of premium; (2) there was some interaction regarding a question of coverage, with the insured relying on the expertise of the agent; or (3) there was a course of dealing over an extended period of time which would have put objectively reasonable insurance agents on notice that their advice was being sought and specifically relied on" (*Hefty v Paul Seymour Ins. Agency*, 163 AD3d 1376, 1378 [3d Dept 2018]), citations omitted).

Conclusion

The Court denies the respondents' motion to dismiss on the ground

that the petitioners failed to comply with SAPA's requirement that they exhaust their administrative remedies before filing their Article 78 petitions — specifically because they did not did not seek a declaratory judgment prior to commencing the proceedings, and precluding this Court from exercising jurisdiction. Simply stated, the declaratory rulings on the myriad of issues raised in the petitions would be fruitless — thus, so the parties can move forward in a more constructive way, a determination of the validity on the Amendment is required.

For the reasons that follow the Court dismisses each Article 78 petition and the request for a declaratory judgment.

Here, the Court finds that the Amendment is a proper exercise of the powers granted to the DFS Superintendent, that it is not an attempt by DFS to improperly legislate, and that is nether arbitrary or capricious.

The record establishes that — albeit the petitioners attempt to argue otherwise — DFS has complied with SAPA in adopting the Amendment. The Amendment, initially proposed in December 2017, went through two rounds of changes before it was promulgated, and in response to all the same issues raised in the petitions. DFS issued a Regulatory Impact Statement (RIS), a Regulatory Flexibility Analysis (RFA) and a statement in lieu of a Job Impact Statement (JIS), receiving 36 comments. DFS met with interested parties

in January and May, 2018. Following a revised proposal/assessment of comments in May, 2018, it did publication, and received further comments. DFS issued a revised RIS, RFA, and JIS, received and responded to a second round of comments, and on July 17, 2018, issued the Amendment.

Turning to the petitioners' argument that SAPA was violated because DFS did not provide a valid cost analysis, the Court finds that the efforts of DFS in this regard are amply sufficient. The petitioners have provided no specifics to back up their own cost estimates, and most of the petitioners' statements regarding the cost increases on insurers and the industry are vague and inconclusive. For example, turning to the petitioners' cost estimate from the American Council of Life Insurers, Vice President of ACLI, Kate Kiernan, explains in a letter to DFS of February 28, 2018, that the ACLI and the Life Insurance Council of New York (LICNY) conducted a member survey to examine the potential cost — with only 63% of New York licensed companies responding — and there was absolutely no breakdown of the cost items or other explanation as to what the survey entailed. DFS explains that the costs associated with the implementation of the Amendment are de-minimus, because it is a principles-based approach allowing producer and insurer flexibility, and that this flexibility makes it impossible to estimate the costs of compliance. DFS asserts, and the record supports, that the

Amendment does not impose any particular system, forms, or procedures for meeting the requirements of the Amendment, that compliance can be minimal, and may be as simple as a document that discloses why a recommendation is being made, or by enhancing a system the petitioners already have in place. According to the NAIFA petition at paragraph 19, "Providing recommendations and performing services to clients that are always in the client's best interest comes second nature to NAIFA-NYS members. In fact, the NAIFA Code of Ethics, to which NAIFA-NYS's members subscribe, embodies some of the very principles contained in the prosed regulatory amendment." Clearly, NAIFA members adhere to a code of ethics which already requires them to primarily consider the best interests of their client, making the requirements of the Amendment far less onerous than they otherwise argue. Additionally, costs that consumers incur when they are sold products that do not fit their needs — wasted premuims/loss of needed benefits — far outweigh any costs to the insurer. Here, the Court also notes that revenues lost from recommending products which are not in the consumer's best interests is not a viable insurer "cost" for the purposes of a reasonable SAPA analysis. Just as the petitioners argue the Amendment will be cost prohibitive for small insurers, it can also be argued that the smaller insurers are more than likely to already have a procedure

in place for making the best suitable recommendations to their consumers.

