January 19, 2012

Mr. Felix Schirripa  
Chief Actuary, New Jersey Department of Banking and Insurance  
Chair, NAIC Contingent Annuities Working Group  
20 West State Street  
PO Box 325  
Trenton, NJ 08625

Re: Consumer Need for Contingent Annuities and Proper Classification of Contingent Annuities as Annuities under State Law

Dear Mr. Schirripa:

The Insured Retirement Institute (IRI)\(^1\) appreciates the opportunity to provide comments regarding the consumer need for contingent annuities and the proper classification of contingent annuities as annuities under state law. In this letter, we will discuss: (1) the retirement income crisis facing consumers in America and the vital and unique role contingent annuities and other insured retirement products play in helping consumers protect against the risk of outliving their assets; (2) the current public policy focus at the federal government level on this crisis and steps federal policy makers are taking to encourage and facilitate the use of annuities for guaranteed lifetime income; and (3) IRI’s strong view that contingent annuities are annuities under state law, a product that can only be sold by life insurers, and not financial guaranty insurance, a product that can only be sold by property and casualty companies.

\(^1\) The Insured Retirement Institute has been called the “primary trade association for annuities” by \textit{U.S. News and World Report} and is the only association that represents the entire supply chain of the insured retirement strategies industry. Our members include major insurers, asset managers, broker dealers, banks and financial advisors. We currently have over 500 member companies and provide member benefits to more than 80,000 financial advisors and 10,000 home office financial professionals. IRI is a not-for-profit organization that brings together the interests of industry, financial advisors and consumers. Our mission is to: (1) encourage industry adherence to highest ethical principles; (2) promote better understanding of the insured retirement value proposition; (3) develop and promote best practice standards to improve value delivery; and (4) advocate before public policy makers on critical issues affecting insured retirement strategies.
Letter to NAIC Contingent Annuity Working Group
January 19, 2012
Page 2 of 6

Retirement Income Crisis In America and the Role of Insured Retirement Products

As a part of its review of contingent annuities, which provide consumers protection against the risk of outliving their assets, we encourage the National Association of Insurance Commissioners (NAIC) to conduct its review in the context of the current state of retirement savings readiness in America and the need for consumers to insure against the risk of outliving their assets (longevity risk). When considering the number of people at risk outlined in this letter and the financial consequences of not protecting against that risk, in the aggregate and individually, the financial longevity risk faced by consumers in America is without question very significant and likely greater than any other insurance risk many consumers face.

Seventy-nine million Baby Boomers today face immediate and unprecedented retirement income challenges—challenges that simply did not exist in earlier generations. Nearly half of these Boomers, over 35 million Americans, are “at risk” for inadequate retirement income, not having sufficient guaranteed lifetime income. Just as concerning, nearly half (45%) of Generation X (ages 36-45) are “at risk” for inadequate retirement income. Alarming, only 40 percent of Americans 30-49 years of age have tried to determine how much they need to save by the time they retire. Meanwhile, nearly one-third of Baby Boomers cite having adequate retirement assets as a top concern, while over half said they will work for income in retirement, meaning they actually will not be retired. However, boomers who own insured retirement products, which include contingent annuities, have a higher confidence in their overall retirement expectations, with 9 out of 10 believing they are doing a good job preparing financially for retirement.

Making the need for retirement savings even greater, individuals are living longer than those of earlier generations. If both spouses are now age 65, there is a 50% chance that one spouse will live to age 92, and a 25% chance that one will live to age 97. Half of today’s 65-year-old men are expected to live to age 85, and half of today’s 65-year-old women are expected to live to age 88. Compounding the concern about retirement income security, in other words, having sufficient income for a lifetime, the cost of health care is expected to be staggering in the years ahead. For a married couple now age 65, the cost of health care and nursing home care over

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2 Employee Benefits Research Institute (EBRI) Retirement Confidence Survey (2011)
3 Ibid.
4 Ibid.
5 Ibid.
6 Ibid.
7 U.S. Annuity 2000 Mortality Table, Society of Actuaries
8 Ibid.
the remainder of their lives is expected to be $260,000.\(^9\) Finally, nearly 50% of Baby Boomers believe they will not have enough money to pay for long-term care during retirement.\(^10\)

The shift from defined benefit to defined contribution plans, longer life spans, and the rising costs of health care are among the challenges that will put a significant retirement savings and income burden on the shoulders of individual consumers, in particular middle-income Americans, and employer defined contribution plan fiduciaries. This reality underscores the critical importance of a regulatory environment that encourages companies to create insured longevity risk protection products like contingent annuities and other annuities and a regulatory environment that provides consumers access to products that meet their needs to protect against longevity risk.

