



**Comments for the Center for Economic Justice**  
**To the NAIC Annuity Disclosure Working Group**  
**Proposed Revisions Annuity Disclosure Model Regulation Regarding Illustration of**  
**Products Tied to Indexes in Existence for Less Than Ten Years**

**May 10, 2019**

The Center for Economic Justice writes to comment on the proposed changes reflected in the March 7, 2019 exposure draft of the Annuity Disclosure Model Regulation and to respond to comments by the Academy and the Committee of Annuity Insurers (“CIA”).

Based on the comments of the Academy and the CIA, it appears necessary to review the history of the proposed revisions to the model regulation and the problems surrounding illustrations of indexed annuities.

The working group was created to evaluate two industry-proposed revisions to the model regulation – both intended to increase the range of products eligible for illustration. During the discussion of the first proposal – allowing assumptions for improvements in performance for participating annuities – we learned that insurers will not offer annuities unless the product can be favorably illustrated. This was dramatic evidence that the ability to generate favorable illustrations is the foundation of product design and competition among insurers.

The second industry proposal was to revise the current prohibition for illustrating a product tied to an index that has been in existence for less than ten years to permit the illustration of such products. The review of the industry proposal, the provisions of the current model and the proliferation of new indexed annuity products tied to a variety of new and opaque indexes revealed serious problems with both the industry proposal and the current model. The industry proposals would allow further discretion to insurers with illustrations and further encourage data mining of recent historical experience of securities and/or anything with a price to generate an index with a favorable recent history to illustrate fabulous “returns” for the consumer.

The problem of product design driven by illustration potential is evidenced by the explosion in indices created for and used in indexed annuity products. In some cases, the indexes have been created specifically for, and only for, an indexed annuity product and introduced at the same time as introduction of the annuity product.

Attachment 1 is a list of 90 indexes used in indexed annuities as of March 2019 prepared by Wink. We know that the vast majority of these indices have been in existence for less than 20 years because industry has asserted that changing the model regulation illustration prohibition from 10 to 20 years would affect some 70% of indices used today.

This expanding list of indexes created for or used with indexed annuities evidences the concern raised by CEJ that insurers and their index partners are data mining recent historical performance to create indexes that have no actual historical experience and/or a very limited theoretical historical experience, but which illustrate fantastic “returns” for consumers.

The industry has created a false narrative, captured perfectly in the comments of the CIA, which calls for “proper balance” and warns against restrictions that would “deprive consumers of information necessary for retirement planning” It is clear, however, from the remainder of the CIA comments – all directed at limiting oversight or restrictions on indexed annuity illustrations – that “proper balance” has nothing to do with consumer protection and everything to do with no disruption to the current indexed annuity business model and sales practices.

We urge working group members to affirm that “proper balance” means significant consumer protection for products involving the transfer of retirement assets to an insurer in hopes of securing reliable future retirement income. If the product marketing promises turn out to be false 15 or 20 years in the future, consumers have no meaningful remedy at that future date. Further the information asymmetry between the insurer / producer and the consumer is massive to the advantage of the insurer. In addition, while industry will be able to adapt to almost any set of illustration guidelines that create a level competitive playing field; consumers have neither the time nor flexibility to recover from misleading sales and defective products. We suggest that regulators keep in mind the debacles of massive long term care insurance rate increases, vanishing premium life insurance and universal life insurance cost of insurance issues to understand that “proper balance” must mean to empower and protect consumers in a market that is susceptible to misleading sales practices because of competitive pressures for insurers and producers to utilize ever more extravagant claims for their products while minimizing the disclosure to consumers of costs and downside risk.

We take issue with CIA's assertion that industry's ability to illustrate products tied to indexes which are confidential and cannot be explained to or understood by consumers is providing consumer choice or responding to actual consumer demand. We would welcome any evidence CIA can provide that consumers are demanding indexed annuity products tied to, say, the Guggenheim RBP, CROCI Sectors III USD 5.5% VCI or BlackRock iBLD Claria® ER indexes. We would also welcome any evidence that consumers are clamoring for indexed annuities from producers who are prohibited from selling the underlying securities – if such securities even exist.

