DATE: **January 31, 2024**

TO: **Insurance Compact Management Committee**

FROM: **Product Standards Committee**

RE: **Index Linked Variable Annuity Contract (ILVA) Uniform Standards Amendments to the Additional Standards for Market Value Adjustment Feature Provided Through A Separate Account**

The Product Standards Committee ("PSC") of the Interstate Insurance Product Regulation Commission ("Commission") is charged with developing proposed drafts of Uniform Standards. In carrying out its charge, the PSC has finalized the following draft uniform standards in the individual annuity product line. The PSC is recommending that the Management Committee initiate the rulemaking procedure[1] with respect to these proposed uniform standards:

- Standards for Individual Deferred Index Linked Variable Annuity Contracts ("ILVA Standards")
- Amendments to the Additional Standards for Market Value Adjustment Feature Provided Through A Separate Account ("MVA Standard")

This recommendation is to initiate the rulemaking process with respect to these two uniform standards.

The Committee recommends these uniform standards be available for Mix and Match to be used in combination with State Product Components as described in §111 of the IIPRC Operating Procedure for the Filing and Approval of Product Filings. The PSC also recommends that filings submitted under these Uniform Standards continue to be subject to prior review and approval and not self-certification.

The Product Standards Committee (PSC) formed a drafting subgroup to develop the initial drafts of the ILVA Standards**.** The subgroup exposed a first draft and held a public call on May 8, 2023, to receive comments. The subgroup prepared a second draft based on the comments received and asked for comments. The subgroup revised the draft and submitted the third draft to the PSC along with amendments to the *Individual Annuity Application Standards* and the MVA Standard.

[1] The rulemaking procedure is set forth in the *Rule for Adoption, Amendment and Repeal of Rules for the Interstate Insurance Product Regulation Commission*.

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The Product Standards Committee held a public call on December 12, 2023, to receive comments. The PSC received written comments from ACLI, the Coalition of Annuity Insurers (CAI), the Insured Retirement Institute (IRI), and the American Academy of Actuaries (AAA). The PSC made edits based on the comments received. The compilation of comments and the PSC response is attached to this memo.

Based on the comments, the PSC is not recommending amendments to the *Individual Annuity Application Standard*, which were originally included in the ILVA Subgroup draft. The ILVA Subgroup added a requirement to add an acknowledgment in applications for ILVAs that the applicant was shown a comparison with other types of annuities. Comments and concerns were raised that proposed comparison was too limited to be of value to consumers; states did not have a comparable application requirement; and, some companies did not offer all of the product types being compared, so there would not be a level playing field among the comparisons. The PSC concluded the acknowledgement was not needed due to state statutory best interest requirements, suitability oversight of the states, and product information disclosure requirements.

Further, the PSC recommendation includes amending the title of the MVA Standard as follows *Additional Standards for Market Value Adjustment Feature for Modified Guaranteed Annuities and Index Linked Variable Annuities*.

The PSC did not consider whether to include other interim value approaches as this has been fully vetted at the ILVA subgroup and is a policy decision for the Commission. The recommendation follows the NAIC Actuarial Guideline 54, other than the ILVA Standards do not permit for material consistent interim value approaches and only allows for the hypothetical portfolio approach. This public policy issue was raised to the Commission during the joint meeting of the Management Committee and Commission at its in-person meeting on August 15, 2023.

Given the extensive, transparent, and documented drafting process preceding these recommendations, the PSC suggests that any additional comments or concerns about these recommended Uniform Standards be raised, considered, and discussed by all members and interested parties during the Management Committee's formal rulemaking process.

The PSC is available to respond to any questions or requests for information to assist the Management Committee.

Product Standards Committee Response to

Public Comments on November 14, 2023 Exposure Draft of ILVA Standards

Prepared by Compact Office

NOTE: The following are in the order presented in each of the comment letters. All changes in the November 14, 2023 draft were accepted and the January 16, 2023 draft tracks only the revisions as discussed below.

American Academy of Actuaries Comments Dated December 8, 2023

1. Is the intent of Section 1. B. 1.(g) (ii) to offer a symmetrical MVA for all applications of Interim Value? If so, we would request additional clarification of that intent.

Response: In addition to the requirement in Section 1.B.1.(g)(ii), Section 1.B.1.(g)(i) requires certification that the MVA also produce results reasonably similar to changes in the market value of the hypothetical fixed income asset and the MVA formula must provide for reasonable equity between the contract holder and insurance company. Members determined that the requirements for the MVA were clear and no revision was needed.

2. Additional clarification as to the purpose of Appendix C since the Interim Value would be equal to or substantially similar to the market value of the Hypothetical Portfolio. Would an actuarial certification be sufficient instead?

Response: See response to ACLI/CAI Comment I.2 regarding revisions to Appendix C. It is expected that the values will be close to zero. However, members felt that this information would be helpful to the Compact reviewer in determining compliance with the hypothetical portfolio methodology. Therefore, Appendix C was retained.

3. The amendments to the Additional Standards for Market Value Adjustments should apply solely to Modified Guaranteed Annuities and Index-Linked Variable Annuities.

Response: See response to ACLI/CAI comments in Comment II.5 below

ACLI/CAI Comments Dated December 10, 2023

I.1 Need for revisions to Sections 3(C) (Assignment) and 3(U) (Ownership) to allow restrictions on assignments and ownership changes to accommodate SEC Rule 12h-7.

