April 30, 2020

Fred Andersen
Deputy Commissioner of Insurance
Minnesota Department of Commerce
Chair, NAIC IUL Illustration (A) Subgroup

Re: ACLI Proposed Draft of Actuarial Guideline 49-A and clarity on earned rate in the DCS and the percentage rate of Indexed Credits

Fred:

This letter is submitted on behalf of John Hancock, Lincoln Financial Group, Pacific Life Insurance Company and Sammons Financial Group. The purpose of this letter is to ask regulators to consider clarifying language on the relationship between the earned rate underlying the DCS in Section 5 and the percentage rate of Indexed Credits in Section 4 of the ACLI draft. The above noted companies have also submitted a separate letter that supports the direction of the ACLI’s proposed AG49-A including prospective-only application and Option #1 regarding the treatment of policy loans. This letter is meant to supplement that letter.

We believe that having clarity regarding the DCS and the rate of Indexed Credits is a minor but necessary change for the industry to have a common understanding of how to apply AG49-A. Different interpretations for this relationship were identified during discussions among carriers regarding potential changes to AG49.

**Interpretation 1:** The earned rate underlying the DCS in Section 5A is not restricted by the percentage rate of Indexed Credits in an illustration.

**Interpretation 2:** The earned rate underlying the DCS in Section 5A should be restricted by the percentage rate of the Indexed Credits in an illustration.

The ACLI examples represent the first interpretation. Example 1 on the tab with the hedge budget equal to the net investment earnings rate shows Indexed Credits at a level of 6.20%, while the Section 5A rate is calculated at 6.53%. In the illustration testing calculations for this example, Interpretation 1 could allow the earned rate underlying the DCS to be 0.33% more than the illustrated rate of Indexed Credits.

However, in a typical IUL design, the contract will state that the index-linked credits will equal the increase in the underlying index and if a carrier has perfectly hedged the amount of index credits, these amounts would be the same and there would be no additional return on the hedge. The hedge return would match the amount credited to the policy values.
Therefore, we believe that the correct interpretation is number 2, that the earned rate underlying the DCS should be limited by the illustrated Indexed Credits. Otherwise, the illustration tests could include margins that are not contractually realizable. For this reason, the IUL Coalition proposal dated February 21 contained the following in Section 5A:

_The assumed return on hedges shall only be used in the disciplined current scale testing to support the illustrated Index Credits in the policy._

If regulators are comfortable with Interpretation 1, that the earned rate underlying the DCS need not be restricted by the level of Indexed Credits, it would be valuable to have AG49-A directly state this or include a drafting note that clearly allows an illustration actuary to use this interpretation. This will ensure there is consistent interpretation on this issue and clarity for actuaries certifying illustrations for these products.

Thank you for consideration of our comments and we are happy to answer any questions or concerns you may have.

Respectfully Submitted,

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cc: Reggie Mazyck, NAIC