Similarly, the Amendment does not impose on insurers any specific form, system, or procedure which must be followed in developing a procedure to monitor their workforce, and the same is true for education and training. Nor does compliance portend increased costs, as insurers already have these procedures in place. The record supports that many insurers were getting ready to implement the Department of Labor "fiduciary" rule (29 CFR 2510), before it was struck down by the 5th Circuit, thus stripping away any merit to their claim that they have been caught off guard by the Amendment, or that this was not a trend the market was moving toward. The applicable provisions of the Amendment take effect on February 1, 2020 — thus, under any reasonable analysis, it can be said that the insurers and producers have adequate time to implement the most cost effective way to meet the requirements of the Amendment.

Nor does the Amendment run afoul of *Borealli.* There is simply no provision in the Insurance Law that precludes the Superintendent from adopting rules governing the conduct of producers, as set out in the Amendment. To the contrary, when the Financial Services Law was enacted in 2011, it charged DFS with the responsibility of ensuring "the continued safety and soundness of New York's banking, insurance and financial

services industries, as well as the prudent conduct of the providers of financial products and services through responsible regulation and supervision" (FSL 102) — with the Superintendent having "broad power to interpret, clarify and implement the legislative policy" (*Matter of New York Land Tit. Assn.*, 169 AD3d at 22, citations omitted). Under FSL 102 (e)(k), DFS was to undertake "effective state regulation of insurance industry" stewarding the "elimination of fraud, criminal abuse, and unethical conduct by and with respect to..the insurance industry." The Court also notes Insurance Law 2110 contains an exhaustive treatment of actions which can be taken by the Superintendent to "encourage high standards of honesty, transparency and fair business practice...[to] eliminate financial fraud, criminal abuse, and unethical conduct in the industry...." Licensing, prohibition of deceptive practices, license suspension for the "untrustworthy and incompetent" are examples of already existing regulations relating to broker conduct (Insurance Law 2110; FSL 201(b)(5)).

The Legislature has not tried to act on the issues addressed by the Amendment. A single or few instances where a bill fails to pass the Legislature is simply not dispositive of this issue or indicative of legislative disapproval or of "repeated efforts to legislatively address the issue with concomitant public debate and lobby" (*Matter of Spence,* 136 AD3d at 1246).

Despite the petitioners' insistence to the contrary, no bill on this subject was introduced in the Legislature or that it failed to act on. The bill, known as the Investment Transparency Act, and cited by the petitioners, was unsuccessfully proposed, and was not geared toward "producers" and instead meant to address other distinct groups of financial consultants, investment advisors and retirement planners. Nor is there any question that the Legislature has not taken any action regarding the Original Regulation 187, which requires a standard of conduct for annuities, such as is now being proposed for all insurance products. The language in the original regulation, that the product be "suitable" to meet the consumers need, is hardly distinguishable from a product which will meet a consumer's "best interests" as set out in the Amendment. Nor is there any question that the Superintendent is charged with eliminating fraud and conduct which can be detrimental to the consumer, and to the extent that such conduct has been noted, the Amendment "operates proactively to prevent consumer harm." In the Court's view, the Amendment was adopted, consistent with statutory authority, well within DFS' broad powers, and after it carefully weighed the benefits to the consumers and societal cost.

Turning to fourth *Boreali* factor — whether DFS "used special expertise or competence in the field to develop the challenged regulation" — the

petitioners' argument that the Superintendent does not have expertise in the area of insurance matters is wholly without merit (*Matter of Medical Socy. of State of N.Y. v Serio,* 100 NY2d 854, 864 [2003]). In formulating the Amendment, DFS relied on its observations of changes in the market, specific and technical trends in the insurance industry, the growing complexity in life insurance and annuity products, and the problem issues it identified, such as high lapse rate. DFS monitored the Department of Labor, the Certified Planner Board of Standards, and the SEC. It is also the agency charged with approving the forms of insurance products sold in New York. All said, DFS possesses the required knowledge and expertise to enact the Amendment.

