Financial Security...for Life.

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Senior Actuary

February 21, 2020

Mr. Fred Andersen
Chair, NAIC IUL Illustration (A) Subgroup

Re: Exposed Edits to Actuarial Guideline 49

Dear Mr. Andersen:

The American Council of Life Insurers (ACLI)[1] appreciates the opportunity to submit the following comments on options proposed by the Indexed Universal Life (IUL) Illustration Subgroup (Subgroup) on its January 28th call.

ACLI has drafted proposed revisions (which are included as Attachment One). This draft incorporates ideas from many of the other versions that had previously been exposed. While there are open technical issues to be addressed through additional discussions and edits due to the time constraints, we believe this draft represents a significant step towards moving forward on the decisions previously made by the Life Actuarial (A) Task Force (LATF) and the Subgroup. We would appreciate the opportunity to discuss our draft on a future call, with the hope of having a more refined version for possible exposure during the NAIC Spring Meeting. We note the following from our draft:

- Consistent with our November 25, 2019 letter, ACLI does not generally support retroactive application of new regulatory guidelines. We have structured the exposure as AG 49-A, to be applicable to new business beginning after the effective date of the guideline. If regulators are comfortable with this approach, the existing AG 49 effective dates should be closed off for new business when AG 49-A applies. Retroactive application for inforce business may require significant rework to the existing AG 49, notably due to the current definition of Benchmark Index Account (BIA).
- In Section 3 (Definitions), we have added or modified definitions for Annual Net Investment Earnings Rate, Benchmark Index Account, Index Credits, Hedge Budget, and Supplemental Hedge Budget.
- This draft removes the notion of multiple BIAs and instead focuses on a single BIA.
- In Section 4 (Illustrated Rate), 4.B establishes the limit to the total percentage rate for Index Credits consistent with the votes taken by LATF and the Subgroup. References have been updated to refer to Index Credits.
- In Section 5 (Disciplined Current Scale), it limits assumed earned interest rate underlying the disciplined current scale to the Annual Net Investment Earnings Rate plus 45% times the lesser of Hedge Budget and the Annual Net Investment Earnings Rate, adjusted for time differences.

[1] The American Council of Life Insurers (ACLI) advocates on behalf of 280 member companies dedicated to providing products and services that promote consumers' financial and retirement security. 90 million American families depend on our members for life insurance, annuities, retirement plans, long-term care insurance, disability income insurance, reinsurance, dental and vision and other supplemental benefits. ACLI represents member companies in state, federal and international forums for public policy that supports the industry marketplace and the families that rely on life insurers' products for peace of mind. ACLI members represent 95 percent of industry assets in the United States. Learn more at www.acli.com.

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We note this approach may create differences in illustrated rates between products with and without multipliers at rates below the maximum. However, we believe this approach most cleanly addresses the main issues identified by regulators without introducing unnecessary complication in the language or perpetuating some of the uncertainty in the requirements.

- Section 6 (Policy Loans) has also been modified to clearly define the limits.

We look forward to a discussion of our proposed language. Thank you.

Sincerely,

cc Reggie Mazyck, NAIC

Actuarial Guideline XLIX-A – Draft

THE APPLICATION OF THE LIFE ILLUSTRATIONS MODEL REGULATION TO POLICIES WITH INDEX-BASED INTEREST SOLD AFTER [greater of 5 months after LATF adoption and 3 months after EX/Plenary Adoption*]

Background

The *Life Insurance Illustrations Model Regulation* (#582) was adopted by the NAIC in 1995. Since that time there has been continued evolution in product design, including the introduction of benefits that are tied to an external index or indices. Although these policies are subject to Model #582, not all of their features are explicitly referenced in the model, resulting in a lack of uniform practice in its implementation. In the absence of uniform guidance, two illustrations that use the same index and crediting method often illustrated different credited rates. The lack of uniformity can be confusing to potential buyers and can cause uncertainty among illustration actuaries when certifying compliance with Model #582.

In 2018, the NAIC decided that illustrations of products with multipliers, cap buy-ups, and other enhancements should illustrate no better than products without such features. This new requirement is intended to apply to illustrations on policies sold on or after the effective date of this guideline while the existing requirements continue to apply for inforce illustrations on policies sold before the effective date of this guideline.

This guideline provides uniform guidance for policies with index-based interest. In particular, this guideline:

(1) Provides guidance in determining the maximum crediting rate for the illustrated scale and the earned interest rate for the disciplined current scale.

(2) Limits the policy loan leverage shown in an illustration.

(3) Requires additional consumer information (side-by-side illustration and additional disclosures) that will aid in consumer understanding.

