SUBMITTED ELECTRONICALLY: JCook@naic.org

June 4, 2019

NAIC Annuity Disclosure (A) Working Group, the Honorable Mike Yanacheak, Chair
c/o Jennifer R. Cook, Senior Health Policy Advisor and Counsel
National Association of Insurance Commissioners (NAIC)
Executive Office, Hall of the States Building, Suite 700
444 North Capitol Street, NW
Washington, D.C. 20001-1512

RE: Supplemental Response to Request for Comment: *Annuity Disclosure Model Regulation (MDL 245), 3-7-19 Exposure Draft*

Dear Chairman Yanacheak and Members of the NAIC Annuity Disclosure Working Group:

At the May 13, 2019 meeting of the NAIC Annuity Disclosure (A) Working Group ("the Working group), NAFA, [1] was asked a question regarding our May 29, 2019 letter[2] that we submitted in response to the Working Group's Request for Comment on your proposed revisions to the NAIC Annuity Disclosure Model Regulation #245, dated March 7, 2019.[3] Specifically, we were asked to further explain NAFA's position as it related to our argument that increasing from the current 10 years to 20 years the required period of time that indexes must have been in existence to be used in annuity illustrations would restrict consumer choice and create unfair advantages within the financial and retirement services industry. On behalf of NAFA, I am grateful for the opportunity to provide some additional clarity regarding this central concern and thank you in advance for your consideration.

<u>Today's illustration requirements provide very robust disclosure and an effective demonstration</u>

An important reason to retain the present 10-year-history requirement to illustrate an index used in an annuity is that requiring a longer period brings no additional client transparency, no

[1] NAFA, the National Association for Fixed Annuities, is the premier trade association exclusively dedicated to fixed annuities. Our mission is to promote the awareness and understanding of fixed annuities. We educate annuity salespeople, regulators, legislators, journalists, and industry personnel about the value of fixed annuities and their benefits to consumers. NAFA's membership represents every aspect of the fixed annuity distribution and marketplace for fixed annuities sold by independent agents, advisors and brokers. NAFA was founded in 1998. For more information, visit www.nafa.com.

[2] https://nafa.com/wp-content/uploads/2019_0510_NAFA-Comment-Exposure-Draft-NAIC-Annuity-Disclosure-MDL-245.pdf

[3] https://www.naic.org/documents/cmte_a_adwg_exposure_draft_249_index_rev.pdf?31

additional disclosure, and no greater protection. An annuity illustration that meets the requirements of today's advertising requirements is a very robust disclosure document. An illustration today explains much about the workings of the annuity product and its limitations. It illustrates three scenarios so that some reasonable and credible view is gained of the annuity's potential performance. Buyers are so much better informed by an illustration today than they would be without any illustration (incorporating the benefits of all other required and recommended disclosures herein).

<u>A 20-year indexed history requirement will reduce the use of illustrations</u>

A 20-year-history requirement would prevent the illustration of annuities with innovative and proprietary indexed interest strategies. These strategies are expected to deliver more competitive and more stable interest rate credits over time, and are an excellent complement to the common all-equity indexes that are almost always available too. We acknowledge that a 20-year history requirement would not prevent the sale of annuities with these newer indexes and underlying interest strategies; those products can and will be sold without an annuity illustration. However, these newer indexes will not be utilized to the same extent as today. *How much less will they be utilized by clients? How many such indexes will be withdrawn by carriers? What sort of sales and marketing abuses will occur or increase because no illustration is available?* We have no answers for these real concerns.

<u>A 20-year requirement is a winning outcome for only a few established indexes</u>

Severely limiting the illustration of interest strategies by imposing a 20-year-history requirement creates the risk of something like an oligopoly or monopoly in the index licensing industry. S&P Dow Jones Indices is the dominant index licensing firm in the indexed annuity industry. Twenty years ago, S&P Dow Jones Indices was almost the only index licensing firm available to insurance carriers offering indexed annuities. Licensing costs are higher when the provider is the dominant licensing provider. A 20-year history requirement will reduce consumer choice and increase consumer cost, and it will not produce greater innovation. While the addition of a volatility-control mechanism to an otherwise 20-year old equity index makes that index an attractive alternative strategy, this will still favor the big, old indexes from S&P Dow Jones Indices and the annuity world will be taking a large step backwards.

