ACLI
Financial Security. For Life.

THE Committee OF Annuity Insurers
www.annuity-insurers.org

August 23, 2022

Mr. Peter Weber, Chair
Mr. Tomasz Serbinowski, Vice Chair
National Association of Insurance Commissioners
LATF Index-Linked Variable Annuity (ILVA) (A) Subgroup

RE: ILVA Subgroup Exposure of *Actuarial Guideline ILVA: Nonforfeiture Requirements for Index Linked Variable Annuity Products*

Dear Messrs. Weber and Serbinowski:

The American Council of Life Insurers (ACLI)[1] and the Committee of Annuity Insurers (CAI)[2] appreciate the opportunity to submit comments to the ILVA Subgroup on the fourth exposure of *Actuarial Guideline ILVA: Nonforfeiture Requirements for Index Linked Variable Annuity Products* (Fourth Exposure).

As you know, we previously submitted comments on (i) January 27 on the Subgroup's original exposure of a proposed ILVA Actuarial Guideline (AG); (ii) May 2 in response to the revised AG exposed on April 1; and (iii) July 1 in response to the revised AG exposed on June 7. We deeply appreciate the Subgroup's continued dedication to the AG, careful consideration of our prior comments, and openness to robust discussion with the industry.

We believe that the Subgroup is close to a workable final solution for the AG. There are, however, two important aspects of the Fourth Exposure that we believe require further consideration and revision:

- ***Effective Date.*** We do not see a single date of April 1, 2023 as manageable from a regulatory or company perspective. We recommend a bifurcated effective date for New and Existing ILVAs (as defined immediately below). The proposed April 1, 2023 effective date is manageable for ILVA contracts initially submitted for first-time approval on or after that date (New ILVAs). However, we believe it is problematic for ILVA contracts approved, or initially submitted for approval, prior to April 1, 2023 (Existing ILVAs), particularly for Existing ILVAs that will require significant AG-related revisions. In order to avoid undue burdens on insurance companies and regulators, as well as

[1] The American Council of Life Insurers (ACLI) is the leading trade association driving public policy and advocacy on behalf of the life insurance industry. 90 million American families rely on the life insurance industry for financial protection and retirement security. ACLI's member companies are dedicated to protecting consumers' financial wellbeing through life insurance, annuities, retirement plans, long-term care insurance, disability income insurance, reinsurance, and dental, vision and other supplemental benefits. ACLI's 280 member companies represent 94 percent of industry assets in the United States.

[2] The Committee of Annuity Insurers is a coalition of life insurance companies that issue annuities. It was formed in 1981 to address legislative and regulatory issues relevant to the annuity industry and to participate in the development of public policy with respect to securities, state regulatory and tax issues affecting annuities. The CAI's current 30 member companies represent approximately 80% of the annuity business in the United States.

significant market disruptions for consumers, we urge the Subgroup to consider an extended July 1, 2024 effective date for Existing ILVAs.[3]

- ***Application of Market Value Adjustments (MVAs).*** We appreciate the dialogue we've had with Subgroup members on the topic of MVAs following the July 13 ILVA Subgroup call. We are encouraged that the Fourth Exposure includes language which increases the flexibility of how MVAs integrate into the Hypothetical Portfolio framework. However, we do not believe MVAs should be restricted to partial withdrawals and surrenders. In order to better align the MVA provisions with the market value framework reflected elsewhere in the AG, we urge the Subgroup to eliminate the language restricting MVAs to partial withdrawal and surrender decrements to maintain a principles-based approach. We also suggest several other targeted clarifying changes to the Text section of the guideline.

In this regard, our recommended revisions to the AG are reflected in the attached mark-up of the Fourth Exposure and discussed more fully below.

<u>The AG Should Include an Extended Effective Date of July 1, 2024 for Existing ILVAs</u>

In lieu of the proposed effective date of April 1, 2023 for *all* ILVA contracts issued on or after that date, we recommend that the AG be revised to include a bifurcated effective date for New and Existing ILVAs, as follows:

New ILVAs

For New ILVAs, we are not requesting that the Subgroup reconsider the April 1, 2023 effective date. We believe the April 1, 2023 effective date to be manageable for new filings initially submitted for approval on or after this effective date.