Text

1. Effective Date

This Actuarial Guideline shall be effective for all new business and in force illustrations on policies sold on or after [greater of 5 months after LATF adoption and 3 months after EX/Plenary Adoption].~~as follows:~~

~~i. Sections 4 and 5 shall be effective for all new business and in force life insurance illustrations on policies sold on or after September 1, 2015.~~

~~ii. Effective March 1, 2017, Section 4 and Section 5 shall be effective for all in-force life insurance illustrations on policies within the scope of this actuarial guideline, regardless of the date the policy was sold.~~

~~iii. Sections 6 and 7 shall be effective for all new business and in force life insurance illustrations on policies sold on or after March 1, 2016.~~

2. Scope

This Actuarial Guideline shall apply to any life insurance illustration that meets both (i) and (ii), below:

i. The policy is subject to Model #582.

ii. Indexed Credits~~Interest credits~~ are linked to an external index or indices.

3. Definitions

A. Alternate Scale: A scale of non-guaranteed elements currently being illustrated such that:

i. The total percentage rate of Indexed Credits~~credited rate~~ for each Index Account does not exceed the lesser of the maximum total percentage~~credited~~ rate of Indexed Credits for the illustrated scale less 100 basis points and the credited rate for the Fixed Account. If the insurer does not offer a Fixed Account with the illustrated policy, the total percentage rate of Indexed Credits~~credited rate~~ for each Index Account shall not exceed the average of the maximum total percentage~~credited~~ rate of Indexed Credits for the illustrated scale and the guaranteed total percentage~~credited~~ rate of Indexed Credits for that account. However, the total percentage rate of Indexed Credits~~credited rate~~ for each Index Account shall never be less than the guaranteed total percentage~~credited~~ rate for that account.

ii. If the illustration includes a loan, the total illustrated Indexed Credits for~~rate credited to~~ the loaned portion of the index account do~~loan balance does~~ not exceed the corresponding illustrated loan charge. For example, if the illustrated loan charge is 4% loan Indexed Credits cannot exceed 4%, regardless of product features available.

iii. All other non-guaranteed elements are equal to the non-guaranteed elements for the illustrated scale.

B. Annual Net Investment Earnings Rate: Gross portfolio annual earnings rate, less provisions for investment expenses and default cost, of the general account assets (excluding hedges for Indexed Credits) allocated to support the policy. Any Supplemental Hedge Budget is not included in the Annual Net Investment Earnings Rate.

~~B.~~C. Benchmark Index Account: An Index Account with the following features:

i. The interest calculation is based on the percent change in S&P 500® Index value only, over a one-year period using only the beginning and ending index values. (S&P 500® Index ticker: SPX)

ii. An annual cap is used in the interest calculation.

iii. The annual floor used in the interest calculation shall be 0%.

iv. The participation rate used in the interest calculation shall be 100%.

v. Interest is credited once per year.

vi. Account charges do not exceed the account charges for any corresponding Index Accounts within the policy in any policy year. ~~If Index Accounts with different levels of account charges are offered with the illustrated policy, more than one Benchmark Index Account may be used in determining the maximum illustrated crediting rates for the policy's Index Accounts, subject to the requirements of 5.D.. However, for each Index Account within the policy, only one Benchmark Index Account shall apply. Any rate calculated in 4 (B) shall not apply for an Index Account if the account charges for the applicable Benchmark Index Account exceed the account charges for that Index Account in any policy year.~~ Account charges include all charges applicable to an Index Account, whether deducted from policy values or from premiums or other amounts transferred into such Index Account.

vii. Additional amounts credited are not less than the additional amounts credited for any corresponding Index Accounts within the policy in any policy year. ~~Any rate calculated in 4 (B) shall not apply for an Index Account if the additional amounts credited for the applicable Benchmark Index Account are less than the additional amounts credited for that Index Account in any policy year.~~ Additional amounts include all credits that increase policy values, including but not limited to experience refunds or bonuses.

viii. There are no limitations on the portion of account value allocated to the account.

~~C.~~D. Fixed Account: An account where the credited rate is not tied to an external index or indices.

~~D.~~E. Index Account: An account where the credited rate is tied to an external index or indices.

F. Indexed Credits: Any interest credit, multiplier, factor, bonus, or other enhancement to policy values that is linked to an external index or indices.

G. Hedge Budget: The total amount assumed to be used to hedge the Indexed Credits of the account, expressed as a percent of the policy's index account value.

H. Supplemental Hedge Budget: The Hedge Budget minus the Annual Net Investment Earnings Rate plus the annual floor for the Index Account, not less than zero.