The Court turns next to the petitioners' arguments that the Amendment is arbitrary, capricious, irrational, and an abuse of discretion on the part of the respondents.

The Amendment, which is directed at providing guidelines for trustworthy and competent producer practices, and preventing self-dealing by producers at the consumer's expenses, falls squarely within the provisions of Financial Services Law and the Insurance Law. Against a backdrop of legitimate concerns for consumers, the burgeoning market of increasingly complex insurance and annuity products, and the rather

remarkable lapse rate the market is experiencing, the Amendment is interstitial — consistent with underlying statutory purposes (*Matter of General Elec. Capital Corp. v New York State Div. of Tax Tribunals,* 2 NY3d 249, 254 [2004]) — and reflects a rational and reasonable movement towards consumer protection. Arguing against a standard that requires a review of the suitability of an insurance product for a consumer is simply counterintuitive, where the recommendation need only be made with "care, skill, prudence and diligence." The recommendation is not binding, and the ultimate choice remains in the hands of the consumer.

In the Court's view, DFS's rationale for the Amendment is amply sound and supported in the record — in sum sufficient to support the powers "expressly conferred...(by the Legislature), as well as those required by implication" (*Greater N.Y. Taxi Ass'n. v New York City Taxi and Limousine Commn.,* 25 NY 3d 600, 608 [2015]). For example, as stated by DFS Deputy Superintendent James Regalbuto, there have been large numbers of innovations to permanent life insurance products, with a large number of additions features and "riders." Between the years 2011 and 2017, according to Regalbuto, there have been 44,624 policy forms submitted to DFS for approval. This, combined with the real life situation where the initial sale, and not ongoing payments of premium beyond four years, is

what generates the most income for a producer, and the lapse rate of almost 50% after ten years, point to real concerns for insurance market regulators. Petitioners are asking the Court to discount market studies, DFS experience, emerging research and recommendations by consumer advocates that a mere disclosure rule is not enough.

The Court turns next to the petitioner's argument that DFS refrain from enacting the Amendment and wait until there has been a meeting of the minds as to define "best interest" — including taking no action NAIC, US Department of Labor, the Securities and Exchange Commission and FINRA have the opportunity to coordinate and develop a best interest standard. As the record shows, the Amendment was proposed in 2017, and concerning the issues addressed by the Amendment, to date there has been no movement by the other entities. Against this backdrop, the Court notes *Chamber of Commerce v US Dept. of Labor* [885 F3d 360[5th Circuit 2018]), which while vacating the fiduciary rule, recognized that this did not foreclose state action "or for other appropriate federal or state regulators to act within their authority" on the issue of consumer protection. All said, given the specific grant of Legislative authority to DFS to "encourage high standards of honesty, transparency and fair business practice...[to] eliminate financial fraud, criminal abuse, and unethical conduct in the industry...." (Insurance

Law 2110), it was not required to await action by the other entities cited by the petitioners and on the issues addressed in the Amendment (*Matter of Riverkeeper, Inc. v Planning Bd. Of Town of Southeast,* 9 NY3d 219, 234 [2007]).

Turning to the petitioner's argument that respondents acted erroneously in equating agents and broker equally (calling them "producers"), the term "producers" is specifically defined in Insurance Law 2101 (k) as "insurance agent, title insurance agent, insurance broker, reinsurance intermediary, excess lines broker, or any other person required to be licensed under the laws of this state, to sell, solicit or negotiate insurance." However viewed, agents and brokers have been, and will continue to be "producers" under the Insurance Law, as reflected in the definition of their actual functions, which are identical: a broker "acts or aids in any manner in solicitating, negotiating or selling any insurance product or annuity "; and, an agent "acts in such a manner in the solicitation of, negotiation for, or sale of insurance...or annuity..." The Amendment applies to these activities, and makes it clear that the consumer is the beneficiary, not the insurer. That the agent has a contractual relationship with the insurer, and the broker a direct relationship with the buyer, is of no real moment, as the Amendment clearly applies not only to

the producer's interaction with the consumer, but contains very specific responsibilities which the insurer itself must undertake.

