AMERICAN ACADEMY *of* ACTUARIES

March 22, 2013

Rosanne Mead
Assistant Commissioner
Iowa Insurance Division
Des Moines, IA 50319

Dear Ms. Mead:

Attached are the American Academy of Actuaries[1] Annuity Illustration Subgroup's comments on the March 18, 2013 draft memorandum, *Annuity Illustrations; 191 Iowa Administrative Code rules 15.61-.69*.

If you have any questions, please contact John Meetz, the Academy's life policy analyst, at 202/223-8196 or meetz@actuary.org.

Sincerely,

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[1] The American Academy of Actuaries is a 17,000-member professional association whose mission is to serve the public and the U.S. actuarial profession. The Academy assists 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.

MEMORANDUM

To: **Persons Licensed in Iowa to Sell Annuities**

From: **Nick Gerhart, Iowa Insurance Commissioner**

Re: **Annuity Illustrations; 191 Iowa Administrative Code rules 15.61-.69**

Date: **March 18, 2013**

I. Introduction

Iowa recently adopted rules providing standards for the disclosure of certain minimum information to consumers considering the purchase of annuity contracts (191 Iowa Administrative Code rules 15.61-15.69).These rules became effective April 11, 2012, and apply to certain annuities issued after January 1, 2013. Since the adoption of these rules, questions have arisen as to interpretation and application of parts of these rules. This memorandum provides guidance to insurers and producers.

This memorandum supersedes prior memos and related e-mail. The references in this memorandum are to 191 Iowa Administrative Code rules.

Any specific waiver request of 191 Iowa Administrative Code rules 15.68-15.73 must be filed in accordance with 191 Iowa Administrative Code rules 4.21-4.36.

Questions concerning this notice or the rules, may be sent to Rosanne Mead at the Insurance Division (rosanne.mead@iid.iowa.gov).

II. Implementation of 191 Iowa Administrative Code 15.61-15.69

A. **Rule 191 IAC 15.64. Buyer's Guide**. Companies shall have a Buyer's Guide available as directed by this rule as of July 1, 2013, and the Division will enforce the rule as of that date. The NAIC currently is working on the annuity Buyer's Guide model. It is anticipated that it will be adopted in the first quarter of 2013. Companies may use their current Buyer's Guides until July 1 for sales of fixed annuities. For the sale of variable annuities, a Buyer's Guide need not be provided until after July 1, 2013. After July 1, 2013, the new NAIC model annuity Buyer's Guide should be used for sales of variable annuities. It can be used for variable annuities until a specific Buyer's Guide is developed for variable annuities.

B. **Rule 191 IAC 15.65. Content of disclosure documents.** This rule took effect January 1, 2013, and insurers should be in compliance at this time.

C. **Rule 191 IAC 15.66. Standards for annuity illustrations.** Prior to July 1, 2013, the IID will investigate any apparent violation of the new annuity illustration rules, and will determine whether the insurer under investigation made a good faith effort to comply with the new rules. Companies shall be in full compliance with the rules on and after July 1, 2013.

III. General principles.

A. Illustrations are to be used to demonstrate how the product works, and not to be used to compare two products against each other except as to how the contract features work.

B. Annuity illustrations are optional. The decision of whether or not a particular annuity contract will be illustrated is made at the company level. An illustration may be prepared (1) by the insurer that issues the product illustrated, or (2) by a producer using software created by the insurer that issues the product illustrated. A producer may design an illustration, but may not use it without the approval of the company that issues the product illustrated. Each company is responsible for monitoring the illustrations used by its producers.

C. These rules apply only to illustrations as defined in 191 IAC 15.63. For something to be an illustration, three elements must be present:

1. A <u>personalized</u> presentation or depiction. Whether information in a presentation is "personalized" is a question of fact. Caution should be used when using nonguaranteed elements in a presentation.

2. Prepared for and provided to an <u>individual</u> customer (including an individual solicited in a group setting).

3. The document must contain the non-guaranteed elements of an annuity contract.

If any one of these three things are missing, it is not an illustration for purposes of these rules, and these rules do not apply. It is possible to present something that is not an illustration, *i.e.*, does not contain all three elements above.

