

Draft Pending Adoption

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Life Insurance and Annuities (A) Committee
Phoenix, Arizona
March 17, 2024

The Life Insurance and Annuities (A) Committee met in Phoenix, AZ, March 17, 2024. The following Committee members participated: Judith L. French, Chair (OH); Doug Ommen, Co-Vice Chair (IA); Carter Lawrence, Co-Vice Chair (TN); Mark Fowler (AL); Barbara D. Richardson (AZ); Karima M. Woods represented by Philip Barlow (DC); Grace Arnold and Fred Andersen (MN); Justin Zimmerman (NJ); Glen Mulready (OK); Elizabeth Kelleher Dwyer represented by Patrick Smock (RI); Scott A. White represented by Julie Blauvelt (VA); and Nathan Houdek (WI). Also participating were: Michael Humphreys (PA); Scott Kipper (NV); Nour Benchaaboun (MD); and Rachel Hemphill (TX).

1. Adopted its 2023 Fall National Meeting Minutes

Commissioner Lawrence made a motion, seconded by Cabinet Executive Officer Richardson, to adopt the Committee's 2023 Fall National Meeting minutes (*see NAIC Proceedings – Fall 2023, Life Insurance and Annuities (A) Committee*) minutes. The motion passed unanimously.

2. Heard a Federal Update

Taylor Walker (NAIC) gave an update on federal activity involving life insurance. She explained that for years, the National Kidney Foundation has been advocating for the passage of its living organ donor legislation, which is the Living Donor Protection Act (LDPA), at both the state and the federal levels. While slightly different iterations have been introduced in Congress over the years, the LDPA primarily seeks to prohibit life, disability, and long-term care insurers from discriminating against living organ donors based solely on their status as living organ donors. The latest version introduced this Congress provides that an insurer may not deny coverage, cancel coverage, refuse to issue, determine the price or premium for, or otherwise vary any term or conditions of a policy based solely on someone's status as a living organ donor without any actual, unique, and material actuarial risks. She said Representative Nadler of New York is sponsoring the House version, H.R. 2923, and Senator Gillibrand, also of New York, is sponsoring the Senate version, Senate Bill 1384.

Walker said the bill's sponsors and the National Kidney Foundation are looking to state insurance regulators for their support. She explained that, currently, the NAIC has not taken a position on this bill. She explained that, in general, the NAIC does not support legislation that would preempt state insurance regulators' oversight of insurance, but this bill version places enforcement authority with state regulators, which is a positive sign. She explained that the NAIC membership is in the process of reviewing the LDPA to determine whether the NAIC will take a position in its response to the sponsors. She said that states have been very active on this issue. To date, 32 states have enacted the LDPA or substantially similar legislation, and more states are considering legislation.

Walker also gave an update on the U.S. Department of Labor's (DOL's) proposed Retirement Security Rule. She reminded the Committee that the NAIC submitted a comment letter in December outlining concerns with both the substance of the proposal and the DOL's lack of coordination with its fellow regulators in the states. Walker said the comment letter also emphasized the changes in the regulatory landscape for annuities since the DOL put forward its last fiduciary rule—45 states have adopted the NAIC's *Suitability in Annuity Transactions Model Regulation (#275)*, which includes a best interest standard for annuity sales. She said the NAIC expressed concern that the revised rule could undermine federal efforts that seek to close the retirement savings gap. She said the DOL received 19,000 comment letters prior to the Jan. 2 response deadline.

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Walker said the proposed Retirement Security Rule was sent on March 8 to the Office of Management and Budget (OMB) for review. The OMB has 90 days to review the proposal, but it could be approved and finalized even sooner. The rule will become effective 60 days after its publication in the Federal Register.

3. Adopted the Report of the Life Actuarial (A) Task Force

Hemphill said the Life Actuarial (A) Task Force met March 15. She said the full report is included in the meeting materials, but she wanted to mention key areas of activity. She said the Valuation Manual (VM)-22 (A) Subgroup continues to develop principle-based reserving requirements for non-variable annuities and is currently preparing for a field test later this year (between July and September), with a planned effective date for the new requirements of Jan. 1, 2026.

