



**Comments of the Center for Economic Justice  
to the NAIC Model Act to Conduct Examination Standards  
August 7, 2017**

CEJ submits the following comments on:

- Additions to the Act
- Actuarial Guideline 49
- Additional provisions on process review and compliance risk review methodologies.

**Additions to Market Regulation Handbook Related to AG 49**

Our comments refer to page numbers of the exposed draft.

Page 3 of 78: STANDARDS, OPERATIONS/MANAGEMENT, Standard 1 The regulated entity files all certifications with the insurance department, as required by statutes, rules and regulations.

Discussion: This standard requires the annual certification requirements required of the illustration actuary in the Life Insurance Illustration Model Regulation (Model 582) – regarding compliance with the requirements of the scales used in the illustration. Section 11F also requires a certification by “a responsible officer of the insurer, other than the illustration actuary” that the requirements have been met and that expense allocation information has been provided to the producer. In model 582, model 582 specifies the methodology to cap the illustrated crediting rates in the “current scale” and specifies that another “illustrated scale” must use crediting rates that are not less than the current scale (those in the current scale or the currently payable scale).

Actuarial guideline 49 and Model 582 supersede some illustration requirements in the current scale.

In addition, Model 582 includes certification requirements of the producer or representative. Section 7D(2) is a requirement for a producer or representative to certify having made the following truthful statement to the applicant for insurance: “I certify that this illustration has been presented to the applicant and that I have explained that any non-guaranteed elements illustrated are subject to change. I have made no statements that are inconsistent with the illustration.” Section 9B(1) and of the model requires a certification “If no illustration is used by an insurance producer or other authorized representative in the sale of a life insurance policy or if the policy is applied for other than as illustrated, the producer or representative shall certify to that effect in writing on a form provided by the insurer. Section 9D of the model requires the insurer to maintain a copy of the basic illustration and any certifications that no illustration was used for three years after the policy is no longer in force.

In addition, Model 580 – the Life Insurance Disclosure Model Regulation – requires a policy summary for products sold without an illustration pursuant to Model 582. However, Model 582 permits an illustration within the policy summary based on “nonguaranteed elements:”

“Nonguaranteed elements” means the premiums, credited interest rates (including any bonus), benefits, values, non-interest rates, and other elements of the policy. ~~It~~ <sup>is</sup> ~~not~~ <sup>to</sup> be used to illustrate the policy.

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Market regulators should also be aware that sales of products, such as fixed -index annuities (formerly referred to as equity -indexed annuities) and index life insurance products (such as universal index life insurance) continue to increase. These products typically include features that require an understanding of bonuses, guaranteed elements and an array of interest -cre



Page 18 of 78: STANDARDS, MARKETING AND SALES, Standard 4, An illustration used in the sale of a policy contains all required information and is d

Testing the compliance of illustrations with Model 582 and AG 49 will be complex and the examiner will likely seek assistance from an actuary familiar with and capable of testing compliance with Model 582 and AG49. However, the examiner should request and obtain information from the insurer necessary for the actuary or other person with expertise in testing illustrations' compliance. The examiner may be able to test implementation compliance issues by confirming that IUL illustration changes were made on or before the effective dates set out above. For example,

Did the insurer implement on or before September 15, 2015 a compliant crediting rate methodology for new and in-force illustrations on policies sold on or after September 15, 2015?

Did the insurer implement on or before March 1, 2016 a compliant credit rate methodology all new illustrations

For new business and in force life insurance illustrations on policies sold on or after March 1, 2016, ensure that the basic illustration includes a table showing the minimum and maximum of the geometric average annual credited rates as referenced in Section 7.B.

For new business and in force life insurance illustrations on policies sold on or after March 1, 2016, ensure that the basic illustration includes a table showing actual historical index changes and corresponding hypothetical interest rates using current index parameters for the most recent 20-year period for each Index Account illustrated, as required by Section 7.C

Page 42 of 78: STANDARDS, MARKETING, AND SALES, Standard 14: The insurer has procedures in place to provide full disclosure to consumers regarding all sales of products involving index life and all sales are in compliance with applicable statutes, rules and regulations.

We make the same suggestion as above for placing the new reference to AG 49 with Model 582.