**Federal Government Actions to Encourage and Facilitate the Use of Guaranteed Lifetime Income Products like Contingent Annuities**

As a result of the imminent retirement income crisis (consumers’ lack of sufficient guaranteed lifetime income), there has never been as much public policy focus at the federal government level on encouraging and facilitating the use of guaranteed lifetime income products like contingent annuities by consumers in America. The President’s Middle Class Task Force has recommended “promoting the availability of annuities and other forms of guaranteed lifetime income, which transform savings into guaranteed future income, reducing the risks that retirees will outlive their savings or that their retirees’ living standards will be eroded by investment losses or inflation.”\(^11\) The Departments of Treasury and Labor are currently considering ways to facilitate “access to, and use of, lifetime income or other arrangements designed to provide a stream of lifetime income after retirement.”\(^12\) The Congress is considering the *Lifetime Income Disclosure Act* (S. 267 and H.R. 677), which will help workers understand their needs and plan for a secure retirement by providing them with an estimate of their potential guaranteed lifetime income monthly payments. The Senate Health, Education, Labor and Pensions Committee is also focused on the retirement savings challenges facing our country and has held a number of hearings on this issue, including a hearing to consider the Report of the General Accountability Office titled, “Retirement Income: Challenges for Ensuring Income throughout Retirement.”

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\(^9\) 2010 Study conducted by the Center for Retirement Research at Boston College
\(^10\) Insured Retirement Institute
\(^11\) See White House Fact Sheet: Supporting Middle Class Families. See also Annual Report of the White House Task Force on the Middle Class, 27 (February 2010).
\(^12\) See Request for Information on Lifetime Income Options for Participants and Beneficiaries in Retirement Plans, 75 Fed. Reg. 5253, 5255 (February 2, 2010).
IRI commends the President’s Administration and the Congress for their leadership on these issues. The retirement savings crisis facing Americans should be a high priority for all public officials, both at the federal and state levels.

Therefore, we ask NAIC and state regulators to take actions consistent with these efforts to encourage and facilitate the use of guaranteed lifetime income products, including contingent annuities. The NAIC and state regulators can do this by taking a clear position that contingent annuities are annuities under state law and assuring a prompt approval process that provides consumers, hundreds of thousands or millions, access to these products they need.

To be clear, insurance companies and their distribution partners are the only providers of guaranteed lifetime income products, including contingent annuities. Therefore, consumer access to these products is dependent on positive insurance regulatory actions. As a practical matter, enormous consumer populations will not be exposed to and therefore will not have access to guaranteed lifetime income products if contingent annuities are not available in the marketplace.

As such, state regulatory actions are critically important and have an enormous impact on the industry’s ability to meet the needs of American citizens. Again, we ask that the NAIC and state regulators take a clear position that contingent annuities are annuities under state law, consistent with the analyses previously outlined by numerous interested parties, including the American Academy of Actuaries, and as set forth in this letter.

**Contingent Annuities are Annuities Under State Law**

IRI’s strong view is that contingent annuities are annuities under state law and should be classified as annuities under state law. This position is supported by the analysis performed the American Academy of Actuaries, numerous state regulators who have approved these products under state laws governing annuities, IRS rulings, the comprehensive and rigorous legal analysis outlined in the letter from Great West Life and Annuity Insurance Company to the Life Actuarial Task Force dated April 28, 2011 (“Great West Letter”), and the long standing recognition and approval of guaranteed living withdrawal benefits (GLWB) as annuity products by state insurance regulators since introduction into the marketplace over 10 years ago, as well as adoption of GLWB standards by the Interstate Insurance Product Compact Commissioner (IIPRC) in June 2010.