We turn now to specific issues raised by the Academy and CIA

### Business Cycle

Both the Academy and the CIA refer to the length of a business or economic cycle as a determinative basis for the length of the index existence requirement. This is a straw-man argument because the length of a business or economic cycle is not relevant for purposes of the disclosure model.

Key required information in the illustration is a demonstration of the worst ten-year period product results in the history of index. The purpose of the requirement is not to capture a business or economic cycle, as asserted by the Academy and the CIA, but to provide consumers with simple information about downside risk and associated product costs. It is a necessary counterpoint to the favorable scenarios highlighted by insurers and producers.

The current model renders this requirement meaningless by permitting products tied to indices in existence for just ten years to be illustrated – with the result that the all three required scales can produce essentially the same result and defeat the purpose of demonstrating variability in outcomes to consumers.

**The proposal to change the minimum time in existence for an index from 10 to 20 years is already a compromise.** Going back 20 years does not provide a lengthy time frame from which to select the best and worst ten year results. Nor does the requirement eliminate the problem of data mining recent historical returns to create a new index that will illustrate well, but has insufficient history to provide consumers with adequate information for an informed and empowered purchase decision.

**The industry argument for a 15-year minimum is not based on any consumer protection logic, but is simply an effort to retain as many indices as possible.** The Academy and CIA proposal for a 15-year prohibition time frame is based on the outcome for insurers – how many products will be affected – and ignores the consumer protection purpose of the requirement. Changing the prohibition time frame from 10 to 15 years does little to address the problem that the time frame is so short to preclude a meaningful worst case ten-year scenario. In fact, 20 years is too short to fulfil the purposes of model, but it represents a compromise.

The metric used by CIA and the Academy in opposition to a 20 year time frame prohibition is how many current indices will be affected. Industry employs the implicit assumption that all current products are good products and any elimination of current products is harmful to consumers. We strongly disagree with both the logic and implicit assumption of the industry argument. The consumer protection goal and the goal of insurers concerned with reputational risk should be to eliminate misleading illustrations based on products fabricated to produce such misleading illustrations. If the proposed changes to the model regulation eliminate the sale of such products because the use of a misleading illustration is no longer permitted, such a result benefits consumers. Such a result does not limit consumer choice any more for fixed indexed annuity products than certain requirements for producers – including criminal history checks and education requirements – limit consumer choice. Yes, imposing reasonable requirements on producers reduces the number of people eligible to sell insurance, but that is not a limit of consumer choice. And imposing restrictions on annuity illustrations to eliminate deceptive illustrations is not a limit on consumer choice.

**The CIA assertion that the proposed 20 year existence creates “operational burdens” and “disruption to existing products” is without merit – CIA itself contradicts the assertions.** CIA argues, without a scintilla of evidence, that the proposed 20 year existence would impose “operational burdens on the current illustration systems” and would cause “disruption to existing products.” Taking the second point first, the purpose of the proposed changes to the model is to disrupt existing products. By eliminating products designed to produce misleading illustrations, the proposed changes promote both consumer protection and fair competition – competition based on product design and insurer service and stability as opposed to a race to the bottom to create ever more fabulous illustrations.

**CIA undercuts and contradicts its assertions in opposition to the 20 year prohibition when it concludes that moving from a 10 year to a 15 year time in existence requirement “could be workable.”** According to CIA, somehow, annuity insurers can handle the “operational burdens” and “disruption” of moving to a 15 year time frame, but moving to 20 years would be insurmountable. Given the ability of insurers to routinely deploy new products and associated illustration systems, we find it implausible that the proposed changes will create significant “operational burdens” on the insurers. And we are certain that the cost of any such “operational burdens” pale in comparison to the consumer protection benefits of providing more reliable product information and eliminating products designed to produce misleading illustrations.

**CEJ suggests that in Section 6(F)(9)(b)(i) and (ii), the minimum time in existence for indexes that comprise be changed to 30 years for an index in existence for less than 20 years.** CEJ draws a significant distinction between an index that has been in existence for 20 years and a composite index comprised of other indices. For an index that has been in existence for 20 years, the opportunity for data mining favorable historical returns effectively does not exist because the index was created prior to current data mining practices. In contrast, with a composite index, there is the possibility of data mining over a recent 20-year time frame specific indices and weights to produce favorable illustrations. This difference is significant and logically leads to a longer time in existence for indexes used in a composite index.

