



May 10, 2019

Mr. Mike Yanacheak
Chair, Annuity Disclosure (A) Working Group
National Association of Insurance Commissioners

Re: Draft of Proposed Revisions to the NAIC Annuity Disclosure Model Regulation (#245)

Dear Mr. Yanacheak:

The Indexed Annuity Leadership Council (“IALC”)¹ appreciates the opportunity to comment on proposed revisions to the NAIC Annuity Disclosure Model Regulation (Model Regulation), relating to illustrations for fixed indexed annuities (FIAs), that was recently exposed by the NAIC Annuity Disclosure (A) Working Group.

The IALC is a consortium of life insurance companies that offer FIAs. IALC was established in 2011 with a mission to educate the public (including regulators) about the benefits of FIAs, which offer principal protection and a predictable, guaranteed retirement income, and can contribute balance to retirement savers’ long-term financial plans. Today, there is more than \$330 billion in FIA policies outstanding.

We have had the opportunity to review the proposed revisions to the NAIC Annuity Model Regulation, and offer our comments below.

- I. **The Exposure Draft’s proposal under Section 6(F)(9)(b) to increase the required index history from 10 to 20 years would preclude a majority of indices in the marketplace today from being illustrated.**

Approximately 70% of indices utilized today have historical data going back at least fifteen years. More than half of these do not have a full twenty years of history. While there are a variety of factors contributing to the limited history of these indices, one of the main factors is the available history of certain types of common index components, such as ETFs and excess return indices.

¹ The IALC is made up of Allianz Life Insurance Company of North America, American Equity Investment Life Insurance Company®, Athene USA, Midland National Life Insurance Company, and North American Company for Life and Health. It was established in 2011 with a mission to educate the public (including regulators) about the benefits of FIAs, which offer principal protection and a predictable, guaranteed retirement income, and can contribute balance to retirement savers’ long-term financial plans.



- ETFs are generally preferred over other types of index components because they are traded frequently, which makes them cheaper and more efficient to hedge, which allows more value to go to the policyholder. The first bond ETFs were introduced in 2002 with other ETFs (bond and stock) introduced throughout the 2000s.
- Excess return indices are generally preferred over total return or price return indices because of their stable option costs in relation to risk-free rates. While the option cost for total return and price return indices is highly dependent on the risk-free rate environment, option costs for excess return indices have no sensitivity to these rates. This leads to more predictable and stable index parameters for policyholders. The first excess return indices were introduced in 2000.

In addition to the above, volatility-controlled indices have become increasingly popular because equity volatility does not impact option costs. Targeting a lower volatility both increases caps and participation rates, and helps to provide more steady renewal rates. Many volatility-controlled indices use excess return indices because the option costs are insensitive to both equity volatility and risk-free rates. This is an important feature, especially considering that illustrations assume a constant cap and participation rate throughout the illustration.

A twenty-year history restriction would exclude these innovative indices and ETFs that offer a significant value to policyholders from being illustrated.

II. **The Exposure Draft’s proposal under Section 6(F)(9)(b)(i) requiring that an index be constructed entirely of a “combination of indices” is overly restrictive and should be revised to permit a “combination of underlying index components.”**

Section 6(F)(9)(b)(i) of the Exposure Draft would require an index to be constructed entirely of “a combination of indices, each of which has been in existence for at least twenty (20) calendar years.” When we began to review this proposed language, we became concerned that the use of “combination of indices” severely limits the options available for index construction, and may create unintended consequences that limit innovation, efficiency, and consumer choice. We instead would propose that the Working Group consider revising “combination of indices” to “combination of underlying index components” for the reasons stated below.

Index components utilized today, including ETFs, excess return indices, and futures contracts, would potentially be left out of consideration for illustrations under the current Exposure Draft. As stated above, these components have beneficial features that allow for more efficiency, stability and consumer value.

We recognize that “underlying index component” is not a defined term, and would thus support the creation of a Drafting Note that would provide additional clarity, particularly around the question of determining the start date for when an index component has been “in existence” for the requisite time period. This clarity is necessary to guide future regulators as well as regulated parties in developing a consistent standard that may be applied uniformly. Without the Drafting Note or further definition, there may be inconsistent applications in determining how long a component has been “in existence.”

In looking at the many index components utilized today as well as the consumer benefits of index innovation, we believe index component start date should be able to be determined in one of two ways, depending on the type of component: (1) In cases where the underlying index component has a clear published live date (not reliant on hypothetical data) the component start date would be the published live date. (2) In cases where the underlying index component is comprised solely of other underlying components, the index component start date is the date upon which each underlying component, standing on their own, have been in existence for the requisite time period and which also have a clear published live date of their own. To further summarize the above, here is a potential starting draft of a Drafting Note²:

DRAFTING NOTE:

An underlying index component is considered in existence so long as it (1) has a published live date exceeding the requisite X years or (2) the underlying index component is comprised solely of other underlying components, each of which, standing on their own, have a published live date exceeding the requisite X years.

We believe the revision from “underlying indices” to “underlying index components” will help avoid the unintended consequences listed above, and, combined with the clarifying information in the Drafting Note, will help regulators and regulated parties apply the standard uniformly.

III. If an algorithm or other method of combination is used to construct a Reference Index, Section 6(F)(9)(b)(iii) of the Exposure Draft would require that the algorithm or other method of combination be “fixed from the creation of the index.”

The IALC generally supports the proposed requirement that the algorithm or other method of combination be “fixed from the creation of the index.” The IALC is concerned that strict interpretation of the proposed requirement could prevent index sponsors from modifying

² As we developed this Drafting Note, we did not want to list the exact number of requisite years required, as we hope this issue is still under consideration. As we noted above, we believe 20 years to be excessive and unduly limiting.



algorithms or other methods of combining index components where modification becomes necessary in response to actions beyond the control of the index sponsor. For example, index sponsors were required to make such a modification as a result of LIBOR being phased out and numerous indices needing a suitable replacement benchmark.

Most index sponsors have rule-based governance structures in place that allow for the modification of the index when such a modification is necessary in response to a significant change to ensure continuation of the index. To preserve flexibility for index sponsors to modify algorithms and other methods of combination in response to significant events, the IALC recommends that the Working Group provide an exception to the proposed requirement that would allow index sponsors to modify algorithms or other methods of combination in response to significant events as permitted by the index sponsor's written governance policies. Index sponsors would be required to then make a written copy of their governance structures available to the Insurance Commissioner upon request.

Thank you for your time in considering our request.

Regards,

Jim Poolman
IALC Executive Director