December 15, 2016

Technical Director

File Reference No. 2016-330
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116

Re: File Reference No. 2016-330 – Proposed Accounting Standards Update, *Targeted Improvements to the Accounting for Long-Duration Contracts (Financial Services – Insurance Topic 944)*

Dear Technical Director:

We appreciate the opportunity to comment on the exposure draft of the Proposed Accounting Standards Update, *Targeted Improvements to the Accounting for Long-Duration Contracts* ("the Proposed ASU"). Nationwide and its subsidiaries ("Nationwide") is comprised of three affiliated mutual insurance companies and their subsidiaries under common management, operating both property and casualty and life insurance companies. Nationwide ranks number 69 in the Fortune 100 rankings and is one of the largest diversified insurance and financial services organizations in the world, with assets of over $200 billion. Nationwide is also a top 10 writer of life insurance products and variable annuities in the United States, a vast majority of which provide guaranteed benefits.

While we have supported and continue to support the efforts of the Financial Accounting Standards Board ("the FASB" or "the Board") to make targeted improvements to the accounting for long-duration contracts issued by insurance entities, we do not believe that all aspects of the Proposed ASU achieve the key objectives of the project or represent an improvement to current United States Generally Accepted Accounting Principles ("U.S. GAAP"). Specifically, while we agree that the decisions to periodically update assumptions for traditional products and simplify the amortization of deferred acquisition costs are improvements, we believe the proposed changes related to market risk benefits and discount rates would negatively impact the decision-usefulness of our financial statements.

In order to be meaningful and decision-useful to stakeholders, the accounting for long-duration contracts should reflect the underlying economics of these contracts, as well as how the business is managed and

product performance is evaluated. We do not believe the proposed requirement to fair value market risk benefits, as defined in the Proposed ASU, reflects the core fundamentals of certain benefits. Specifically, life-contingent benefits (i.e., those with inherent mortality or longevity risks), are not well-suited for a fair value model, as they have no value to the policyholder until the occurrence of an insurable event. These benefits are unlike all other financial instruments that are required to be carried at fair value in accordance with existing U.S. GAAP, as they are not marketable through a sale or otherwise redeemable. As such, a value based on a theoretical exit price, using current market assumptions, is inconsistent with the nature of these products, and is mostly unrelated to the ultimate benefit expected to be paid out. This creates financial statement results that are significantly impacted by short-term, often temporary, changes in the market. Such results are not reflective of the future expected cash flows, and are therefore difficult to understand and not decision-useful for our stakeholders. Instead, the accounting model should reflect the eventual payout of the obligation to the policyholder through an orderly insurance transaction, as that would be a more meaningful measure than an exit price for a liability that is generally unable to be exited otherwise.

In addition, we understand the Board's decision was partially based on stakeholder concerns that current U.S. GAAP creates a disincentive to hedge capital market risk exposures arising from these benefits. However, the Proposed ASU would have the unintended consequence of incentivizing companies to employ a particular risk management strategy in order to dampen the accounting volatility created by the proposed standard and not the real economics of the products. This issue is further compounded by the potential impacts to insurance company solvency if a fair value hedging strategy is employed. As a result, companies may be forced to choose between mitigating U.S. GAAP earnings volatility and managing solvency capital levels. Furthermore, additional costs borne by companies to expand their current hedging programs would result in real economic consequences that could ultimately be passed onto policyholders through product pricing.