Hemphill said that for indexed universal life policies (IUL), the Indexed Universal Life (IUL) Illustration (A) Subgroup members are actively reviewing company illustrations for compliance with current requirements and identifying any concerns. Andersen said regarding illustrations and marketing of life insurance and annuity products, regulators are looking into illustrations for compliance with existing rules, looking at specific company examples. He said the focus is not just on indexed universal life products but also on other life insurance products and annuities. Regulators want to ensure that companies are not overpromising or understating the downside risks of products. He said the Life Insurance and Annuities (A) Committee will be updated on any developments, whether it's a summary of enforcement activity for compliance with existing rules or recommendations for new or revised rules.

Director French asked if Andersen had an idea when they might be able to report the results of some of the Subgroup's work. Andersen said the Subgroup has started to notice things in their product reviews, and the Subgroup is having more productive conversations among the states about what they are seeing. He said the Subgroup is starting to consider another round of illustration guideline changes. He said he did not know at this point whether they would focus on specific areas or recommend more comprehensive changes. He said that they would like to have some additional actuaries to work on this rather than depending on the same regulators already involved in the many other Task Force projects. Director French asked for regulator volunteers who would like to get involved in the work.

Hemphill said that there has been a lot of activity on the NAIC's Generator of Economic Scenarios (GOES) project. Both the Generator of Economic Scenarios (GOES) (E/A) Subgroup and the Life Actuarial (A) Task Force have been very active. She explained that economic scenario generators are critical for determining appropriate reserve and capital requirements for products that are interest or market sensitive. Economic scenario generators produce 10,000 unique economic scenarios or future paths for interest rate, equity, and corporate returns. They will be used when determining reserves (and, in some instances, capital) for life products, variable annuities, and non-variable annuities.

The GOES project already has a substantial history, reflecting significant effort and work product from NAIC staff, regulators, industry, and the American Academy of Actuaries (Academy). In 2017, the Academy notified the Task Force that it did not have the resources to maintain the prescribed generators, except in their current form, until a suitable replacement could be found. In 2019, the Financial Stability (E) Task Force noted a potential deficiency in the prescribed generators related to a limited reflection of long periods of low (or negative) interest rates and requested the Valuation Analysis (E) Working Group assess risk to insurance organizations. After extensive work with regulators, the industry, and Academy subject matter experts (SMEs), the NAIC issued a request for proposal (RFP) for a new generator in March 2020. Conning was selected as the vendor in September 2020.

In 2021, a drafting group formed to develop recommendations to the Life Actuarial (A) Task Force and the Life Risk-Based Capital (E) Working Group. Industry and Academy SMEs were included in June 2021 to incorporate

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more feedback and plan a June 2022 field test. The field test began in June 2022, and most results were turned in by August 2022. VM-20, VM-21, C3 Phase II, and C3 Phase I field test results were shared and discussed at public Life Actuarial (A) Task Force meetings in 2023. In August 2023, based on public discussions and industry input regarding the longer-term maintenance of the generator, the GOES (E/A) Subgroup was formed at the 2023 Summer National Meeting to support implementation, develop acceptance criteria, build a model governance framework, and maintain the generator.

Between August 2023 and February 2024, the Academy proposed criteria provided over time to the Life Actuarial (A) Task Force for interest rates, corporate, equity, and joint interest rate/equity. In October 2023, the Task Force exposed a set of updated acceptance criteria based on input from the Academy, industry, and regulators during discussions within the Task Force, as well as a project timeline in response to industry requests. In November 2023, there was general agreement that the updated calibration was a significant improvement while noting areas for further refinement. In December 2023, the Life Actuarial (A) Task Force exposed updated targeting criteria and evaluation statistics again based on additional input from the Academy, industry, and regulator discussions within the Task Force.

In February 2024, the GOES (E/A) Subgroup reviewed results and insights from a model office based on the first field test. The model office will be used to analyze new scenario sets using sample blocks of business for different product types, to reduce the number of items that need to be field tested. Also, in February, the GOES (E/A) Subgroup selected the correlation approach proposed by the industry, updated equity criteria, and the Conning Corporate model. Currently, Conning is recalibrating the model based on updated criteria and modeling decisions. The resulting scenarios and scenario statistics will be made public as they are available and will be discussed at a GOES (E/A) Subgroup meeting later this month.

