December 4, 2019

Mr. Fred Andersen
Chair, IUL Illustration (A) Subgroup
National Association of Insurance Commissioners

Dear Mr. Andersen,

On behalf of the American Academy of Actuaries\(^1\) Life Illustrations Work Group (the “Work Group”) I appreciate the opportunity to provide comments and insight on the questions posed on November 15, 2019 by the IUL Illustration Subgroup regarding the illustrations of Indexed Universal Life (IUL) insurance policies under Actuarial Guideline 49 (AG 49).

1. **Section 3.C., to address a potential concern that product enhancements with charges could be interpreted as a benchmark.**

   The Work Group suggests modification to Section 3.C.vi. to clarify that multipliers will not create additional Benchmark Index Account(s). Additional clarification might be needed if the intent is that additional Benchmark Index Accounts are only for products with different levels of account charges that offer different levels of cap rates.

   Regarding Section 3.G, the Work Group also suggests that the definition of *Supplemental Option Budget* be modified to be *Supplemental Hedge Budget*, to allow for consistency of wording within AG 49 (Sect 5, “companies engaging in a hedging program”) and to recognize the use of hedge instruments other than options.

2. **Section 4.E., to ensure relevance and consistency with Section 5 in light of changes to Section 5 and to ensure the coordination with Sections 4A and 4B to produce a clear and appropriate calculation.**

   The introduction in the draft AG 49 of the definition of *Supplemental Hedge Budget* and Section 4.E., along with the current AG 49 wording of Section 3.C.vi have complicated how products with different levels of account charges are considered within AG 49. If Section 4.E is intended only to apply to supplemental hedge budgets that provide enhancements to the account value after the Benchmark Indexed Account (BIA) crediting rate (such as multipliers) has been calculated and does not include cap buy-ups which apply an elevated cap to the

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\(^1\) The American Academy of Actuaries is a 19,500-member professional association whose mission is to serve the public and the U.S. actuarial profession. For more than 50 years, the Academy has assisted public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.
crediting rate (and are therefore already limited by the BIA in Section 4), then Section 4.E.
(and 3.C.vi. as stated in 1 above) will need to be modified to appropriately reflect that.

The Work Group also suggests that some adjustment be allowed to overcome timing
differences between charges and credits for multiplier products. Adding language that allows
the illustrated credits to be sufficient to enable the cash value of a multiplier product to equal
that of a non-multiplier product could be reasonable. Therefore, we offer the following
potential changes to Section 4.E:

*If charges that fund a Supplemental OptionHedge Budget are deducted from the illustrated
cash account value and have not been used to develop additional Benchmark Index
Accounts, then Indexed Credits generated by the return from the Supplemental OptionHedge
Budget within the scenario being illustrated may be illustrated up to [amount adjusted for
timing differences].*

3. Section 5B (new part of Section 5), to ensure:
   a. Inappropriate double counting of credits or charges is avoided;
   b. Clarity is added, including defining the new term “net” in 5B(A); and
   c. Cap buy-ups are appropriately addressed.

Supplemental math examples may be provided to add clarity.

The Work Group suggests a drafting note could be useful in clarifying application of the
145% principle.

The Work Group is providing examples of results to assist in clarification, if needed, on how
Section 5B DCS* earned rates are be calculated, showing both gross and net earned rates, as
shown below.

* (DCS) disciplined current scale

<table>
<thead>
<tr>
<th>Scenario</th>
<th>Non-Multiplier</th>
<th>Multiplier</th>
<th>Cap Buy-up</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cap</td>
<td>11%</td>
<td>11%</td>
<td>13.5%</td>
</tr>
<tr>
<td>Section 4 Benchmark Index Account Credited Rate</td>
<td>6.58%</td>
<td>6.58%</td>
<td>7.35%</td>
</tr>
<tr>
<td>Supplemental Hedge Budget</td>
<td>0.00%</td>
<td>2.00%</td>
<td>0.50%</td>
</tr>
<tr>
<td>Section 4 Maximum Illustrated Rate</td>
<td>6.58%</td>
<td>8.58%</td>
<td>7.35%</td>
</tr>
<tr>
<td>Net Illustrated Rates</td>
<td>6.58%</td>
<td>6.58%</td>
<td>6.85%</td>
</tr>
</tbody>
</table>

Annual Net Investment Earnings Rate | 4.55% | 4.55% | 4.55% |

145% multiple | 6.60% | 6.60% | 6.60% |

+ Supplemental Hedge Budget | 0.00% | 2.00% | 0.50% |

= Gross Section 5 Disciplined Current Scale Earned Rate | 6.60% | 8.60% | 7.10% |

- Supplemental Hedge Budget | 0.00% | 2.00% | 0.50% |

= Net Section 5 Disciplined Current Scale Earned Rate | 6.60% | 6.60% | 6.60% |
The Work Group believes that cap buy-up products are not being considered in the current revisions of AG 49 since Section 3.G.vi. of AG49 results in the creation of a separate Benchmark Index Account for cap buy-up products. If the intent of the revisions is indeed to focus solely on multiplier type features, potential future issues associated with illustrations of such cap buy-up accounts should be considered. Under the revised wording, cap buy-up accounts may be able to be illustrated at rates higher than accounts without the charges associated with the higher cap as can be seen in scenario 3 in the table above. In this scenario, the net effective illustrated rate would be higher than the earned rate underlying the DCS although it is unclear if an insurer would be able to pass the DCS testing. An additional consideration in the final illustrated rate is detailed in Section 6C of the Model Regulation 582 which states, “If an interest rate used to determine the nonguaranteed elements is shown, it shall not be greater than the earned rate underlying the disciplined current scale.”

The Work Group believes the application of Section 6C to new business could be unclear as to whether it limits the rate as shown on the illustration, or the rate actually being used in the calculation of the illustration’s values. We believe these scenarios should be more fully considered and vetted before finalizing any AG49 revisions.

4. **Section 6B to ensure the 100 basis point loan limits is applied as intended.**

The Work Group suggests that the wording in 3.A.ii and 6B be consistent, with the only difference being that 3.A.ii not allow for the 100 bps differential between the charges and the credits.

In general, the Work Group notes that the approach used in the exposed draft AG 49 results in increased complexity for both the illustration actuary and the consumer. The Work Group has discussed alternative paths that might be less complex but would allow for higher illustrated values for multiplier products than non-multiplier products. The Work Group would be happy to share further thoughts on alternatives should that route wished to be discussed.

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The Work Group appreciates the efforts of the IUL Illustration Subgroup to review AG 49. We would be happy to provide more specific suggested wording but would need an exposure period of more than ten days to ensure that we provide you quality comments. If you have any questions or would like further dialogue on the above topics, please contact Ian Trepanier, life policy analyst, at trepanier@actuary.org.

Sincerely,

Donna Megregian, MAAA, FSA
Chairperson, Life Illustrations Work Group
American Academy of Actuaries