Although petitioners strenuously argue otherwise, the Amendment, by requiring a producer to recommend an insurance product that is in the consumer's best interest, does not impose a standard that is inapposite to common law or statutory purpose of the Insurance Law and FSL. Merely because the Amendment requires a producer to recommend to the consumer a product which best fits the consumer's insurance needs does not impose a "special relationship" from which liability for fraud or tort can arise. The common law duty to obtain the requested coverage remains the same, the Amendment requires only that the producer review the consumer's options and make a recommendation based upon the product's suitability to consumer, with regard to the product's purpose, affordability and duration. All said, it is a recommendation which the consumer can accept or not, and the Amendment does not shift the actual decision making from the consumer to the producer. Once a recommendation has been made, the producer records it. It does not necessarily entail a relationship of trust (although trust is not bad per se) it merely requires job proficiency. It does not entail any further activity on the part of the producer; for example, no follow-up is required, and it still remains incumbent on the consumer, not

the producer, to identify any ongoing insurance needs.

Nor is the Court persuaded by the petitioners' arguments or exception to being equated with fiduciaries — particularly considering the assertion by NAIFA petitioners that they should be allowed to designate themselves (as some have) as investment advisers. Given investment advisers owe a fiduciary duty to a consumer, "independent of their contractual duties" (*Bullmore v Ernst & Young Cayman Islands*, 45 AD3d 461 [1st Dept 2007], the Court finds no error in the Amendment provision that prohibits producers from using the designation "investment advisor" unless the individual possess the appropriate credentials — nor is the prohibition irrational — particularly considering insurance products and annuities perform important roles in investment and retirement planning, and that misuse of the term may be misleading to the consumer.

Turning to the petitioners' arguments that the Amendment is unconstitutional or that is unconstitutionally vague, the arguments fail. The Amendment is not retroactive, and does not apply to routine services in already in-force policies, like renewal. The Amendment does require producers to review the current policy with the consumer and determine if it is the consumer's best interest, however, they do not have to comply with the full suitability requirements set forth in the Amendment or disclose the

basis for the recommendation.

The Amendment is not ambiguous; in fact, it is clear and quite self-explanatory. It provides that the producer must consider the best interest of the consumer (11-NYCRR 224.4[a]-[b]). It contains precise definitions of the issues highlighted by the petitioners. To be clear, the Court is not persuaded by the arguments that different meanings could be ascribed; for example: "consumer." Consumer is defined as "the owner or prospective purchaser of a policy" (224.3[a]). Recommendation is defined under 11 NYCRR 224.3 (e)(1) and (2) as "advice" provided to a consumer intended, or reasonably perceived by the consumer to be intended, "to result in the consumer entering into or refraining from a transaction." Contrary to the petitioner's argument otherwise, it is expressly stated whose best interest is to be considered, and that is the consumer. As noted, the issues raised by both petitions were repeatedly raised, and answered, by the Superintendent prior to the enactment of the amendment, including that the Superintendent remains available to answer any questions which arise as producers and insurers prepare their methods of compliance.

Nor does the Amendment run afoul of common law. Specifically, while the Amendment sets out a standard which requires a producer, or insurer, to adhere to what is in a consumer's best interest, the standard can only be

enforced by the Superintendent and creates no independent cause of action. The Amendment does not guarantee a particular outcome. DFS considered the strenuous objections to the Amendment, and the suggestion by the ACLI, and other groups, that a provision be added which stated that nothing in the Amendment created a private right to action for violation of any of the requirements of Part 224. Of course, on a case by case basis there will always be those situations where a producer, through their own conduct, express or implied, wittingly or purposefully, may assume or acquire duties in addition to those fixed on the common law.