Response: The revisions in the November 14, 2023 draft were retained and "or successor regulations" was added to address the potential for future revision to the SEC

Rule and desires by members to avoid needing to update the Standard for such revision.

I.2 Minor revisions to Appendix C – Illustration Examples of Interim Value Methodology

Response: Accepted proposed revisions to account for trading costs and to remove the reference to market value in the heading since the Hypothetical Portfolio Return may or may not be adjusted by a market value adjustment.

I.3 Remove Application Standard Acknowledgement

Response: The revision to the Application Standard to include an acknowledgement was removed. Members agreed that the acknowledgement was not needed due to state statutory best interest requirements, suitability oversight of the states, and product information disclosure requirements. The members reviewed information about the new SEC requirements for ILVA specific disclosures in Form N-4 that will be required by June 1, 2024 for ILVAs/RILAs. The disclosures highlight the key features of ILVAs/RILAs that may substantially differ from other investment products which was the primary purpose of the acknowledgement. In addition, members were concerned with the potential for an unlevel playing field between companies that have comparison products and companies that do not have comparison products.

Comment II.1.--- Allow fixed account MVA to not comply with Model 805

Response: The non-variable account value in a variable annuity is subject to the minimum nonforfeiture value floor after any MVA consistent with Model 250 and the Variable Annuity Compact standard. This same principle was applied to ILVAs in the draft standard so that non-variable account value must comply with the minimum nonforfeiture requirements including any MVA. Members consider this an important consumer protection, and no change was made to draft standard and the non-variable account value must comply with Model 805 after any MVA.

Comment II.2.--- Clarify permissible duration in the determination of the MVA

Response: Accepted correction to MVA definition and revision to Drafting Note under Section 1.B.1.(d)(vii)(3) as follows:

"Market Value Adjustment (MVA)" means a positive or negative adjustment applied to the fixed income asset proxy or strategy value in order to reflect an increase or decrease in the value of **the hypothetical fixed income assets** ~~fixed income assets held by the company supporting the ILVA~~;

Added "**The determination of the MVA in i above may be based on the duration of the Index Strategy Term, surrender charge period, or the fixed income assets backing the ILVA**" to the Drafting Note.

Comment II.3 Clarify requirement for Index substitution

<u>Response</u>: Members recognized that a comparable index may not be available and should be addressed. In addition, members had concerns with the unlimited discretion for the insurer to discontinue an index in this provision in the draft standard, particularly if the index was a reason for a consumer to select a particular ILVA product. The members concluded that by keeping the "may", the Standard should set forth limitations on when an insurer may discontinue an index to provide consumer safeguards. Taking this into consideration along with both the current and prior ACLI/CAI comments on this section, the following revisions were made to the section:

K. DISCONTINUATION OF OR SUBSTANTIAL CHANGE TO AN INDEX

*(1) The contract shall contain a provision indicating the conditions under which a company may discontinue an index and what occurs when an index is discontinued, with the provision being labeled as such. The provision shall state that if the company discontinues an index, the company will substitute a comparable index**<u>, if available</u>**. The contract shall also specify that, before a substitute index is used, the company shall notify the owner and any assignee of the substitution.*

(2) Each index used in determining amounts credited to the contract including any index substituted for another index under this section is subject to prior approval by the IIPRC.

<u>(3) The conditions under which a company may discontinue an index include discontinuation of the index, unavailability of index values, substantial change in the calculation of an index, loss of a company's license or permission to use an index, inability to hedge risks associated with the index, or similar conditions approved by the Interstate Insurance Product Regulation Commission.</u>

Comment II.4 Clarify Separate Account disclosure requirement

<u>Response</u>: Accepted correction to move the requirement in Subsection 3(AA)(1)(d) "If there is no readily available market for assets in the separate account, then the contract shall specify how the assets would be valued" to Section 3(AA)(2) so that it is only applicable to variable accounts.

Comment II.5 Minor updates to Additional Standards for Market Value Adjustment Feature Provided Through a Separate Account (IIPRC-A-07-I-3)

<u>Response</u>: Accepted correction to the title to reference Modified Guaranteed Annuities and Index Linked Variable Annuities and to strike "modified guaranteed" in Section 3(G)(1)(b)

IRI Comments Dated December 7, 2023

Comment: Significant concerns with new provision in the application standard and believe new provision would only cause confusion and is ultimately unnecessary.

Response: See response to ACLI/CAI Comment I.3.

Comment: Allow other interim value approaches that are determined to be materially consistent with the hypothetical portfolio methodology.

Response: Although AG 54 allows other methodologies that are determined to be materially consistent with the hypothetical portfolio methodology, material consistency remains without objective definition. The Product Standards Committee and ILVA Subgroup recommend to the Management Committee that in the absence of a definition of material consistency agreeable to Compacting states, the products filed under the Compact ILVA standard will need to use the hypothetical portfolio methodology.

Additional Revision based on a company question about the MVA requirements in the November 14, 2023 draft

Response: Clarify in Drafting Note under Section 1.B.1.(d)(vii)(3) that adjustments to an MVA are allowed as follows:

An alternative methodology that adjusts the full MVA determined under i. by a factor no lower than 0 and no higher than 1 will comply with i. and ii. above as long as 1) the factor is either level or varies only by duration; and 2) the resulting adjusted MVA results in values that continue to provide reasonable equity to both the contract holder and insurance company.