<u>New Indexes usually are oriented toward volatility control</u>

The addition of volatility-control mechanisms within indexed interest strategies is a very significant and beneficial development in the entire annuity industry, both fixed indexed and variable annuity industries. The benefits of volatility control were known but rather academic and arcane before the Great Recession crash of 2008 to 2009. The investment and annuity industries added volatility-control mechanisms to manage various risks inherent to offering annuities or owning annuities. Volatility control reduces the market risk of loss, and it stabilizes the cost of hedging indexed interest rate strategies. Indexed annuity carriers can offer more interest potential to annuity buyers because of volatility control and annuity buyers have the potential to earn more interest. This is the innovation of volatility control.

<u>Investment industry's use of volatility control and management is a big innovation</u>

The variable annuity industry uses volatility control and volatility management features to hedge their risks of offering guaranteed lifetime income benefits. With better risk management with volatility control, those carriers can offer more competitive features and benefits to their annuity clients. In addition, volatility-control and management features are easy to find in the mutual fund industry, with exchange-traded funds, within structured investment products, and within even indexed bank certificates of deposit. The proliferation of specifically-constructed indices for volatility control and additional diversification shows how valuable this innovation is seen by the entire financial services community.

<u>Fixed Indexed Annuity Illustrations are also form of client protection</u>

If indexed annuity interest strategies cannot be illustrated because they lack enough history, consumers will not understand them and utilize their benefits. There is a substantial risk that consumer interest will migrate to the investment industry—variable annuities, indexed variable annuities, and structured investment products. If that happened, it would bring greater risk of retirement savings losses to many individuals. There could be substantially less principal protection, less guaranteed income, and higher costs to clients. Twenty years of index performance history might be relevant if this was an investment product – if client principal was at risk of substantial market loss. Ten years of market history permits more illustration of more choices and makes many more retirement savings and investment products available for consumer evaluation and comparison.

<u>Broadly-available illustrations extend protection and reduce sales abuse</u>

Current fixed annuity products are principal-protected by state standard non-forfeiture laws. The surrender charges of every annuity product are tested against each state's standard non-forfeiture laws when a product is initially filed for review and approval by that state's insurance department. If clients are dissatisfied with the outcome of their annuity purchase, they can surrender the contract at the end of the surrender charge term or sooner. More relevant here, if clients are dissatisfied with their indexed interest strategy selection where indexed interest performance is less than expected, they can reallocate to another indexed interest strategy after one or two years on the anniversary date, without penalty or tax. Many indexed annuity owners allocate among several indexed interest strategies, as they choose.

The fixed indexed annuity is a long-term savings vehicle and not an investment product. It does require some time to work and develop its full benefits. When indexes have become little utilized now and in the past for whatever reason, carriers have removed them and substituted something else. That will continue. It will be very difficult for a client to get "locked into" an index they do not like or want. Despite best efforts, there will always be some risk of defective products from carriers and of sale abuse by agents. Limiting index strategy illustrations does nothing to reduce those risks.

Conclusion

The illustration of indexed interest strategies linked to newer, innovative indexes is not a threat to the retirement assets and financial security of indexed annuity buyers. The annuity illustration as regulated and required today is a primary disclosure document. Preventing the illustration of many indexes because they lack history will reduce disclosure to annuity buyers. That should not be the objective or consequence of annuity illustration regulation. Removing most indexes now available for sale today from inclusion in illustrations used today will eliminate an important option and potential benefit for many annuity buyers. Some sales will be made nonetheless and with less disclosure. Some sales will be made of securities products and investments instead, with potentially more risk and greater cost. The fixed indexed annuity product, over the past 23 years, has delivered full principal protection and many valuable income and other important benefits to annuity buyers. We hope to continue to improve annuity buyer outcomes, benefits, and disclosure.

Again, on behalf of NAFA's members, thank you for the opportunity to submit these supplemental comments. Please do not hesitate to contact me if you would have any further questions or require additional information.

Sincerely,

Charles DiVencenzo
NAFA President and CEO

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