



Illinois Department of Insurance

PAT QUINN
Governor

MICHAEL T. McRAITH
Director

May 6, 2011

Karen Z. Schutter, Executive Director
Interstate Insurance Product Regulation Commission
444 North Capitol Street, NW
Hall of the States, Suite 701
Washington, DC 20001-1509

Re: Illinois Department of Insurance Review of Adopted Interstate
Compact (IC) Standards.

Dear Ms. Schutter:

As you know, the Illinois Department of Insurance (IDOI) is currently in the process of reviewing the 69 adopted IC standards. We have completed a first review and this letter summarizes IDOI's progress and the issues that remain outstanding.

The outstanding issues concern the standards for products that utilize a separate account and products that include market value adjustment features. We do not believe these issues are unique to Illinois. Over the years companies have continued to develop innovative products with risk profiles that do not fit squarely within the current definitions of "variable" and non-variable." Such products may have guarantees and the reserves for the guarantees may be held in either "insulated" or "non-insulated" separate accounts. Indexed products are not strictly "equity-indexed" anymore. Some of the laws and regulations that have not changed for several years have become more difficult to interpret as the lines blur. While we support innovation, as regulators we must preserve the ability to ensure financial solvency and protect consumers.

Except with respect to IIPRC-LTC-I-3-RATEM Rate Schedules for Individual Long-Term Care Insurance – Modified Rate Schedules, we believe we can implement in Illinois 55 of the 69 standards that have been adopted by the IC as of the date of this letter. Specifically regarding IIPRC-LTC-I-3-RATEM, Illinois is not opting out of this standard but we are notifying the Commission that we do not permit Modified Rate Schedule filings. With respect to "mix and match," IC staff has confirmed Illinois' understanding of the Compact's Operating Procedure For The Filing And Approval Of Product Filings that a state component that has not been approved by the IC cannot be used in other states that have also not approved the component simply by the component's being attached to a filing that has been approved by the IC.

The remaining standards are problematic and fall into two groups – twelve standards for products utilizing a separate account (SA) and one for products sold in a general account that contain a market value adjustment feature. Specifically these standards are:

- IIPRC-L-06-I-1 Individual Modified Single Premium Variable Life Insurance Policy Standards;
- IIPRC-L-06-I-3 Individual Modified Single Premium Joint First to Die Variable Life Insurance Policy Standards;
- IIPRC-L-06-I Individual Flexible Premium Variable Adjustable Life Insurance Policy Standards;
- IIPRC-L-06-I-2 Individual Joint Last to Die Survivorship Flexible Premium Variable Adjustable Life Insurance Policy Standards;
- IIPRC-A-03-I Core Standards for Individual Deferred Variable Annuity Contracts;
- NO CODE Individual Fixed Premium Deferred Variable Annuity Contract Standards (with Separate and General Accounts);
- NO CODE Individual Flexible Premium Deferred Variable Annuity Contract Standards (with Separate and General Accounts);
- NO CODE Individual Immediate Variable Annuity Contract Standards;
- IIPRC-A-03-I-GLB Additional Standards for Guaranteed Living Benefits for Individual Deferred Variable Annuities;
- IIPRC-AB-I-GMDB Additional Standards for Guaranteed Minimum Death Benefits for Individual Deferred Variable Annuities;
- IIPRC-A-03-I-BONUS Additional Standards for Bonus Benefits for Individual Deferred Variable Annuity Contracts;
- IIPRC-A-07-I-3 Additional Standards for Market Value Adjustment Feature Provided Through a Separate Account; and
- IIPRC-A-07-I-2 Additional Standards for Market Value Adjustment Feature Provided Through a General Account.