We support the Board's decision to recognize changes in the discount rate in accumulated other comprehensive income. We also recognize that there is no perfect discount rate and agree with the theoretical merit of a liability discount rate. However, we do not believe the use of a high-quality fixed-income instrument yield, as required in the Proposed ASU, is representative of insurance liability cash flows. While the use of a defined rate would increase the transparency and consistency desired by the Board, the high-quality fixed-income rate does not reflect an adequate adjustment for illiquidity and therefore is not well-suited for measurement of insurance liabilities. While we understand the Board's desire to use a rate that exists in other U.S. GAAP today, despite their long-dated and illiquid nature, there are fundamental differences between pension plans and insurance companies that justify the use of a different rate. For example, pension plans may be unfunded, which makes the use of an expected yield inoperable. Additionally, pension plans may warrant a certain level of conservatism in their rates given the lack of regulatory funding requirements. By contrast, insurance companies are held to a high standard of capitalization imposed by regulatory requirements, thereby mitigating the need for additional conservatism to be layered into the discount rate used for insurance liabilities. An unintended consequence of using such a conservative rate is that it could cause losses at issuance for traditional and limited pay policies which are anticipated to ultimately be profitable.

Overall, we appreciate the Board's efforts to limit the project to only targeted improvements rather than a complete overhaul of the accounting for long-duration contracts. However, certain aspects of the proposed changes are both costly and will not provide the intended benefit to users of our financial

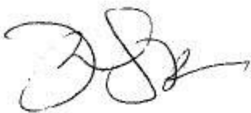
statements. As such, we respectfully request the Board to consider the following key recommendations relating to the Proposed ASU:

- Market Risk Benefits
    - Modify the scope of market risk benefits to exclude life-contingent benefits, and add clarifying guidance to existing U.S. GAAP to address preparer concerns around complexity, while ensuring the accounting model reflects the underlying economics of these benefits;
    - Permit insurance companies to irrevocably elect the fair value option for life-contingent benefits, allowing for offsetting accounting effects when a fair value hedging strategy is employed;
    - Require fair value disclosures for life-contingent benefits measured using the insurance accrual approach to provide users with a means of assessing these benefits on the same basis of accounting, without introducing non-economic income statement volatility that may lead companies to alter their hedging strategies for non-economic reasons; and
    - Allow a practical expedient upon transition to prospectively fair value any market risk benefits in which it is impractical to retrospectively apply the proposed guidance, as this approach is consistent with existing U.S. GAAP.

- Discount Rates
    - Perform additional stakeholder outreach and field study to determine a liability rate that is more representative of the illiquidity inherent in long-duration insurance contracts. Until a discount rate or discounting approach is developed that actually achieves the Board's objective of reflecting the characteristics of the liability, a change to current U.S. GAAP should not be made.

While we are supportive of the overall FASB project to make targeted improvements to long-duration contracts, we have significant concerns that the proposed guidance for market risk benefits and discount rates will not achieve the Board's objectives, and also will not provide information that is reflective of the insurance business or useful to management and financial statement users for making sound economic decisions. We encourage the Board to consider the recommendations included above and in the attached appendix that includes Nationwide's response to the comprehensive listing of questions asked by the Board. In the event that any Board or staff member would like further clarification of our positions, please do not hesitate to contact us.

Respectively,



James D. Benson
Senior Vice President, Enterprise Controller and Chief Accounting Officer
Nationwide

APPENDIX

Liability for Future Policy Benefits—Contracts Other Than Participating Contracts

Question 1—Scope: Do you agree with the scope of the proposed amendments on the accounting for the liability for future policy benefits for contracts other than participating contracts? If not, what types of contracts, contract features, or transactions should be included in or excluded from the scope and why?

Yes.

Question 2—Cash flow assumption update method and presentation: Do you agree that the effect of updating cash flow assumptions should be calculated and recognized on a retrospective basis in net income? If not, what other approach or approaches do you recommend and why?

No. We do not believe the effect of updating cash flow assumptions should be calculated and recognized on a retrospective basis, and support the prospective approach recommended by the ACLI.

Question 3—Cash flow assumption update frequency: Do you agree that cash flow assumptions should be updated on an annual basis, at the same time every year, or more frequently if actual experience or other evidence indicates that earlier assumptions should be revised? If not, what other approach or approaches do you recommend and why?

