VIP Working Group

File No: S7-16-23

November 10, 2023

Commissioners:

We are a working group comprised of 8 attorneys from 5 insurance companies that offer variable products and some registered index-linked annuities (RILAs). This Variable Insurance Products Working Group meets quarterly to discuss the issues of the day. Please accept our input on this important rulemaking. These views do not necessarily represent the views of our employers. We largely support the proposal but believe many of the required disclosures lack balance and paint RILAs harshly.

Regulatory Clarification:

- Please clarify whether the RILA contract or each index option is the security required to be registered. This is a gray area in the variable annuity space (that is, whether the contract or the interests in the separate account are the security), but the Commission has stated that each purchase payments and subaccount transfer requires registration. In the RILA context, in all cases the issuer is the insurance company. If the contract is the security, then a single premium contract never needs to update its registration statement after it ceases sales or deliver an updated prospectus after the initial sale. If the index option is the security, then each index option renewal and transfer requires delivery of a current prospectus. Please also clarify the extent to which the exemption provided in section 3(a)(9) of the Securities Act is applicable to index option transfers and renewals.
- Please consider providing relief consistent with the Commission Position on Discontinued Products to all variable products and RILAs. These are long term products. It hurts new entrants and innovation by requiring insurance companies to keep registration statements current for the indefinite future, even for new products that have largely failed to launch or for existing contracts with a very small investor base.
- Please clarify whether old variable products and RILAs can rely on regulation D when assets and contract owners dwindle. Is it a continuing public offering if contract owners continue to accept additional money or permit index option transfers or renewals from a very narrow group of current contract owners many years after the offering to the public? Historically, the staff has said that the public offering is ongoing, but this does not seem correct or consistent with our interpretation of the Securities Act of 1933.

- We believe the market value adjustment features fall plainly within the definition of a RILA under the RILA Act. They are:
    - annuities;
    - registered securities;
    - issued by a regulated and supervised insurance company;
    - not issued by an investment company; and
    - returns are based in part on the performance of a specified benchmark index or rate.

  As such, they should be permitted to register on Form N-4 and if not, insurance companies should be able to rely on the self-help provision of the RILA Act.
- We believe that contingent deferred annuities (CDAs) can also be read to be covered by the RILA Act because that are regulated as annuities, they are securities, they are not issued by an investment company, and returns are based on a reference asset (that is, a basket of securities typically held within a brokerage or retirement account). We believe CDAs should be able use N-4 or at least be permitted to use the same accommodations such as permitting the use of STAT financials, permitting the omission of MD&A, executive compensation and any future operating company ESG disclosures.

Form Amendments:

We have several significant concerns about the proposed form text:

1. Disclosing the maximum loss on the cover page and elsewhere in the prospectus is inappropriate where no other securities offerings are required to do the same. Your own investor testing shows that losses on these products over the long term have historically been quite small in magnitude.
2. Treating interim value adjustments as a fee is inappropriate because it is a product feature based on market risk; it is not a fee. The federal securities laws do not require that these securities be redeemable. Insurance companies could design products that investors can only exit at the end of the period. However, we provide a means to exit early as an accommodation to investors and we do so approximately at cost. The SEC proposed to penalize insurance companies for providing investors ready access to their money. Also, forcing disclosure of the maximum theoretical loss gives the investors the wrong impression. This feature is no different than a fund being available for redemption at current net asset value. Even if you did want to disclose a loss figure, your own investor research suggests that investors may be more interested in the actual losses borne by others rather than a maximum theoretical loss.

3. Current rates for RILAs change frequently. Sometimes the rates are different based on when you purchased your contract, your distribution channel, the contract class, and the optional benefits available. Disclosing this every few days in the form of stickers will overwhelm investors. Insurance Companies could offer rates that do not change as often, but to offset the risk to the insurance company of keeping rates more constant means that investors will receive lower rates. Please allow rates to be made available online. The SEC can condition the website posting of rates on a record keeping requirement and consenting that the information be subject to prospectus or registration statement liability. Alternatively, make it an untagged independently filed document that must be delivered with and affixed to a prospectus akin to a pricing supplement.
4. The historical index performance presentation is problematic. Historical index performance should not be overlaid with a made-up artificially low cap. This is misleading. The SEC should not compel misleading disclosure. Cap rates have never been that low. If you are going to require actual index performance, you should require actual buffer and cap rates. You intend to require disclosure of a 10% buffer and a 5% cap. Your own investor testing suggests that with a 10% buffer over 1-year, an 18% cap is a common offering. However, instead of illustrating a common offering of 18%, you intend to show returns that are 28% (28% = 5/28) that of the common offering. That is plain wrong and unjustifiable.