Hemphill said that while a lot of attention is focused on areas where there may be differences in views among stakeholders, it is worth noting that on this very technical project, most of the work represents areas of agreement. Even where there are topics of potential disagreement, stakeholders and regulators are working from a position of fundamental common ground. She explained that there is a common goal of avoiding calibrations that produce unreasonable scenarios, so that the current inadequate and now long outdated economic scenario generator can be replaced. She said regulators and industry may have differences on what is “plausibly more extreme” than history, but they agree that: 1) a generator would not be reasonable if it did not produce scenarios more extreme than history; and 2) there should be a limited percentage of such worse than historical events. She said it is preferable for company actuaries to have exhaustive model documentation. After negotiation between the NAIC and Conning, this documentation is now available to company actuaries by signing a nondisclosure agreement. She said in response to regulator requests for suggestions of a moderated approach for the treasury/equity relationship (between assumed independence and full functional linkage), the American Council of Life Insurers (ACLI) proposed and the GOES (E/A) Subgroup adopted a moderate approach, where a positive correlation is introduced without a full functional linkage. She said the GOES project has been vastly improved by the open dialogue and collaboration, and she encouraged continued feedback as the project continues.

Commissioner Ommen made a motion, seconded by Commissioner Houdek, to adopt the report of the Life Actuarial (A) Task Force. The motion passed unanimously.

4. Received an Update on the Accelerated Underwriting (A) Working Group

Commissioner Houdek gave an update on the planned work of the Accelerated Underwriting (A) Working Group. He said the Accelerated Underwriting (A) Working Group last met Feb. 22, 2023. He said the Working Group at that time was making progress towards completing its charge to “Consider the use of external data and data analytics in accelerated life underwriting ... including drafting guidance for the states.” He reminded the Committee that the Working Group had exposed two documents: 1) a draft regulatory guidance document and

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2) a referral to the Market Conduct Examination Guidelines (D) Working Group. The public comment periods for both ended in March 2023. He said the documents and comments are posted on the Accelerated Underwriting (A) Working Group's web page on the NAIC website.

Commissioner Houdek explained that at same time the Working Group was exposing its documents, the Innovation, Cybersecurity, and Technology (H) Committee and its Big Data and Artificial Intelligence (H) Working Group were working on a couple of projects, the results of which would inform the Working Group's work products. The Working Group decided to pause its work pending the completion of this other work.

Commissioner Houdek explained that the survey on the use of artificial intelligence (AI)/machine learning (ML) in life insurance under the Big Data and Artificial Intelligence (H) Working Group and the NAIC *Model Bulletin on the Use of Artificial Intelligence Systems by Insurers* are now complete, and the Working Group plans to begin meeting again and revisit the two documents it exposed for comment last March. On Feb. 13, the draft regulatory guidance document and the draft referral were re-distributed to give regulators and stakeholders an opportunity to get re-acquainted with the drafts and consider them in light of the work completed under the Innovation, Cybersecurity, and Technology (H) Committee. He explained that written comments were not requested at this time, but stakeholders were asked to consider the impact of the model bulletin and survey results on the draft documents. The next meeting of the Accelerated Underwriting (A) Working Group has been set for Wednesday, April 3, to discuss next steps.

5. Received an Update on the Annuity Suitability (A) Working Group

Commissioner Ommen gave an update on the planned work of the Annuity Suitability (A) Working Group. He said the Working Group has been encouraging the adoption of the revised Model #275. As of March 11, the best interest revisions in Model #275 have been adopted in 45 states and territories and are pending in three.

Commissioner Ommen said the Annuity Suitability (A) Working Group plans to resume its meetings to continue its discussion of potential questions to add to the current frequently asked questions (FAQs) document related to the safe harbor/comparable standards provision in the revised Model #275. He said that Iowa and several other states have been involved in reviews of the implementation of the best interest provisions in Model #275. He said that, in general, the policies and procedures that have been reviewed are comprehensive and cover the key requirements of the regulation. He said, however, most reviews have disclosed one or several deficiencies, but these deficiencies have generally not been systemic across the industry, apart from the safe harbor provisions, where they have seen more systematic deficiencies.