No. We agree that cash flows should be updated on an annual basis, at the same time every year. However, insurance liabilities are very long-term in nature and no single quarter (or quarters) of experience would suggest a need to update company assumptions. Therefore, we recommend that the requirement be revised so that it does not imply a need to justify that the assumptions should be reviewed more frequently than annually, which only serves to create operational burden and offers no value to the users of the financial statements. This could be accomplished by stating that assumptions need only be revised when known material, adverse events impacting the cash flow assumptions have occurred.

Question 4—Discount rate assumption: Do you agree that expected future cash flows should be discounted on the basis of a high-quality fixed-income instrument yield that maximizes the use of current market observable inputs? If not, what other approach or approaches do you recommend and why?

No. While we agree with the theoretical merit of using a liability rate to discount expected future cash flows, we do not agree with the proposed use of a high-quality fixed-income instrument yield.

Inadequate Illiquidity Provision
While this proposal will result in consistency throughout the industry and transparency for users of financial statements, we believe it will result in a liability measurement that is not a faithful representation of the amount of benefits expected to be provided to policyholders. As noted in the

Board's basis for conclusions, there is no perfect discount rate and the proposed rate is meant to be a proxy of the risk-free rate plus liquidity adjustment. Typically, a high-quality fixed-income instrument has been interpreted as a fixed-income debt security that receives one of the two highest ratings given by a recognized rating agency. These debt securities are considerably more marketable than the liability for future insurance benefits, and therefore the proposed proxy rate would not take into consideration the illiquid nature of these future cash flows. While we appreciate the Board's emphasis on ease of operability, we do not believe the proposal would result in a liability that accurately reflects the future obligation, which should be the first objective of the guidance and would not represent an improvement to existing U.S. GAAP.

Conservatism
Although the basis for conclusions refers to a similar discount rate being used for pension obligations, we believe there are meaningful distinctions between pension obligations and insurance liabilities that make using the same proxy rate for both pensions and insurance liabilities inappropriate. While pension liabilities are also relatively illiquid, insurance companies are held to a higher standard of capitalization and investment requirements than a pension plan. The conservatism of this rate in the pension guidance may be warranted, whereas it would not be for insurance liabilities. While pension plans are generally not funded beyond accumulated and projected benefit obligations, insurance companies are subject to significant regulatory and capital standards to ensure there are necessary future cash flows to pay for policyholder liabilities, thereby mitigating the need for conservatism otherwise present in the high-quality fixed-income instrument yield. In addition, in certain cases the proposed rate could result in immediate losses being recognized for insurance contracts which are ultimately expected to be profitable, providing further evidence that the use of such a conservative rate would not provide a faithful representation of the liability.

Recommendation
We agree with the Board that there is no perfect discount rate. We also agree with the Board that a liability rate has theoretical merit. However, the proposal replaces one imperfect approach with an approach that would not be an improvement to existing U.S. GAAP. If the Board elects to change the guidance to utilizing a liability rate that is easily operable and observable, we recommend the Board perform further outreach to determine a liability rate that is representative of the illiquid nature of long-duration insurance contracts.

Question 5—Discount rate assumption update method and presentation: Do you agree that the effect of updating discount rate assumptions should be recognized immediately in other comprehensive income? If not, what other approach or approaches do you recommend and why?

Yes. We agree the effect of the updated discount rate assumptions should be recognized immediately in other comprehensive income. As small changes in the discount rate can result in material changes to the liability, measuring the effects of the change in the discount rate in earnings would drive significant earnings volatility for a liability that is very long-term in nature. Other comprehensive income is generally reserved for temporary market-driven changes and as such would align to guidance for other financial instruments.

Question 6—Discount rate assumption update frequency: Do you agree that discount rate assumptions should be updated at each reporting date? If not, what other approach or approaches do you recommend and why?

Yes. We agree that discount rate assumptions should be updated at each reporting date. This would provide the most accurate picture of capital for users, as this would coincide with updating of assets measured at fair value.

Liability for Future Policy Benefits—Participating Contracts

Question 7—Scope (participating contracts): Do you agree with the scope of the proposed amendments on the accounting for the liability for future policy benefits for participating contracts, including closed block contracts issued by a demutualized insurance entity? If not, what types of contracts, contract features, or transactions should be included in or excluded from the scope and why?