Life Insurance Illustrations Model Regulation (#582) and Actuarial Guideline 49 – The Application of the Life Illustrations Model Regulation to Policies with Index Based Interest

We make the same suggestion for documents to be reviewed

Page 75 of 78: Supplemental Checklist

We support the addition of this checklist. We suggest the addition of other items related to implementation of AG49:

For new business and in force life insurance illustrations on policies sold on or after September 1, 2015, determine whether the credited rate for the Illustrated Scale has been limited according to the requirements of Section 4

For new business and in force life insurance illustrations on policies sold on or after September 1, 2015, determine whether the earned interest rate for the Disciplined Current Scale hasMi



In this paragraph, process review is presented as a tool to “determine the credibility of the issue being considered” and “pinpointing failures” in Company processes causing the adverse outcome and a “remedial tool.” The process review described is based on the assumption that a problem has been identified by some other means with consumer complaints proffered as the most effective of these tools.

With a little bit of overstatement, process review is a solution in search of a problem. In our view, market regulators need much better tools to identify poor consumer outcomes – certainly much better than consumer complaints or the current Market Conduct Annual Statement. Consider that Wells Fargo falsely placed 800,000 force-placed policies on auto loan borrowers over a five year period causing hundreds of thousands of delinquencies and tens of thousands of defaults and repossessions. Yet, consumer complaints did not bring this conduct of the force-placed insurers to whom Wells Fargo had outsourced the tracking and force-placed insurance placement.

Similarly, even when consumer complaints or MCAS raise a concern, these tools are so blunt that much further examination is needed. Mr. Koch’s stated rationale for the process review is a result of the inadequate market monitoring tools available to regulators. While Mr. Koch simultaneously criticizes analysis of granular market outcome data – “it is not particularly helpful to sift all outcomes to find the ones that are of interest because they are harmful” – and asserts that there are existing tools to identify the harmful outcomes, his description of the process review methodology is simply a non-data methodology to identify harmful market outcomes.

As stated in our July 19, 2017 comment, process review or compliance risk methodologies may have a role in market regulation, but they are not a substitute for or precursor to the collection and analysis of granular market outcome data – data far more granular than currently being collected.

Consider the following scenario. A consumer complaint or MCAS indicates a potential problem with suitable sales of complex annuities or life insurance products. We know that with MCAS, the problem will have to be severe to cause the company to be an outlier, so the bad outcomes produced by a bad producer may not cause anything noticeable in MCAS ratios. Similarly, there may or may not be a number of complaints regarding the producer. Utilizing process review in this context is, literally, a fishing expedition that might involve an extensive review of a number of systems and processes for a problem limited to a single producer and a single system or manager.

Now consider how this problem might be identified if MCAS consisted of data on every life insurance and annuity sale including key characteristics of the sales transaction including specific type of product, producer involved, consumer characteristics, product characteristics. By utilizing robust data mining and statistical analysis, the market analyst could identify unsuitable sales by a specific producer or for a specific product. Armed with this analysis, the regulator is much better positioned to examine the causes of the problem and to ascertain whether there is a systemic problem with company processes or a problem limited to particular products, producers or classes of consumers.

As a tool for market regulators, the process or compliance risk review requires much more specific description of the types of situations in which it can be used. But, the broad application of process or compliance risk review set out in the proposals as a tool to identify causes of bad consumer outcomes is more appropriately a tool marketed to insurers to help them evaluate and improve their processes to ensure consumer market outcomes. The process or compliance risk review proposals are further inappropriate for market regulators because they reflect and perpetuate a particular view of what good corporate governance and procedures regarding treatment of consumers should be. Our view is that regulators should focus on identifying market problems and poor consumer outcomes when they occur and not attempt to become partners with insurers for corporate governance related to market regulation.

In summary, process or compliance risk review may have a role in market regulation if the specific circumstances of its use are clearly articulated and if process or compliance risk review has a limited and clearly defined role. As presented, these proposals articulate a broad role for process and compliance risk review serving as an alternative to traditional examination methodologies.

But, the most important point we wish to make is that the future direction of market regulation should be one in which more granular consumer market outcome data are collected and analyzed by market analysts utilizing the same types of Big Data tools as insurers, but for purposes of more efficient and effective market regulation. We ask the Market Conduct Examination Standards Working Group to join in this vision of the future of insurance market regulation and recommend to the Market Regulation Committee and the NAIC to move towards a regulatory Big Data future by enhancing the Market Conduct Annual Statement with transaction detail data on individual sales and claims.