Below are more specific concerns about the proposed form amendments:

- Item 1(a)(6) - The cover page required maximum loss disclosure which is apparently only required for RILAs and no other securities regardless of their level of risk. RILAs should have the same type of risk of loss disclosure as other securities with a similar risk/return profile. In addition, the statement about potential losses exceeding potential gains provides little value and may be true for all investments.
- Item 1(a)(7) – First, contracts do not include a minimum guaranteed limit on losses. Second, this disclosure about maximum loss on an interim value adjustment is not ripe for a cover page as it is entirely theorical and extremely remote. If we include this language, we should include the risk of an asteroid impacts wiping out humanity on the cover page as well. Consider replacing with the language from item 2(d) and add “under extreme market conditions”.
- Item 1(a)(11) - We believe that because the product has the term “registered” in its name, the rule 481(b)(11) legend should be required on both the ISP and USP cover pages. Alternatively, despite the RILA Act’s use of the term, the SEC should move away from the term RILA and use something like a Structured Annuity. The term “registered” in RILA may only serve to confuse investors as to

what that term means when there are other registered products including product subject to both ’4o Act and ’33 Act registration that do not use the moniker “registered” (such as variable annuities, mutual funds & ETFs).

- Item 2(b)(2)(iii) – Please explain what the minimum limit on index losses guaranteed for the life of the contract refers to. If we do not have such a limit, can we omit the disclosure? Is the SEC requiring that contracts be amended to include such a limit? Insurance Companies cannot guarantee particular limits for the life of the contract because they are very long-term products and insurers do not know what options may or may not be available in the future.
- Item 2(b)(2)(iv) - Please explain what the minimum limit on index gains guaranteed for the life of the contract refers to. If we do not have such a limit, can we omit the disclosure? Is the SEC requiring that contracts be amended to include such a limit? Insurance Companies cannot guarantee particular limits for the life of the contract because they are very long-term products and insurers do not know what options may or may not be available in the future.
- Item 2(d) - Remove the instruction from this item. The disclosure is sufficient with<u>out</u> including a numeric figure. Also, add that the losses can be significant under “extreme market conditions”.
- Instr. 2(a) to item 3 – Interim value adjustments are not fees. It is the approximate fair market value of the investments underpinning the product. This amount can be positive or negative.
- Instr. 2(a) to item 3 – There are concerns that excluding “implicit” index-linked ongoing fees, but requiring variable annuities to show ongoing fees is an unfair presentation. They both have the same approximate margins for the insurance company. We also note that the Commission is most concerned about transaction charges, which are easily avoidable but are content to omit ongoing RILA charges which will hit each investor year-over-year. RILAs and variable annuities are two product investors may choose between, you should try to create as much parity as possible when it comes to fee presentations.
- Fee table
    - Interim value adjustments are not fees.
    - Some indices have built in fees. They do this because they are total return indices, or they track a price return index that does not pay out sufficient dividends to help compensate the insurance company. So, the index builds in a fee. Should this fee be reflected in the fee table? On the one hand it reduced performance just like a fee; on the other hand, it is no different than the use of other price return indices which likewise take a

haircut off of index performance. The fee can also be said to be imposed by the index provider rather than the insurance company. We are looking for clarity as to the treatment of these types of indices with built-in fees or similar haircuts.