No. Consistent with the ACLI response, we recommend that closed block contracts issued by a demutualized insurance entity be excluded from the scope of the Proposed ASU.

Question 8—Cash flow assumption update method and presentation (participating contracts): Do you agree that the effect of updating cash flow assumptions should be calculated and recognized on a retrospective basis in net income? If not, what other approach or approaches do you recommend and why?

No. We do not believe the effect of updating cash flow assumptions should be calculated and recognized on a retrospective basis, and support the prospective approach recommended by the ACLI.

Question 9—Cash flow assumption update frequency (participating contracts): Do you agree that cash flow assumptions should be updated on an annual basis, at the same time every year, or more frequently if actual experience or other evidence indicates that earlier assumptions should be revised? If not, what other approach or approaches do you recommend and why?

Yes.

Question 10—Discount rate assumption (participating contracts): Do you agree that expected future cash flows should be discounted on the basis of a high-quality fixed-income instrument yield that maximizes the use of current market observable inputs? If not, what other approach or approaches do you recommend and why?

No. We do not agree with the use of a high-quality fixed-income instrument yield discount rate and would support the approach recommended by the ACLI.

Question 11—Discount rate assumption update method and presentation (participating contracts): Do you agree that the effect of updating discount rate assumptions should be recognized immediately in other comprehensive income? If not, what other approach or approaches do you recommend and why?

Yes.

Question 12—Discount rate assumption update frequency (participating contracts): Do you agree that discount rate assumptions should be updated at each reporting date? If not, what other approach or approaches do you recommend and why?

Yes.

<u>Market Risk Benefits</u>

Question 13—Scope: Do you agree with the scope of the proposed amendments on the accounting for market risk benefits? If not, what types of contracts or contract features should be included in or excluded from the scope and why?

No. While we understand stakeholder concerns around complexity and consistency, we do not believe fair value measurements accurately reflect the true economic value for all market risk benefits, and therefore the Board should modify the scope of market risk benefits. Specifically, we recommend that the definition of market risk benefits exclude life-contingent benefits with inherent mortality or longevity risk, as we believe accounting for these benefits under an insurance accrual model is more reflective of the economic obligation and long-term nature of these liabilities.

<u>Economic Value of Life-Contingent Benefits</u>
Fair value accounting generates values that are very sensitive to short-term changes in interest rates, despite the fact that these interest rate movements have little to no impact on the amount ultimately paid for these benefits. Included within Exhibit 1 are examples that demonstrate the volatility that is experienced when life-contingent benefits are measured at fair value. As shown in Exhibit 1, under a fair value model, a minor fluctuation in interest rates suggests that a benefit that will be paid many years in the future (i.e., often 30 or more years in the future) suddenly has significantly more or less value, even though the capital market environment at the time of the insured event is unknown and has very little, if any, relationship to the short-term event that has occurred. While this model may be appropriate for those liabilities that involve marketable commodities and securities, as noted in FASB Concepts Statement No. 5, this model would be inappropriate for life-contingent benefits, which are not marketable or otherwise redeemable.

Further, we understand that the proposed fair value treatment is based on the Board's view that capital market movement is the most important driver of how much will be owed to the policyholder, while the occurrence of the insured event primarily drives the timing of when the liability occurs. However, the occurrence of the insured event drives the amount paid on life-contingent benefits just as much as, if not more than, the capital market variables. For example, with a guaranteed lifetime withdrawal benefit ("GLWB"), the total amount paid on the guarantee is dependent on how long the policyholder lives and when the policyholder elects withdrawals. While we recognize that these insurance risk assumptions are

incorporated within the fair value model, we do not believe a model derived from the exit price at the balance sheet date is appropriate, especially given that insurance companies do not have the opportunity to exit the obligation at that date or at that calculated exit price. Instead, the use of an insurance accrual model better reflects the long-term nature of these benefits and the intended settlement of these obligations through the eventual payout to policyholders. Furthermore, as the insurance accrual model results in the ratable build up of the liability, we believe the resulting equity better reflects the available capital after providing for future insurance obligations, and is more reflective of how companies manage their business.