**Academy’s Report.** As outlined in the Academy’s report:

“The [Academy Contingent Annuity Working Group] has reviewed the existing regulatory structure and concluded that the basic regulatory framework in place for other products can be applied to contingent annuities with little or no modification -
principally since the NAIC models for reserves and risk-based capital already exist, and the fact that all states have procedures in place that can allow for approval of GLWBs. It is logically consistent to classify the contingent annuity product as an annuity from an actuarial or risk perspective, and not as a form of financial guaranty insurance. The contingent annuity has a comparable structure to other annuity products based on the risks insured and the benefits paid to the consumer. . . .”

In testimony to the NAIC Life and Annuity Committee, the Academy representative stated, “We believe [the NAIC] should classify a contingent annuity as an annuity and not as a financial risk product. The product has a material longevity component, and the life industry has the experience to manage these risks.”

The Academy has also firmly concluded that financial guaranty products (e.g., bond insurance) protect against specific types of financial losses and contain no life contingent element, unlike a contingent annuity.

**Contingent Annuities Embody the Core Concept of Annuities.** As set forth and detailed fully in the Great West Letter, the core concept of an annuity is an “obligation” or “agreement” “to make periodic payments.” This is reflected universally in the statutory definitions found in the codes of those states that set forth a definition, recognized legal treatises, common law, and case law. Contingent annuities, which provide a GLWB, fall squarely within this definition.

**Contingent Annuities are Not Financial Guaranty Insurance.** As also explained in the Great West Letter, contingent annuities are simply not financial guaranty insurance. The withdrawals from the account are not “changes in the value of specific assets or commodities . . . or price levels in general,” as contemplated by certain financial guaranty insurance statutes. Rather, the withdrawals constitute the removal of assets from the account. The withdrawals therefore are not the kind of “changes in value” that relate to financial guaranty insurance. Yet, as the Academy and others have concluded, the withdrawals and the number of them through time are the primary and most actuarially significant factors in account depletion, and those in turn depend on how long a contract owner lives (longevity).

Explaining this further, the Great West letter continues:

“Financial guaranty insurance, by contrast, has no mortality risk factor whatsoever. Mortality risk is a wholly alien concept to financial guaranty insurance. Assuming financial guaranty insurance could be written on market risk, only market risk would be factored into the underwriting and reserving. Mortality risk is absolutely critical to the underwriting and reserving for Contingent Annuities.”
GLWBs are Classified as Annuities and Contingent Annuity GLWBs Operate the Same Way in All Material Respects. A GLWB offered as an element of a Contingent Annuity works in all material respects the same way as a GLWB offered through a variable annuity. Both are withdrawal benefits that provide guaranteed payments for the remainder of a contract owner’s life. State regulators have long classified and approved GLWBs as annuity products and the Compact has adopted GLWB product standards. Given these products operate the same way in all material respects, contingent annuities offering a GLWB should be classified as an annuity.

Consistent with or in addition to the reasons set forth in the letters and reports submitted by other interested parties, IRI’s strongly holds the view that contingent annuities are annuities under state law because contingent annuities:

1. Provide a lifetime series of payments, the very hallmark of an annuity contract;
2. Offer guaranteed income to a policyholder for his or her remaining lifetime, a feature that can only be provided by a life insurance company;
3. Permit, once payments from the issuing insurance company begin, the continuation of those payments based solely on the longevity of the policyholder;
4. Provide a level of annual income as dictated by the terms of the contract benefit; and
5. Can be written only by life insurance companies, which have the actuarial and reserving expertise to offer all guaranteed income products, unlike property and casualty companies.

**Conclusion**

Based on the forgoing analysis and the analysis of other interested parties, we request that the NAIC and state regulators take a clear policy position that contingent annuities are annuities under state law and assure a prompt approval process that provide consumers access to these products they need.

With best regards,

J. Lee Covington II  
Senior Vice President & General Counsel  
Insured Retirement Institute (IRI)