**CEJ suggests that the time in existence requirement in Section 6(F)(9)(b) be changed from “has not been in existence for at least twenty (20) calendar years” be changed to “has not been in existence continuously since January 1, 1999.”** We suggest this change to better reflect the purpose of the time in existence limitation – to ensure meaningful results for best and worst product results over a ten-year period. The goal should be to expand the time frame for the calculation of best and worst ten year periods. CEJ’s proposal does this by starting at the draft’s proposed 20 year time in existence limitation – which would be approximately in existence continuously since 1999 – then expands this time frame over time.

In addition to the improved consumer protection of longer time frames to produce the critical best and worst ten year outcomes, the fixing of a starting date will create operational efficiencies for insurers. For example, if the worst ten year period is 1999 to 2008, why would we want to eliminate that data point for consumers as we move into 2020 and beyond? In addition, by setting a fixed starting date (instead of a rolling 20 year time frame) there should be fewer changes to best and worst ten year outcomes resulting in operational efficiencies for insurers and improved understanding by consumers.

Taken together, CEJ suggests the following for Section 6(F)(9), 6(F)(9)(a), 6(F)(9)(b) and 6(F)(9)(b)(i) and (ii) to reflect our recommendations:

(9) In determining the non-guaranteed illustrated values for a fixed indexed annuity, the index-based interest rate and account value shall be calculated for three different scenarios: one to reflect historical performance of the index for the most recent ten (10) calendar years; one to reflect the historical performance of the index for the continuous period of ten (10) calendar years from the beginning of the existence of the index through the most recent calendar year~~out of the last twenty (20) calendar years~~ that would result in the least index value growth (the “low scenario”); one to reflect the historical performance of the index for the continuous period of ten (10) calendar years from the beginning of the existence of the index through the most recent calendar year~~out of the last twenty (20) calendar years~~ that would result in the most index value growth (the “high scenario”). The following requirements apply:

(a) The most recent ten (10) calendar years and the most recent~~last twenty (20)~~ calendar years are defined to end on the prior December 31, except for illustrations prepared during the first three (3) months of the year, for which the end date of the calendar year period may be the December 31 prior to the last full calendar year;

(b) If any index utilized in determination of an account value has not been in existence continuously for at least the lesser of thirty~~twenty~~ (320) calendar years or since January 1, 1999, indexed returns for that index shall not be illustrated unless all of all of the following criteria are met:

(i) The index is a combination of indices, each of which has been in existence for at least twenty~~thirty~~ (230) calendar years;

(ii) The method of combination is such that a unique twenty~~thirty~~ (230) calendar year history of the index can be constructed;

The effect of CEJ’s proposed changes is to create now a 20-year time in existence requirement (January 1, 1999) which will increase over time to 30 years. The proposed changes to 6(F)(9), 6(F)(9)(a), 6(F)(9)(b), 6(F)(9)(b)(i) and 6(F)(9)(b)(ii) complement one another and provide a logical framework consistent with the purpose of the model regulation.

Thank you for your consideration.

## » The Many Indices Available on Indexed Annuities

**March 18, 2019 by Sheryl J. Moore**

Hi everyone. I have to make this short, as we are preparing 4Q2018 sales.

I recently participated in a call for the National Association of Insurance Commissioners (NAIC), regarding the matter of indexed annuities and the illustrations that accompany them.

For those who are interested, the following indices are available on indexed annuities today:

- (PM) London Gold Fixing Price
- 10-Year U.S. Treasury Bond
- Annuity Linked TVI Index
- Bank of America Merrill Lynch GPA Index
- Barclays All Caps Trailblazer 5 Index
- Barclays ARMOUR II Volatility Control Index
- Barclays Low Vol 5%
- Barclays Trailblazer Sectors 5
- BlackRock Diversa™ Volatility Control Index
- BlackRock Endura™
- BlackRock iBLD Ascenda
- BlackRock iBLD Claria Index
- BlackRock iBLD Claria® ER Index
- Bloomberg Barclays U.S. Agg Bond Index
- Bloomberg Commodity Index
- Bloomberg US Dynamic Balance II ER Index
- Bloomberg US Dynamic Balance Index II
- BNP Paribas High Dividend Plus
- BNP Paribas Momentum Multi Asset 5 Index
- BNP Paribas Multi-Asset Diversified 5 Index
- Citi Flexible Allocation 6 Excess Return
- CROCI Sectors II USD Index
- CROCI Sectors III USD 5.5% VCI
- CS Tactical Multi Asset
- Dow Jones Industrial Average
- Dow Jones U.S. Real Estate
- Euro Stoxx 50®
- Franklin US Index
- FT Balanced Capital Strength 6
- Gold Commodity
- GS Dynamo Strategy Index
- GS Momentum Builder® Multi-Asset Class Index
- GS Motif Aging of America Dynamic Balance
- Guggenheim RBP®
- Hang Seng

- iShares U.S. Real Estate
- iShares® U.S. Real Estate ETF
- Janus SG Market Consensus Index II
- Janus SG MC Index
- Janus Societe Generale Guidance
- JP Morgan ETF Efficiente® 5
- JP Morgan Mozaic II Index
- JP Morgan Strategic Balanced Index
- JP Morgan U.S. Sector Rotator 5 Index
- Merrill Lynch RPM Index™
- ML Strategic Balanced Index®
- Momentum Asset Allocator 5.5% VCI
- Morgan Stanley 3D Index
- Morgan Stanley Diversified Select Index
- Morgan Stanley Dynamic Allocation
- Morgan Stanley Dynamic Balance Index
- Morgan Stanley Global Opportunities Index
- Morningstar® Dividend Yield Focus Target
- MS Target Equity Balanced
- MSCI EAFE
- Multi-Strategy
- NASDAQ- 100®
- Nikkei 225
- NYSE® Expanded Opportunities™ Index
- NYSE® Zebra Edge®
- PIMCO Balanced Index
- PIMCO Global Optima Index™
- PIMCO Tactical Balanced ER Index
- PIMCO Tactical Balanced Index
- Russell 2000®
- S&P 500 Daily Risk Control 2 8%™ Index
- S&P 500 Daily Risk Control 5%™ Index
- S&P 500 Daily Risk Control 5%™ Total Return
- S&P 500 Daily Risk Control 7.5% (USD) ER
- S&P 500 Global BMI™
- S&P 500 Low Volatility DRC 5% ER
- S&P 500 Risk Control™
- S&P 500 Sector Rotator Daily Risk Control 2 5%
- S&P 500®
- S&P 500® Aristocrats Daily Risk Control 5% ER
- S&P 500® Aristocrats® Daily Risk Control 5%
- S&P 500® Average Daily Risk Control 10%
- S&P 500® Avg Daily Risk Control 10% Excess Return
- S&P 500® Dividend Aristocrats DRC 5% ER
- S&P 500® Low Volatility Daily Risk Control 5%
- S&P 500® Low Volatility Daily Risk Control 8%
- S&P MidCap 400®
- S&P U.S. Retiree Spending
- S&P® MARC 5% ER Index
- S&P® MARC 5% Index
- Shiller Barclays Cape US Sector Risk Controlled
- SPDR Gold Shares
- Strategic4 Index

- UBS Market Pioneers

While we anticipate releasing 4Q2018 indexed annuity sales tomorrow, I am able to preliminarily share that 2018 sales were just shy of \$68.5 billion. For fourth quarter sales alone (a nearly \$20 billion quarter), experienced record sales to hybrid indices- \$6.43 billion in sales.

Hybrid indices are indexes that are formed by one or more other indices, as well as a cash or bond component. They are frequently volatility-controlled and often proprietary.

I wish that I were able to research which, of these 90 indices, had 10 years of history, much less 20 years of history. I apologize that I am not in a position to provide this research, as not only am I trying to get sales out-the-door, but my father-in-law passed away a couple of days ago. I am busy making final arrangements for him at this time. While family is most important, this is an important matter and I have no doubt that one of the product manufacturers who has “a dog in the fight” on the matter of hybrid index illustrations will be able to lend the human resources to perform this research.

I welcome any credible information on this matter. Thank you! sjm