AMERICAN ACADEMY *of* ACTUARIES

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January 27, 2022

Mr. Peter Weber
Chair, Index-Linked Variable Annuity (A) Subgroup
National Association of Insurance Commissioners (NAIC)

Re: Proposed Actuarial Guideline ILVA, *The Application of Model 250 to Variable Products Supported by Non-Unitized Separate Accounts* ("Proposed Actuarial Guideline")

Dear Mr. Weber,

The American Academy of Actuaries[1] Index-Linked Variable Annuity Work Group (the "Work Group") appreciates the opportunity to provide comments on the Proposed Actuarial Guideline.

Currently there is a wide range of practices related to index-linked variable annuity (ILVA) nonforfeiture that are not reflected in the actuarial guideline. This is a complex topic with a relationship to several NAIC model laws with many components to address. At this time, the Work Group is not providing any specific language changes, but offers the following conceptual comments for your consideration:

Scope of Actuarial Guideline:

1. The work group suggests more clarification related to the application of the Proposed Actuarial Guideline to Models 805, 250, and 255. Specifically, if an ILVA product falls under this Proposed Actuarial Guideline, it is unclear how the various provisions of the model laws are addressed by this guideline or would otherwise continue to apply. Of additional interest is how an index account (with a guaranteed zero floor) offered in a fixed index annuity (FIA) could be treated within an ILVA.
2. The Proposed Actuarial Guideline states that it "does not apply to products supported by a general account." Therefore, these scenarios would not be considered: non-insulated separate accounts supported by general accounts; insulated separate accounts supported by general accounts (if there is a shortfall); and the assets/derivatives supporting ILVA products often held in the general account. Therefore, we encourage using broader language to identify the scope of the guideline.
3. The Proposed Actuarial Guideline recognizes that not all ILVA products reflect the market value of fixed income assets; however, there is text within the draft that assumes market values are used. For example, the assumptions text appears to be written with the

[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.

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assumption that the fixed-income asset proxy value reflects market values. The Work Group suggests that the guideline should allow for different approaches consistently throughout the text.

4. The drafting note in the Proposed Actuarial Guideline is not clear, and seems to imply that all ILVA products have explicit charges. However, some ILVA products are spread-based or a combination of spread- and fee-based. Therefore, the Work Group suggests clarifying this drafting note.

Terminology within Actuarial Guideline:

5. The Work Group found the term "Index Option Value" to be unclear, because it would be expected that this term describes the value of an option rather than an entire contract value. The Work Group recommends using Indexed Account Value as it would better describe the index portion of the contract value.
6. The Work Group notes that it may be easier to define hypothetical portfolio value, fixed-income asset proxy value, and the derivative asset proxy value, because most uses of these defined terms seem to be referring to their values. The guideline could then specify in its definitions that the fixed-income asset proxy value may be a market or book value depending on product design and that the derivative asset proxy value should be a market value.
7. The Proposed Actuarial Guideline states that the product filing must quantify the maximum difference between the value of the hypothetical portfolio and the index option value at the beginning of the index term. However, it is unclear how these values could be different because they are defined to be equal. The Work Group encourages clarification.

Hypothetical portfolio considerations in Actuarial Guideline:

8. The third principle in the Proposed Actuarial Guideline states that the hypothetical portfolio must be designed to perfectly hedge the benefit guarantees at the end of the term. The Work Group suggests additional clarification regarding: is the expectation of a perfect hedge for each individual who persists or for the aggregate in-force population (which would recognize various decrements)?
9. The Proposed Actuarial Guideline allows the determination of interim values to be based on actual assets or a hypothetical portfolio of assets. The use of actual assets could lead to very different interim values for two products that are otherwise similar, because there is a wide variety of current company approaches to these assets. With respect to hedge assets, the use of a hypothetical portfolio of static hedges may produce more understandable and/or consistent interim values across insurers.
10. The Proposed Actuarial Guideline states that the assumptions used to value the hypothetical portfolio should be based on market prices. However, if there are market prices, then it is expected those prices would be used to determine values, and assumptions would not be needed. If there are no market prices, then assumptions would be needed, but they could not be based on market prices. Therefore, the Work Group encourages clarification.

11. The Proposed Actuarial Guideline allows the hypothetical portfolio to be valued using static or dynamic assumptions. For proxy values that reflect market values, the assumptions should be dynamic and reviewed frequently, potentially as often as monthly intervals.

The Academy's Work Group appreciates the efforts of the Index-Linked Variable Annuity (A) Subgroup on this Proposed Actuarial Guideline. If you have any questions or would like further dialogue on the above topics, please contact Khloe Greenwood, life policy analyst, at greenwood@actuary.org.

Sincerely,

Beth Keith, MAAA, FSA
Chairperson, Index-Linked Variable Annuities Work Group
American Academy of Actuaries