- Item 6(d)(2)(ii) – It is unclear what the required statement is intended to convey or whether it is even an accurate statement. If anything, it appears potentially applicable to all investments.
- Item 6(d)(2)(ii)(B) – For disclosing current crediting rates. How far in advance must the rates be filed? DO investors get the rates at the time the application is signed or the date the insurance company received the money or transfer request? Today, some products do not disclose rates in advance and instead use thresholds or bailout features. Is this approach no longer permissible? Can existing products continue to operate with these features since the investor already set parameters such that they do not regularly check rates?
- Item 6(d)(2)(iv) – Do not require the index performance overlay with a 5% cap. This rate does not reflect reality and undermines the point of showing historical performance. Other investments, such as structured notes, show index performance without an overlay.
- Item 6(d)(2)(iv)(c) – The proposal requires examples to reflect fees. We think this is problematic. First, index options are difficult enough to explain and illustrate without fees. Second, what fees should be assumed? What product features should we assume are elected? Should we assume the imposition of an option benefit fee that few investors elect or that are charges on a basis other than contract value? How old is the contract (which bears on surrender charges). The best course is to keep examples as clean as possible and acknowledge that other fees (and you can require the type to be named) may also be deducted. This approach is also consistent with the current approach to presenting separate account performance. If you believe interim value adjustments are fees, what interim value adjustment should we assume?
- Item 7(e) – This should be moved to item 6 since an interim value adjustment is not a charge.

Financial Statements:

- We support permitting the use of statutory financial statement for RILA issuers just as it permitted for variable contracts. Investors are used to dealing with these types of financial statements because the vast majority of Americans own insurance and have statutory financial statements available to them.

  - The SEC should extent the use of statutory financial statement to market value adjustment contracts, contingent deferred annuities, funding agreement, as well as index features and MVA features associated with life insurance. The relief should extend to all annuity or life insurance products offered by a state regulated insurance company where the product is also regulated as insurance or annuities. This can be accomplished through a Class Order, an amendment to rule 12h-7 or by amending Regulation S-X.

- Form N-4 has an instruction that states an insurance company cannot use statutory financial statements if you prepare GAAP financial statements with respect to a corporate parent that is a GAAP filer. Can you please either eliminate this provision or more clearly explain this. Historically, if an insurance company had a publicly traded corporate parent that prepared GAAP financial statements the subsidiary likewise had to prepare GAAP financial statements. However, The Commission granted STAT relief to Brighthouse and Jackson National both of which have publicly traded parent companies.

- If you decided to rescind 3-13 Relief for RILAs since it is provided for in the form, please ensure that any relief is not rescinded until the final compliance date.

- Currently, on Form N-4, registration statements that go effective in the first 90 days of the year can use third-quarter stub financials of the depositor. The unwritten staff position has historically been that this also applies to the separate account financial statements. Can you please include this in Form N-4 and N-6 to remove any doubt?

- RILA issuers should be allowed to use Form N-VPFS to file a single set of financial statements on EDGAR instead of needing to file the financial statements with each registration statement. In addition, please clarify if an insurance company can incorporate the insurance company financial statements filed under one of the insurer's separate accounts instead of needing to refile the information multiple times on EDGAR.

Filing Questions:

- If the proposal is not adopted by June 2024, please provide detailed instructions as to how insurance companies can use the self-help provision. We understand that EDGAR, as currently programmed, will not permit a non-investment company to file on Form N-4.

- If there is a variable annuity that also offers a RILA, we do not believe that 2 registration statements need to be filed on EDGAR (1 under the insurance

company and 1 under the separate account). Instead, an insurer should only be required to file a single tagged registration statement. In addition, consider permitting the use of a single 24f-2. Requiring multiple nearly identical filings has little value to investors, leads to additional complexity for both the staff and insurance companies, makes tagged data less useful (as a single product will have multiple identical tags under different registrants and IDs), and provides no upside.

Timing of Effectiveness and Compliance:

- The use of rule 485 as proposed would have a 6-month delayed compliance period. We believe that it is imperative that rule 485 be implemented before 12/31/2024 so insurance companies can file under rule 485(a) ahead of their May 1, 2025 annual update. We expect significant staff comments and would need to go to print by early April, so rule effectiveness as of early 2024 is insufficient.
- Can insurers comply early with certain provisions before complying with the full N-4 requirements? For instance, can insurance companies immediately use STAT financial statements and avoid preparing MD&A and executive compensation even before moving over fully to Form N-4?