Commissioner Ommen explained that, in order for the safe harbor to apply, an insurer must “[m]onitor the relevant conduct of the financial professional seeking to rely on [the safe harbor] or the entity responsible for supervising the financial professional.” He said the reviews have generally disclosed several ways in which companies' safe harbor implementation is failing to rise to the level of “monitoring the relevant conduct of the financial professional,” including inadequate onboarding of new broker-dealers to sell for the insurer and not necessarily ensuring that the broker-dealer is even prepared to review fixed annuities. He said some insurers seemed to reduce their monitoring responsibilities into a once-every-several-years audit; and then some insurers have instituted an audit process that reviews a scant fraction of a percent of the sales actually made by the insurer. He said that given the results of the reviews, the Annuity Suitability (A) Working Group is prepared to take up the work of providing regulatory guidance in its FAQs.

Smock supported the Annuity Suitability (A) Working Group continuing to work on regulatory guidance on the safe harbor provisions in Model #275. He said Rhode Island concluded an analysis last week, and all the concerns they identified came down to the lack of safe harbor oversight.

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6. Discussed Other Matters

Carrie Haughawout (ACLI) highlighted for the Committee a set of banking regulations that were issued last summer. She said the Regulatory Capital Rule: Large Banking Organizations and Banking Organizations with Significant Trading Activity, referred to as Basel III Endgame, are currently being considered by banking regulatory agencies (the Office of the Comptroller of the Currency—OCC, the Board of Governors of the Federal Reserve System—Board, and the Federal Deposit Insurance Corporation—FDIC). She said the ACLI and other insurance industry representatives have submitted comment letters on the proposal. She highlighted two primary concerns.

First, Haughawout said the proposal's corporate exposures provision would unnecessarily and arbitrarily harm mutual insurers and other non-public life insurers. She explained that this provision assigns a significantly higher (50% higher) risk weight for bank exposure to non-public life insurers solely because they are not publicly listed companies. When justifying the lower risk weighting for publicly traded companies, the proposal asserts that public companies "are subject to enhanced transparency and market discipline as a result of being listed publicly on an exchange." This line of reasoning overlooks the requirement that all U.S. insurance companies provide audited, publicly accessible financial statements that reflect their financial strength and creditworthiness as insurers.

Haughawout said ACLI's letter points out that the proposal would substantially disrupt the bank-owned life insurance (BOLI) market by driving banks away from working with life insurers despite their outstanding credit quality and long-standing participation in the BOLI market. Today, over 60% of banks own BOLI with at least \$1 million in account value, and as of 2022, 70% of BOLI contracts sold in the U.S. were issued by mutual insurers. Because the proposal would unexpectedly subject a policy to a higher risk-weight than had it been issued by a publicly listed insurer, it would harm bank policy holders with existing BOLI contracts issued by non-public life insurers. This distinction is discriminatory, not justified by creditworthiness, and could lead to an exodus of in-force BOLI policies.

Haughawout said that in addition to the arbitrary banking requirements impacting mutuals and other non-public life insurers, the letter also highlighted that the unnecessarily excessive bank capital requirements would increase costs for life insurance hedging transactions, which help insurers manage market-based risks in investment portfolios and products that deliver financial security to millions of Americans. She said the proposed Basel III Endgame approach fails to recognize the highly regulated environment that all U.S. life insurance companies operate in, the enhanced transparency of all companies in the industry, the exceptional financial strength of life insurers, and the negative impact such a policy change would have on the banking system.

Haughawout said the ACLI submitted comments to the Federal Reserve, FDIC, and OCC requesting changes to the proposal including: 1) revising the proposal so corporate exposures to all investment grade life insurers are treated the same, regardless of the ownership structure, and 2) eliminating or revising approaches impacting life insurers' risk hedging activities including the proposed Global Systemically Important Bank (GSIB) surcharge. Haughawout said banking regulators need to understand the robust solvency regulation provided by the current state-based system. Haughawout agreed to share the ACLI comment letter with Jennifer Cook (NAIC) to distribute to regulators.

Having no further business, the Life Insurance and Annuities (A) Committee adjourned.

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