Nor can the Amendment be said to be arbitrary because it exempts sales which involve no producer, such as on-line, television, and phone sales. The explanation by DFS — that such sales generally relate to death policies (just enough insurance to cover final expenses, or policies under $10,000.00) — is reasonable; particularly considering the application and the underwriting process are simplified and can be done without the assistance of producers, if the consumer so wishes. Where the consumer decides to proceed with a producer, the Court notes that these same sales are subject to the best interest standard (although petitioners did push to have term life insurance sales excluded from the amendment)[3] and on this

[3]According to DFS, in 2018, 19% of consumer complaints arose from the sale of term insurance, up 4% from 2017.

record declines to find the distinction either arbitrary or irrational.

All said, the stated purpose of the Amendment is to insure that producers who have not already done so "establish standards and procedures for recommendations to consumers with respect to policies...so that any transaction with respect to those policies is in the best interests of the consumer and appropriately addresses the insurance needs and financial objectives of the consumer at the time of the transaction." (Reg. 187 §224.0 [b]). It is consistent with the purposes asserted by the petitioners, as stated the petitioner Donald Damick in his affidavit in support of the NAIFA petition, at paragraph 5, where he states: "When I make a proposal to a customer, under Regulation 187, I must place the customer's interests over any consideration for my compensation and any considerations for my principal, the insurer." The Amendment specifically seeks to prevent insurers and producers from recommending a product designed to maximize compensation to seller and one that may be otherwise properly disclosed and suitable, but not in the best interest of the consumer. As such, the Superintendent acted within the scope of her authority and jurisdiction, the Amendment is consistent with her authority to interpret and implement the Insurance Law and FSL, and it was properly considered and weighed against all alternatives, and is not unconstitutional.

Accordingly, it is

DETERMINED and ORDERED, that each petition is dismissed.

This constitutes the Decision and Order of the Court. This original Decision and Order is returned to the attorneys for the Defendants-Respondents. All other papers are delivered to the Supreme Court Clerk for transmission to the County Clerk. The signing of this Decision and Order shall not constitute entry or filing under CPLR 2220. Counsel is not relieved from the applicable provisions of this rule with regard to filing, entry and Notice of Entry.

Dated: July 31, 2019
Troy, New York

Henry F. Zwack
Acting Supreme Court Justice

8/7/19
KM

Papers Considered:

1. Verified Petition by Independent dated November 16, 2018 with Exhibits "1" through "10"; including the Affirmation of Gary Slavin dated November 13, 2018; and Affidavit of Stephen Testa, sworn to on November 13, 2018;
2. Notice of Motion to Dismiss Independent Article 78; Verified Answer dated April 1, 2019; Certified Regulatory Record, Affidavit of James Regalbuto, sworn to on March 5, 2019, Affidavit of Peter A. Dumar, Jr., dated April 1, 2019, Memorandum of Law;
3. Attorney Affirmation of Howard S. Kronenberg in further support of the Verified Article 78 Petition and in Opposition to the Motion to Dismiss dated April 15, 2019, with Exhibits "A" through "P";
3. Notice of Motion of Amended Verified Petition and Declaratory Judgment Action dated November 30, 2018; Amended Verified Petition of NAIFA dated ; Affidavit of Donald Damick, sworn to on November 16, 2018; Memorandum of Law;
4. Verified Answer to NAIFA Amended Petition/Declaratory Judgment dated March 6, 2019; Affidavit of James Regalbuto in Support of Respondents's Answer to the Amended Petition, sworn to on March 5, 2019; Respondent's Memorandum of Law in Support of Their Verified Answer and Cross-Motion to Dismiss;
5. Reply Memorandum of Law in Further Support of the Amended Verified Article 78 Petition and Declaratory Judgment Petition and in Opposition to Cross-Motion to Dismiss;
6. Respondent's Reply Memorandum of Law in Further Support of Their Cross-Motion to Dismiss the NAIFA Petition.