



May 5, 2014

Blaine Shepherd
Chair, Separate Account Risk (E) Working Group
National Association of Insurance Commissioners

Dear Blaine:

The Separate Account Products Work Group (SAWG) of the American Academy of Actuaries¹ Life Practice Council appreciates the opportunity to provide comments on the Potential Actions/Recommendations document exposed for comment on November 18, 2013 by the Separate Account Risk (E) Working Group (NAIC Working Group).

At the March 24, 2014 meeting of the NAIC Working Group, Bill Carmello (NY) shared some observations on our [January 10, 2014 comments](#) on items 1.d. and 2.a. As agreed, the SAWG later met with Bill to discuss his observations and update its comments as appropriate, which follow:

1. Incorporate Suggested Principles for Insulating Separate Account Assets for Non-Variable Products

The first sentence of item 1.b. states, “Insulated assets should derive only from funds contributed by customers, plus earnings thereon, less any withdrawal and fees.” We suggest the addition of the following sentence: “The implementation of such principles will require a redefinition in NAIC Model Regulation 255 of the funds that may be insulated in MGA contracts.” We do not believe that the principles are consistent with the MGAs currently sold, which are designed to comply with Model Regulation 255, and that if the NAIC Working Group wishes to proceed with these principles, under the assumption that such contracts may be insulated, it is necessary to make this statement up front as part of the principles section.

Item 1.d. states, “For fair value separate accounts, reserves should be calculated to correctly reflect the nature of the liabilities and the underlying assets as well as to the adequacy of the assets, including risk charges, to meet future expected payouts.” We are unclear of the intent of this wording, but we are concerned that it is not completely accurate as it stands. We suggest this sentence be changed to read, “For fair value separate accounts, reserves should be calculated to correctly reflect the nature of the liabilities and, where required by regulation, the yield on the assets.”

¹ The American Academy of Actuaries is an 18,000-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.

2. Review and Consider Updating Revisions to SSAP No. 56 and Model #255

If the NAIC Working Group decides to allow MGAs to be classified as insulated products, the requirement under item 2.a. that, “Recommended revisions would clarify that such transferred assets are non-insulated assets ...” may need to be clarified to state, “Recommended revisions would clarify that such transferred assets are non-insulated assets, to the extent that the transfers represent funds in excess of funds contributed by customers, plus earnings thereon, less any withdrawals and fees, ...”

We previously mentioned that applying the proposed principles to MGAs would be problematic. That comment was made in the context of how we understand MGAs are designed and accounted for today (consistent with NAIC Model Regulation 255, whether it has been adopted in the state or not), under the assumption that such design and accounting would not change for new issues. Today the reserve amount, which also is the contract insulation guarantee, is deposited into the separate account. This would then require subsequent transfers to be made into the separate account to recognize reserve increases from the annual decrease in the surrender charge. But if we assume that for future contracts the entire initial amount is deposited in the separate account, there are still challenges in applying the principles to MGAs designed for the individual market. This is because the principles are designed to provide aggregate insulation in an institutional purchase situation (e.g., BOLI and COLI), where cash surrender values may exceed the insulated amount under certain circumstances; however, MGAs are individually purchased policies, where reserves (the contractually insulated amount) are unlikely to exceed the proposed insulated amount (both initially and ultimately).

Insulating assets in the aggregate does not recognize the individual circumstances applicable to each MGA contract (e.g., investment environment and type of assets purchased to support individual guarantees, which would need to be tracked to support policy-specific insulation requirements). In addition, insulating accumulated assets does not recognize that the contractual insulation guarantee for MGAs is the reserve, and may lead to aggregate insulated assets that are greater than the insulation guaranteed to the policyholder. This could lead to surplus accumulation in the separate account or in another separate account, which would be effectively a non-insulated amount since in the event of an insolvency it would not be backing a contract guarantee.

The appropriate accounting and reporting approach would depend upon regulatory requirements. This could include a requirement to set up a payable from the separate account to the general account for the accumulation of “insulated” surplus that will not be needed to satisfy the guarantee. If the potential challenges for insulation of this product under the proposed principles were attempted to be addressed by redefining the insulation guarantee, such as being based on asset accumulation, it would significantly complicate the nature of the guarantee provided to the policyholder and the manner in which it would be described.

Our intention is only to point out that general principles that are intended to create a level playing field could have unintended consequences. We hope these comments are helpful.

We will continue to follow further developments on this issue and offer additional comments as appropriate. In the meantime, if you have any questions please contact John Meetz, the Academy's life policy analyst (202-223-8196; meetz@actuary.org).

Sincerely,

Cande Olsen, FSA, MAAA
Chairperson
Separate Account Products Work Group
American Academy of Actuaries

Cc: Bill Carmello, NYID