Existing ILVAs

If our recommended Existing ILVA effective date is adopted, any Existing ILVA contracts issued on or after July 1, 2024 would need to comply with the AG.

We believe the proposed effective date is unworkable for Existing ILVAs that would require significant AG-related revisions and would impose undue hardships on issuers of those Existing ILVAs, as well as SEC and state regulators. It may also cause significant market disruption, as some companies will not be able to meet an April 1, 2023 deadline, forcing temporary withdrawal of their ILVA products from the market.

Our concerns about the proposed AG effective date for Existing ILVAs primarily relate to the significant SEC filing, state filing, and implementation challenges that some companies will face following the adoption of the AG. We believe that a July 1, 2024 effective date would provide all companies with the necessary time and flexibility to address those challenges, which we have briefly summarized below.

---

[3] To be clear, based on this approach, the term "Existing ILVA" includes both (i) contracts approved prior to April 1, 2023 and (ii) contracts initially submitted for approval prior to April 1, 2023 that are ultimately approved on or after April 1, 2023. The AG would apply to all Existing ILVA contracts issued on or after July 1, 2024. The AG would not apply to any Existing ILVA contracts issued prior to July 1, 2024.

- ***SEC Filing Challenges.*** By way of background, ILVAs are securities that must be registered and periodically updated with the SEC. SEC registration calls for detailed information about ILVA product features, as well as extensive financial and other information about the issuing insurance company.

  Following the AG's adoption, some companies will have to file either new or amended SEC registration statements reflecting changes to their Existing ILVA designs. The SEC filing process will be labor intensive, for both companies and SEC staff reviewers. AG-related changes may impact many SEC disclosures, especially the detailed disclosures and examples on the computation of interim values. Indeed, if a company must overhaul its interim value methodology to comply with the AG, the SEC filing process could be akin to registering an entirely new product.

  In addition, it could take several months for a company to prepare and file a new or amended registration statement, respond to potentially multiple rounds of SEC staff comments, and obtain an SEC order of effectiveness. While the length of this process will depend on a company's particular facts, we expect it will take approximately six months for most companies making registration statement filings, and potentially longer for those companies that must overhaul their interim value methodologies.

  Importantly, the SEC filing process will require companies to navigate complex timing issues. ILVAs are registered with the SEC on either Form S-1 or Form S-3, but most companies use Form S-1. As such, some companies will be making filings on Form S-1 following the adoption of the AG. Form S-1 filings require the inclusion of prior year-end audited financial statements, and, depending on the timing of the filing, may also require the inclusion of unaudited quarterly ("interim") SEC financial statements. Insurance companies using Form S-1 do not generally prepare interim SEC financial statements. Accordingly, companies using Form S-1 routinely limit the implementation of any changes that trigger registration statement filings to when interim SEC financial statements are not required, *i.e.*, May 1. May 1 also coincides with such insurance companies' requisite "Annual Update" filings. Filings at other times of the year ("Off-Cycle" filings) trigger the need for interim SEC financial statements.

  With that as background, from an SEC timing perspective, the proposed April 1, 2023 effective date for Existing ILVAs presents potential undue and unmanageable burdens on insurers and regulators, as follows:

  - *Annual Updates.* Form S-1 registrations must be fully amended/re-filed annually. These Annual Updates must be completed no later than May 1. Each year, companies dedicate substantial resources to Annual Updates beginning in January (sometimes earlier) through May 1. Annual Updates require all product and business-related disclosures to be fully updated, as well as the preparation of audited SEC financial statements for the prior fiscal year. It is likely that companies would opt to address any significant AG-related revisions as part of the Annual Update. However, the ability of a company to do so will depend on resource constraints, any other product or business-related matters requiring new disclosures, the timing of the AG's finalization, and the point at which the audited financial statements become available (for most companies this is not until *after* April 1 each year).

