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The NAIC Considers Whether a New Framework Should Apply to Innovative Annuity Products

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The Life Actuarial Task Force's Index-Linked Variable Annuities (A) Subgroup (the "ILVA Subgroup") began a fresh look at the regulatory framework for annuity products. On February 6, it held a call to review its January 15, 2014 *Discussion Points for Separate Account Index-Linked Products* Paper (the "*Discussion Points Paper*"). The *Discussion Points Paper* addresses a new type of annuities. Regulators are concerned that the new "index-linked annuities" do not fit within the existing regulatory framework. Index-linked annuities are similar to currently available fixed index annuities in that their value is based on a change in a financial index. However, index-linked annuities differ in the following ways:

- A negative return can be credited to an index-linked annuity if the index decreases in value. Currently, there are two variations on how much negative return will be credited to the annuity value:

	"Buffered" Design	"Hard Floor" Design
Decrease up to a stated percentage (e.g., -10%)	Insurer bears this risk	Annuity owner bears this risk
Additional decrease beyond the stated percentage	Annuity owner bears this risk	Insurer bears this risk

- A separate account holds assets that support the obligation of the insurer. The separate account, however, does not invest in the securities or commodities that comprise the index. Moreover, the annuity value does not reflect the "unit value" of the separate account.

During the call, the ILVA Subgroup discussed (i) whether the index-linked annuities should be viewed as "variable annuities" and subject to nonforfeiture requirements; (ii) what reserves should be established; (iii) what valuation applies to the separate account; (iv) what RBC applies; (v) whether there are other financial reporting issues; and (vi) what consumer issues arise. One regulator posited that a principles-based approach should be adopted to develop the regulatory framework to address the variety of new products, including contingent deferred annuities ("CDAs") and synthetic guaranteed investment contracts ("synthetic GICs"). This would also provide a framework for future product designs. While some regulators acknowledged the appeal of such an approach, others were concerned that an immediate solution was needed to address the new index-linked annuities currently in the market. Several regulators called on the insurance industry to provide information on the current practices of insurers that issue index-linked annuities. The ILVA Subgroup also invited the industry to help consider the appropriate regulatory framework. This invitation is a window of opportunity for insurers to plant the seeds for a regulatory framework that could apply to an array of innovative annuity designs.

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