Interaction with Risk Management
Given that we do not believe the proposed fair value treatment reflects the true economic value of life-contingent benefits, we have further concerns about the potential impacts of this treatment on companies' risk management strategies. The Board's basis for conclusions states that measuring market risk benefits at fair value would better align the accounting for these benefits with the related accounting for insurance entities' risk management activities (i.e., hedging). However, we disagree that the Proposed ASU would better align with all insurance companies' risk management strategies and could instead force companies into a particular risk management strategy. For example, many companies choose to hedge only the portion of these benefits that they expect to result in future liabilities, or manage their hedging programs based on statutory surplus or capital volatility. The proposed fair value treatment could force these companies to purchase new hedging instruments simply to minimize the accounting impact of temporary or short-term movements. Said another way, the proposed accounting change may have the unintentional consequence of dictating risk management decisions, instead of providing transparency into how companies manage their business. It is even possible that in some circumstances fair value hedging could result in a company going insolvent as a result of massive losses on interest rate hedges, even though true policyholder liabilities (and therefore statutory reserves) are not decreasing. For example, in November 2016, market conditions could have resulted in companies that employ fair value hedging to have lost in excess of a billion dollars on interest rate hedges. As statutory reserves are floored at the cash surrender value, these market movements would have little, if any, impact on the statutory reserve, and as a result, would cause significant solvency concerns.

Furthermore, forcing companies to employ a fair value hedging strategy only to mitigate accounting volatility would be costly to implement and maintain, creating real economic disadvantages in order to manage non-economic accounting results. These incremental costs, including the ongoing additional costs of hedging, could ultimately be passed to the policyholder through increased product pricing.

Moreover, there may be unfavorable impacts of the Proposed ASU at the time of transition. Specifically, we are concerned with the availability at transition of hedging instruments in the marketplace that may result from companies' implementing larger hedging programs in response to the Proposed ASU. We are also concerned with hedging mismatches that might occur upon transition. As the Proposed ASU would apply to the earliest period presented, companies that modify their hedging strategy as of the effective date may have unhedged volatility reflected in prior period earnings, which may cause confusion for financial statement users and would impact comparability between reporting periods.

Recommendation to Allow Fair Value Option

As each insurance company manages risk differently, we realize that some companies may desire to record life-contingent benefits at fair value based on their individual risk management and hedging strategies. As a result, we recommend that companies should be able to irrevocably elect the fair value option for these benefits, at transition and as products are introduced. This treatment would be consistent with other existing guidance, particularly the optional application of hedge accounting and trading designations.

We realize that existing guidance under ASC 825-10-25-7 does not permit the fair value option to be elected only for the benefit (i.e., it must be elected for the entire contract, meaning the base contract and riders). As part of the Board's basis for conclusions for the fair value option accounting standard (i.e., SFAS No. 159), it states that electing only a portion of an asset or liability would not meet the objective of expanding the use of fair value measurements. However, we contend that permitting the fair value option for life-contingent benefits on a stand-alone basis would, in fact, still expand the use of fair value measurements. Furthermore, accounting for these benefits separately from the base insurance or annuity contract is consistent with existing accounting guidance and the Proposed ASU.

Although current U.S. GAAP permits companies to elect the fair value option on an instrument-by-instrument basis, we recommend that this election be made at a more aggregated level (i.e., by product feature within a guaranteed benefit). The Board's basis for conclusions for the instrument-by-instrument election decision specifically notes that this allows companies to achieve offsetting accounting effects of the changes in fair value without having to apply complex hedge accounting. As it is common industry practice to manage risks at the product feature level (or higher), we believe that this more aggregated election option would be appropriate.