Respectfully, IDOI does not accept that these standards adequately address many of the issues surrounding SA, and likely conflict with Illinois' SA law (215 ILCS 5/245.21). For example, Illinois law provides that SA assets equal to reserves and other liabilities must be insulated, and that reserves for guaranteed benefits may not be held in an SA absent the explicit approval of the Director. The standards lack guidance on whether the SA assets may be insulated or non-insulated, or whether separate Director approval is required for products in which reserves supporting guarantees are held in an SA. Similarly, the standards do not

recognize that the SA laws existing in Illinois provide the Director with additional discretion over Illinois' domestic insurers regarding book value versus market value accounting, approval of asset transfers between the general and SA's and the imposition of requirements with respect to guarantees relating to SA products.

Additionally, state laws regarding SA products and nonforfeiture depend upon the definitions of "fixed" versus "variable" contracts; however, these terms are not clearly defined in the standards. These ambiguities and divergences in the standards from Illinois law directly impact consumer rights, and are likely to result in policyholder litigation if not properly resolved prior to implementation.

These and similar issues are presently being reviewed by various NAIC groups including the Life Actuarial Task Force (LATF), Separate Account Risk Charge (E) Working Group, and the Receivership and Insolvency Task Force. On the last call of the IC's Actuarial Working Group (AWG) it was recommended that existing standards be re-opened and these issues be addressed.

Illinois offers the following observations:

- 50 Illinois Administrative Code Part 1451 defines a "variable contract" as "a contract which provides benefits that vary according to the investment experience of any separate account or accounts maintained by the insurer as to such contract." Any contract (or portion thereof) that does not meet this definition is considered "non-variable." The IDOI recommends consideration of these or similar definitions and would support further clarification that a "variable contract" essentially means "unitized." In our view broader definitions of "variable" result in the exclusion of some guaranteed contracts from the annuity nonforfeiture law without changing the express language of the (model) law itself.
- Under Illinois law an SA must be insulated; that is, its assets equal to reserves and other liabilities cannot be charged with the liabilities from any of the company's other business. However, when reserves supporting guarantees are held in an insulated SA this creates a preferred class of policyholders in the case of insolvency. In other words, the policyholders who have premiums invested in these guarantees would be paid ahead of policyholders who have premiums invested in guarantees in the general account.

For these reasons, Illinois is concerned with standards that explicitly or implicitly allow for assets supporting reserves for guaranteed benefits to be held in an insulated SA. Illinois would consider supporting IC standards allowing guarantees in non-insulated SA's that would not create a preferred class of policyholders, but believes compliance with general account nonforfeiture requirements should be required. Also, given the complexity of these products, other ramifications of non-insulated SA's would require additional consideration.

The remaining standard about which Illinois has concerns is:

- Additional Standards for Market Value Adjustment Features Provided Through General Accounts.

This standard does not require compliance with the prospective minimum nonforfeiture requirement in the Standard Nonforfeiture Law for Individual Deferred Annuities. The Standard should require compliance without incorporating the market value adjustment into the test, thus preserving smoothly declining surrender charges.

Illinois believes the above-described issues should be further explored and resolved on a national level so the most uniform result will be achieved. Illinois looks forward to participating in this on-going national dialogue and unequivocally supports the IC's continued efforts to promote uniform national standards. Given the early stages of much related dialogue, IDOI cannot make an informed and final determination on whether to opt-out of the thirteen standards at this time. Section 104(g) of the IIPCRC, Operating Procedures For Providing Notice of Opt-Out Of Uniform Standard By Regulation And For Submission And Consideration Of Petitions For Stay Of Uniform Standard, allows for a Compacting State to request for extension of a stay to exceed one year upon demonstration of extraordinary circumstances warranting continuance of the stay. Given the significance of the issues identified above, Illinois believes that such extraordinary circumstances presently exist. IDOI accordingly requests an extension of the stay of the standards described herein until such time as the issues concerning such standards have been fully resolved by the NAIC.

Sincerely, .



Michael T. McRaith
Director of Insurance

cc: The Honorable Roger Sevigny
Commissioner, State of New Hampshire