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February 3, 2022

Mr. Mike Boerner
Chair, Life Actuarial Task Force (LATF)
National Association of Insurance Commissioners (NAIC)

Re: IUL Exposure from the December 8, 2021 LATF Session

Dear Mr. Boerner,

The American Academy of Actuaries¹ Life Illustrations Work Group (the “Work Group”) is pleased to provide comments to the LATF on the Indexed Universal Life (IUL) Exposure from the December 8, 2021, session.

As described in the IUL Exposure, some volatility control index accounts have a lower hedge budget than a capped S&P 500 index account but illustrate at the same lookback rate as the Benchmark Index Account (“BIA”). These accounts illustrate at the same lookback rate as the BIA because their option profits (hedge returns relative to hedge costs) are assumed to be higher than the option profits for the BIA. The remaining net investment earnings that are not put toward purchasing options may then be used to offer a fixed bonus, which results in higher illustrated values than those under the BIA.

Although the illustrated values for these accounts can be higher, as noted in the IUL Exposure, the differences may be smaller in magnitude than the illustrations of multipliers or other index enhancements that were addressed by AG 49-A. Indeed, the Work Group notes that AG 49-A has largely had the intended effect that products with multipliers and other index enhancements should not illustrate any better than products without these features.

However, if LATF decides an update to AG 49-A is needed, the Work Group suggests consideration of either of the following approaches that could be used to address current practices:

(A) Apply an additional limit to the illustrated option profit (e.g., 45%)

This approach would apply a fixed predetermined limit to the illustrated option profit, similar, in concept, to the current limit of 145% of the net investment earned rate.

However, it differs from the net investment earned rate as it would place a limit on the illustrated option profit for each account. LATF could apply a limit to the illustrated

¹ The American Academy of Actuaries is a 19,500-member professional association whose mission is to serve the public and the U.S. actuarial profession. For more than 50 years, the Academy has assisted public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

option profit by requiring an amendment to AG 49-A that would bring the illustrated option profits of volatility control indices more in line with the illustrated option profits of other indices. However, this approach could still result in some index accounts illustrating somewhat higher policy values than what the BIA would produce (although more limited than today). An appropriate factor, such as 45% or something else, would have to be determined.

(B) Align BIA limit with option spend through multiple BIAs

Under this approach, the illustrated index rate for each index account would be limited to the lookback rate for a BIA with the same amount spent on hedging. BIAs with lower hedge budgets would have lower caps, and therefore lower lookback rate limits would be applied to the index accounts that use lower hedge budgets. The Work Group notes that multiple BIAs were allowed under AG 49 for cap buy-up accounts but were eliminated under AG 49-A, so we suggest language could be borrowed from AG 49 and applied to indices with lower hedge budgets without reversing decisions that have already been made for multipliers and buy-ups. In contrast to approach (A), approach (B) would not result in some index accounts illustrating higher policy values than the BIA and would not require an agreed-upon appropriate factor. While drafting language for approach (B) may be more difficult and therefore may take more time than for approach (A), the Work Group notes that approach (B) may be a more comprehensive solution.

Changes to AG 49-A that make index accounts illustrate more similarly may result in reduced customer understanding because the differences are not shown in the illustrated values. The Work Group also notes that the approaches described in (A) and (B) do not place limits on the illustration of fixed bonuses, because fixed bonuses do not appear to be the core issue.

In addition, the Work Group notes that there were some questions during the December 8, 2021, LATF session about how volatility control index accounts work and how they may perform relative to other index accounts, such as those based on the S&P 500. The Work Group notes that these questions could be addressed via disclosures.

The Work Group appreciates the efforts of the LATF and IUL Illustration Subgroup to review AG 49 and AG 49-A. If you have any questions or would like further input on the above topics, please contact Khloe Greenwood, life policy analyst, at greenwood@actuary.org.

Sincerely,

Alicia Carter, MAAA, FSA
Chairperson, Life Illustrations Work Group
American Academy of Actuaries