Additional Asks:

- Please extend rule 482 to RILAs. These products should be able to be marketed similarly to like products (variable annuities and funds). The Commission can condition use of rule 482 on the submission of marketing materials for FINRA approval and that insurance companies comply with certain principles to ensure performance presentations are not misleading. Alternatively, the Commission staff can also review marketing materials in lieu of FINRA.
- Just like your are excluding RILAs from the need to file GAAP financials, MD&A, executive compensations and any pending ESG rule, for the same reasons (providing appropriate tailored disclosures), all insurance product securities shows be excluded from these inapplicable requirements.
- Do not refer to index-linked returns as “interest”. Fixed indexed annuities use this term because it is always positive. When an investor is subject to losses, the term “interest” is misleading or just unclear. While not required, insurance companies will likely gravitate to terms used in the form so consider using the most appropriate terms.

- Today, many of the reputable insurance companies hold RILAs and variable annuities to the same standards. They both comply with the 2-day/5-day rule, are redeemable in 7 days, and set rates and fees that are reasonable in relationship to the services rendered and risks assumed under the contract. If RILA issuers want to be treated like N-4 registered products, the Commission should make all RILAs comply with these provisions. This can be accomplished by building these requirement into rule 12h-7 or rule 482 or condition the use of statutory financial statements and the exclusion of executive compensation, MD&A and any pending ESG disclosures on compliance with these provisions. After all form N-4 was designed as it is for variable annuities in part because the Investment Company Act has built in guardrails designed to protect investors. (For example, a RILA investor need not be concerned about executive compensation if they can be assured the rates they are charged are reasonable.). This will also help address the concern about RILA issuers reserving the right to charge exceptionally low crediting rates.

A note about SEC staff reviews:

- About 20 requests for 3-13 relief have been filed over the last 4 years. These requests have been substantially identical; however, it takes the staff more than 6 months to grant a request that is substantially identical to prior relief. The requests are just a few pages. In the interests of a level playing field and good government, the staff should process these requests more quickly. Alternatively, the SEC should consider granting class relief in this area. It is better to grant relief as part of this rulemaking which is subject to public comment than for the staff to grant this relief on its own accord. The staff should also be more open to granting similar relief to products issued by regulated insurance companies and where the products are themselves regulated for all the same reasons it grants relief to RILAs, MVAs and CDAs.
- Many of the proposed disclosure requirements have been enforced by some of the SEC's disclosure review staff for years, without regard to form requirements, notice and comment, or PRA requirements. The Commission should instruct the staff to stick more closely to the forms the Commission has adopted and only impose additional requirements where there are significant additional risks to investors as compared to the products contemplated by the form.
- There appear to be 2 SEC disclosure review branches responsible for RILA products. One branch requires robust disclosure about maximum losses and maximum negative interim value adjustments, forcing insurers to guarantee the availability of certain options, disclosing maximum interim value adjustments as

fees, and requiring “pages” of cover page disclosure. Another branch seems more even keeled. The Commission should ensure consistent treatment and application of form requirements to the same product by the disclosure review staff.

- More generally, insurance products used to be reviewed by a dedicated SEC staff known as the Office of Insurance Products. They were responsible for all aspects of insurance product regulation under the federal securities laws (disclosure review, rulemaking, interpretive relief, exemptive relief, etc.). It also appears that the Division of Investment Management has lost significant expertise over the years with the recent retirements of Susan Nash, Bill Kotapish, Keith Carpenter and Harry Eisenstein who were all insurance product subject matter experts. It now seems that are just a few staff member remaining with a deep understanding of insurance products (such as Sally Samuel, Liz Bentzinger and Michael Kossoff). Given the complexity and specialized nature of insurance products, we highly encourage the SEC to reinstate such an office and rebuild its insurance product expertise. Currently, it seems that many in the Chief Counsel’s Office and Disclosure Review Office seem to lack sufficient familiarity or interest in insurance products (and in fact have told some of us as much). A dedicated office with deep expertise should focus on these products as they products are seeing significant renewed interest from investors and increasing complexity.

Thank you for your consideration. We believe that insurance products serve an important role in protecting the retirement of Americans. The regulation of these products should be fair and the disclosures should be informative and balanced.

Sincerely,

VIP Working Group