D. Illustrations must be specific to the annuity contract.

E. The combining of an illustration and a disclosure is permissible as long as the disclosure statement takes precedence over the illustration. The disclosure may not be unduly minimized. . Duplication of information should be avoided to avoid confusion and unnecessary length.

F. To the extent that any of the definitions in rules 15.61 through 15.69 are in conflict with definitions used in 191 IAC Chapter 16.(Replacements), the definitions in rules 15.61 through 15.69 shall govern annuity illustrations.

G. An illustration is considered to be "issued other than as applied for" when an illustration is used at point of sale and then substantive changes to a contract are made after the taking of the application and before contract issuance. In this event, a revised illustration must be issued. Mere premium or contributions changes do not constitute substantive changes requiring a new illustration. 'Substantive" means affecting the way the contract works.

IV. Topical Guidance.

A. **Delivery requirements.** The Division's expectations for compliance with the delivery requirements of these rules are set forth above in section III.

B. **Insurers should calculate separate values for each crediting method.** If a product has multiple crediting methods, an insurer must separately track the performance of each crediting method. The insurer need not show separate values for each crediting method in the illustration. Only the crediting methods chosen by the contract owner must be ~~shown~~used.

C. **Allocations to more than one account.** ~~If a fixed indexed annuity provides an option to allocate the account value to more than one indexed or fixed declared rate account, the allocation used in the illustration shall include the options selected.~~ All scenarios must use the same allocation assumptions.

D. **Ten-year period.** If an annuity has an index-based crediting method longer than ten years, the insurer shall construct index values beyond the ten-year period by repeating the movements of the index during the ten-year period.

Comment [A1]: We believe the word "shown" conflicts with the statement that "the insurer need not show separate values for each crediting method in the illustration."

Comment [A2]: Moved from S to immediately follow B.

Comment [A3]: We believe this is already covered in B, and could be confusing for the following reasons:
1. Could be misinterpreted to require insurance companies illustrate all available index options.
2. Could be misinterpreted to require a revised illustration if an owner selects different options on the allocation than the options used in the illustration.

For example, if index-based interest is calculated on a 12-year basis, the insurer should construct index values for end of year 11 and end of year 12 by applying the annual changes from years 1 and 2 to the end of year 10 index value. This approach will produce the same historical index environment as an annual crediting method that repeats the first ten years of index changes.

E. **Illustration beyond age 70.** Depending on the age of the annuitant at the time of illustration, the requirements outlined in subrule 15.66(8) may appear to result in an illustration for a period past the annuitization date, which is an apparent violation of subrule 15.66(6)(s).

The Division interprets subrules 15.66(6)(s) and 15.66(8) to mean the narrative summary should include values up to the later of 30 years or age 70, but should not extend beyond the maturity date. If the maturity date occurs before the later of 30 years or age 70, the narrative summary should stop at the maturity date.

An illustration should not demonstrate values beyond a contract's maximum annuitization date.

F. **Illustration of nonguaranteed elements statement required by subrule 15.66(6)(n)**. The required statement about nonguaranteed elements shall be contained in the narrative summary. The Division believes that a best practice would be to include the statement prominently below the illustrated values.

G. **Annuitization must be illustrated**. *See* subrule 15.66(7)(a).

H. **Subrule 15.66(6)(q) requires that illustrations be concise and easy to read.** There is no specific technical guidance on this subrule. The illustration should be reasonable in relation to the complexity of the product.

I. **Low and high scenarios under subrule 15.66(6)(i)(9).** The rule means that in any of the prescribed scenarios, the values should reflect at least one index-based interest rate at the floor (typically 0%) and at least one index-based interest rate that is less than the full index value increase (as limited by the contract language, if any, such as a cap, participation rate or spread.) If this does not happen in any of the prescribed scenarios the narrative should explain what could happen.