    An April 1, 2023 AG effective date essentially requires the AG-related changes to be layered into insurers' upcoming 2023 Existing ILVA Annual Updates. As described above, the typical Annual Update process is already a lengthy one, and building in AG-related revisions will add additional

time to that process. Respectfully, any insurers that need to make significant product changes for the AG would need to begin that process in earnest immediately, which is not feasible given the fact that the AG changes are not yet final. Moreover, even if the changes were final, an Existing ILVA effective date that is one month sooner than ILVAs' current long-standing SEC annual May 1 compliance date creates two compliance dates that are firmly at odds. Most companies will not be able to accelerate the SEC compliance date to accommodate the AG's because they will not have their SEC audited financial statements in place by April 1 (which are essential to any SEC filing date). In addition, at that time of the year, SEC staff is working diligently to clear comments on filings by May 1, not April 1. In essence, for some companies, an April 1 Existing ILVA effective date will be unmanageable and will result in the temporary suspension of ILVA sales.

- *Off-Cycle Filings.* Form S-1 registrations may be amended or re-filed apart from an Annual Update. As noted above, however, such Off-Cycle filings present additional challenges. In particular, when making an Off-Cycle filing, a company must prepare interim SEC financial statements and other interim financial disclosures. The preparation of these interim SEC financial statements and financial disclosures is burdensome and costly, which is why S-1 insurers diligently avoid Off-Cycle filings. In this regard, it is important to understand that extending the Existing ILVA proposed effective date by a few months is not a viable solution. Any effective date that does not accommodate a May 1 filing will result in the need for interim SEC financial statements.[4]

We believe these very practical timing issues are important to consider. The effective date for Existing ILVAs should provide companies with the flexibility to address any significant AG-related revisions via an Annual Update (which we believe will be the strong preference) or an Off-Cycle filing, as a company sees fit based on its particular circumstances. To accomplish this, the effective date should be a reasonable period of time after May 1, 2024. We believe this flexibility will be essential in avoiding market disruption to consumers.

- ***State Filing Challenges.*** The AG will require revisions to some existing ILVA policy forms, which must be re-filed and approved in all states where an ILVA is sold. In addition, companies would be required to prepare and submit the actuarial certification and memoranda called for by the AG. This will be a resource-intensive and time-consuming process. It will also be a large burden on state insurance departments, whose staff will be responsible for reviewing and approving the complex filings. Given the significant time and effort necessary to complete these multi-state submissions, we do not view an April 1, 2023 effective date – or any effective date in 2023 – as a viable option.

- ***Implementation Challenges.*** Companies that revise their Existing ILVA designs to comply with the AG will be faced with significant challenges related to implementation. For example, such companies must: newly program systems for the administration of contracts issued on or after the effective

---

[4] We note that whether a registration statement is for a New or Existing ILVA, the same financial statement requirements apply. With New ILVAs, however, companies will be able to comply with the April 1 AG effective date but can, in turn, delay any New ILVA launch date and SEC filing until May 1 (when the audited year-end financial statements are typically readily available). In other words, the April 1 date will not cause market disruption, it will simply potentially briefly delay New ILVA launches. Conversely, with Existing ILVAs, companies may be forced out of the market as of April 1 because they will not have the required SEC financial statements and cannot sell without them.

date (while maintaining old systems for the administration of contracts issued prior to the effective date); analyze, prepare, and/or revise marketing and other client-facing materials; train personnel and vendors on the new product designs; and engage with selling broker-dealer firms on matters such as onboarding and training. These implementation challenges will only serve to further stretch such companies' limited resources as they work towards the AG's effective date.

In order to allow for an orderly SEC filing, state filing, and implementation process, to ease the coming burdens on SEC and state insurance department staff, and to avoid significant market disruption to consumers, we recommend an extended effective date for Existing ILVAs in lieu of the effective date proposed in the Fourth Exposure. Based on our extensive experience with SEC filing, state filing, and implementation matters, we believe that a July 1, 2024 effective date would be a fair and workable solution.