4. Illustrated Scale

The credited rate for the illustrated scale for each Index Account shall be limited as follows:

A. Calculate the geometric average annual credited rate for the ~~each applicable~~ Benchmark Index Account for the 25-year period starting on 12/31 of the calendar year that is 66 years prior to the current calendar year (e.g., 12/31/1949 for 2015 illustrations) and for each 25-year period starting on each subsequent trading day thereafter, ending with the 25-year period that ends on 12/31 of the prior calendar year.

i. If the insurer offers a~~an applicable~~ Benchmark Index Account with the illustrated policy, the illustration actuary shall use the current annual cap for the ~~applicable~~ Benchmark Index Account in 4 (A).

ii. If the insurer does not offer a~~an applicable~~ Benchmark Index Account with the illustrated policy, the illustration actuary shall use actuarial judgment to determine a hypothetical, supportable current annual cap for a hypothetical, supportable Index Account that meets the definition of the~~a~~ Benchmark Index Account, and shall use that cap in 4 (A).

B. For the~~each applicable~~ Benchmark Index Account the total percentage rate of Indexed Credits for the illustrated scale shall not exceed the minimum of (i) and (ii), added to (iii):

i. the arithmetic mean of the geometric average annual credited rates calculated in 4 (A)

ii. the assumed earned interest rate underlying the disciplined current scale in 5 (A) or 5 (B), as applicable

iii. the Supplemental Hedge Budget

~~B.~~C. The above limit applied to the percentage rate of Indexed Credits prior to the deduction of any charges used to fund the Supplemental Hedge Budget~~the maximum credited rate(s) for the illustrated scale~~.

The interest rate shown that is referenced in section 6 (C) of Model #582 shall be the minimum of 4 (B) (i) and 4 (B) (ii).

~~C.~~D. For other Index Accounts using other equity, bond, and/or commodity indexes, and/or using other crediting methods, the illustration actuary shall use actuarial judgment to determine the maximum total percentage~~credited~~ rate of Indexed Credits for the illustrated scale. The determination shall reflect the fundamental characteristics of the Index Account and the parameters shall have the appropriate relationship to the expected risk and return of the ~~applicable~~ Benchmark Index Account. In no event shall the total percentage~~credited~~ rate of Indexed Credits for the illustrated scale exceed the total percentage~~applicable~~ rate of Indexed Credits calculated in 4 (B).

~~D.~~E. At the beginning of each calendar year, the insurer shall be allowed up to three (3) months to update the credited rate for each Index Account in accordance with 4 (B) and 4 (C).

5. Disciplined Current Scale
The earned interest rate for the disciplined current scale shall be limited as follows:

A. If an insurer engages in a hedging program for Indexed Credits~~index-based interest~~, the assumed earned interest rate underlying the disciplined current scale for the policy, inclusive of all hedge or derivative assets that support Indexed Credits and all other investments that support the policy shall not exceed:

i. the Annual Net Investment Earnings Rate, plus

ii. 45% of the lesser of the Hedge Budget and the Annual Net Investment Earnings Rate, adjusted for timing differences to ensure that fixed interest is not earned on the hedge cost

Neither the hedge cost nor the hedge return are included as separate cash flows. The Supplemental Hedge Budget is not added because the hedge cost is not modeled as an expense.

~~A.~~B. If an insurer does not engage in a hedging program for index-based interest, the assumed earned interest rate underlying the disciplined current scale shall not exceed the annual net investment earnings rate of the general account assets allocated to support the policy.

~~B.~~C. These experience limitations shall be included when testing for self-support and lapse-support under Model #582, accounting for all benefits including illustrated bonuses.

~~C.~~D. If more than one Benchmark Index Account is used for an illustrated policy, each set of Index Accounts that correspond to each Benchmark Index Account must independently pass the self-support and lapse-support tests under Model #582, subject to the limitations in 5 (A), (B), and (C). All experience assumptions that do not directly relate to the Index Accounts as to expenses, mortality, investment earnings rate of the general account assets, lapses, and election of any Fixed Account shall equal the assumptions used in the testing for the entire policy.

6. Policy Loans

If the illustration includes a loan, the total illustrated Indexed Credits for~~rate credited to~~ the loaned portion of the index account value~~loan balance~~ shall not exceed the illustrated loan charge by more than 100 basis points. For example, if the illustrated loan charge is 4%, loan Indexed Credits cannot exceed 5%, regardless of product features available.

7. Additional Standards

The basic illustration shall also include the following:

A. A ledger using the Alternate Scale shall be shown alongside the ledger using the illustrated scale with equal prominence.

B. A table showing the minimum and maximum of the geometric average annual credited rates calculated in 4 (A).

C. For each Index Account illustrated, a table showing actual historical index changes and corresponding hypothetical Indexed Credits~~interest rates~~ using current index parameters for the most recent 20-year period.

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