J. **Market value adjustment (MVA)**. Subrule 15.66(9)(f) requires that a positive and negative scenario be shown. ~~An illustration that shows the MVA at the floor (guaranteed values) and flat (nonguaranteed values), where no positive scenario is shown, would not meet the criteria of subparagraphs 15.66(9)(f) and (g).~~ A flat scenario is not considered a positive scenario.

Comment [A4]: We believe this sentence is confusing, and is already covered in the next sentence.

K. **If an illustration is not used, client-specific information may be used as described in paragraph III.B.** According to the definition of "illustration" in rule 15.63, as long as only guaranteed elements are used, a producer may use a company-approved brochure to explain the benefits of a contract, but the producer may not show numbers that illustrate nonguaranteed elements.

A producer may not verbally do what is not permitted by the rules. An oral presentation of personalized values is an illustration and is subject to the regulation.

Hypothetical generic examples are permitted. The Division will review the use of such examples to determine whether the item was used in its original form or if it was altered. If altered, there will be a question of fact whether the alteration created a personalized document which could be considered to be an illustration.

L. ~~**Terms.** Terms such as "projection" or "calculator" may be used in an illustration.~~

Comment [A5]: Specifically allowing the term "projection" seems to contradict other statements in the memo (e.g., "Comparison of Products: It is not appropriate to use illustrations to compare the earnings on products.").

Re-letter the rest of IV

M. **Surrender Value**. If the amount of a policy's surrender value is different than the account value, both surrender value and account value must be shown in an illustration. Surrender values need not be shown for the low and high ten-year scenarios.

N. **Portrayal of periodic income options**. The annuity option required under subrule 15.66(7)(e)(6) must constitute a personalized depiction.

O. **Comparison of products.** Illustrations are not intended to be used to compare products except as to how the contract features work. It is not appropriate to use illustrations to compare the earnings on products. Insurers and producers must use caution in presenting illustrated and non-illustrated products together.

P. **Violations.** Violations of the rule on illustrations will be considered unfair trade practices and will be prosecuted under Iowa Code Chapter 507B (2013). *See* rule 15.68.

Q. **Use of internet materials.** If illustrations or documents from the internet are used for sales in Iowa, Iowa law applies.

R. **When in a sales presentation the disclosure requirements apply.** The requirements of the annuity disclosure regulation are triggered when the producer starts talking about the attributes or potential elements of any contract the producer is offering. A producer should identify the company for whom the producer is working and identify the product prior to the presentation. *See* 191 IAC 15.3(9). The name of the company and the product name must be clearly disclosed on the product-specific disclosure.

S. **Appendix V.** This is only an example illustration. It illustrates how information can be shown. There is no requirement that illustrations have to be exactly like

Appendix V. If information is required by the rules to be included, then that information should be included. If a product has attributes which are not contemplated by these rules, paragraph 15.66(9)(h) requires that a description must be included. An illustration may not show something that cannot happen. For example, if an interest rate has no room to go down, the illustration should not show an interest rate below what the contract provides.

T. **Account value vs. index value method**. The low and high ten-year scenarios should be determined based on lowest and highest index value growth, not account value growth. In other words, the high 10-year scenario should be the same for all insurers for each index (e.g. S&P 500), regardless of the index-based crediting methods, caps, spreads, participation rates, etc. Although unlikely, it is mathematically possible that a low scenario determined using the index value method could result in higher account values than the account values in the high scenario. The Division considered this fact, but ultimately rejected the account value method due to its complexity. In addition, under the account value method, cap changes could cause low and high periods to shift. The index value method is simpler for systems calculations (since the low and high scenarios for each index are determined only once per year), easier for regulators to review (since all insurers use the same time periods for each index), and more easily understood by the consumer.

Modal Premiums. If a buyer ~~applies~~ selects for payment of premiums for a time frame other than annual premiums, the illustration ~~shall~~ may show annual policy values.

Comment [A6]: Please add "U." It currently seems that Modal Premiums is a subsection of Account Value vs. Index Value Method.

Comment [A7]: Illustrations are often run days before the time of application.

Comment [A8]: We believe companies should be allowed to illustrate modal premiums if they choose to do so.