The AG Should Maintain a Principles-Based Approach for MVAs

As noted previously, the most material concern we have with the language in the Fourth Exposure is the sentence indicating that market value adjustments may only be applied to partial withdrawals and surrenders. We share the Subgroup's view that MVAs should apply in instances where a company would experience a mark to market impact on fixed income assets, but focusing on only partial withdrawal and surrender decrements excludes many other relevant scenarios. Examples include:

- **Death.** The payment of a death benefit involves the liquidation of fixed income assets supporting the product in a similar fashion to a full surrender. Providing a death benefit tied to market values is also consistent with the market value framework reflected elsewhere in the AG and is aligned with how traditional variable annuities work.

- **Annuitization.** While assets do not leave the insurance company in a lump sum upon annuitization, this event still involves a rebalancing (and marking to market) of fixed income assets to support the new liability profile.

- **Transfer.** This could manifest in multiple ways depending on product design, but one straightforward example is for products that offer traditional unitized VA sub-accounts. A transfer from an ILVA account to a traditional VA sub-account would lead to fixed income assets being liquidated because they wouldn't be used to back the liability in the traditional VA sub-account.

This list is not meant to be exhaustive but illustrates the need to broaden the AG's perspective on MVAs. Rather than attempting to enumerate all of the instances in which MVAs may apply, we recommend deleting the sentence in question and aligning the treatment of MVAs with the principles-based nature of the AG. This approach also works well in light of the actuarial certification related to MVAs described in item 1.e on page 4 of the AG. The certification addresses (i) the alignment with changes in fixed income asset market values, and (ii) equity between the contract holder and the insurance company. These conditions should be sufficient to ensure that MVAs are applied appropriately in ILVA products.

Clarifications

The other recommended changes related to MVAs reflected in the attached mark-up are:

- In the first sentence of the Text section, we added a parenthetical reference to the MVA. Because the Interim Value is defined to exist at any time other than the start date and end date of an Index Strategy Term, the reference here to the Strategy Value needs to be qualified to exclude any MVA. This is applicable in instances where the maturity used for the MVA calculation is longer than the Index Strategy Term. Making this update is consistent with the AG's subsequent language on MVAs, and also ensures that the traditional point-to-point crediting nature of ILVA accounts is maintained.

- In the second sentence of the Text section, the term "weighted average maturity" has been replaced with "investment horizon." An MVA is a hypothetical representation of changes in fixed income asset values. The term "weighted average maturity" is inconsistent with a principles-based approach because it may be interpreted to necessitate direct calculation of a metric tied to the actual assets the insurance company holds. Our suggested term, "investment horizon", conveys a substantively similar concept that the MVA may be tied to a time period that is different than the Index Strategy Term.

- In item a.ii of the Text section, the term "interest rates" has been replaced with "yield." This aligns with the way item a. is framed and captures the fact that fixed income asset values are a function of both interest rates and credit spreads.

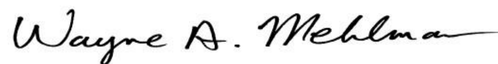
- The remaining marked changes in the Text section are not material, but may improve the clarity of the AG for readers not familiar with its development.

* * *

The ACLI and the CAI appreciate the opportunity to comment on the Fourth Exposure and we urge the Subgroup to consider our recommendations as it continues its progress towards a final AG.

Respectfully submitted,

AMERICAN COUNCIL OF LIFE INSURERS (ACLI)



Wayne Mehlman
Senior Counsel, Insurance Regulation
waynemehlman@acli.com

Brian Bayerle, Senior Actuary
brianbayerle@acli.com

COMMITTEE OF ANNUITY INSURERS (CAI)
For the Committee of Annuity Insurers, By:

Eversheds Sutherland (US) LLP

Eversheds Sutherland (US) LLP
steveroth@eversheds-sutherland.com
maureenadolf@eversheds-sutherland.com