Complexity

Within the Board's basis for conclusions and as noted above, the Proposed ASU was based on stakeholder concerns over the complexity that is required under current U.S. GAAP when evaluating whether benefits should be accounted for as an embedded derivative in accordance with ASC 815. This complexity could be better addressed through amendments to existing guidance. For the majority of market risk benefits, preparers have evaluated existing guidance and arrived at well-founded accounting conclusions that are consistent within the industry. However, as noted in the Board's basis for conclusions, there has been diversity in practice as it relates to the accounting treatment of certain life-contingent benefits (e.g., GLWBs) as there is not explicit authoritative guidance, and preparers have analogized implementation guidance for other benefits to determine the proper accounting treatment. To address this issue, we recommend a scope exception be added to ASC 815-10-15-13 to exclude all life-contingent benefits (including those benefits that include both life-contingent and non life-contingent elements). As a result, life-contingent benefits would be measured using the insurance accrual approach within ASC 944, which, as stated above, is more reflective of the true economic value.

We believe the spirit of existing guidance within ASC 815-15-55-59 supports this treatment. This guidance concludes that net settlement criteria for derivative classification have not been met for certain guaranteed minimum income benefits, with a determining factor that a policyholder has no immediate access to the economic benefit of the guarantee at the end of the accumulation period or during payout and the only way for the policyholder to access the benefit is to continue to live. We believe this underlying concept applies to all life-contingent benefits, and therefore these benefits would not be

considered embedded derivatives and should be excluded from the scope of ASC 815. By excluding life-contingent benefits from the scope of ASC 815, there would be greater clarity for preparers and reduce the diversity in practice that exists today. Further, this treatment would result in guarantees with inherent longevity risk, such as GLWBs, and guarantees with inherent mortality risk, such as guaranteed minimum death benefits ("GMDBs"), to be accounted for on the same accounting basis, which supports the Board's consistency objective, given the similar underlying economics of these guarantees and the long-term nature of these risks that both vary with the lifespan of the policyholder.

Comparability

We do not believe that a mandated fair value model promotes comparability for life-contingent benefits. Given that there is not an active market for these benefits, fair value measurements would be based on significant unobservable inputs and the measurement of these benefits would be more subjective under the Proposed ASU. Although the Proposed ASU does provide for enhanced quantitative and qualitative disclosures around the assumptions used in the fair value measurement of these benefits, the extensive range of inputs that would be disclosed for many assumptions (e.g., mortality, lapse rates, annuitization rates, withdrawal utilization, and equity volatility) would not result in transparent and meaningful disclosures for the financial statement users.

While we do not believe that fair value measurements create comparability due to the subjectivity required in measuring life-contingent benefits, we do recognize stakeholder desires to assess benefits on the same basis of accounting. Therefore, should the Board decide fair value is an alternative basis worth measuring for these benefits, similar to other financial instruments not carried at fair value, we recommend that stakeholder concerns be achieved through disclosures instead of measurement through the financial statements. Specifically, we recommend that fair value disclosures in accordance with ASC 825-10-50-10 be required for life-contingent benefits accounted for using the insurance accrual approach. This requirement would be consistent with existing U.S. GAAP that permits other assets and liabilities to be measured on different bases of accounting, while requiring fair value disclosures (e.g., debt securities and servicing assets and liabilities). By disclosing the fair value of these benefits within the notes to the financial statements, users may assess benefits on the same basis of accounting, without introducing the volatility that is unrepresentative of the underlying cash outflows that will be paid for these benefits.

Question 14—Measurement: Do you agree that all market risk benefits should be measured at fair value, with fair value changes attributable to a change in the instrument-specific credit risk recognized in other comprehensive income? If not, what other alternative or alternatives do you recommend and why?

No. As discussed in our response to question 13, we do not believe life-contingent benefits should be defined as market risk benefits and measured at fair value. See our recommendations discussed in question 13 (i.e., modification of the market risk benefits definition, clarification of existing U.S. GAAP, allowance of the fair value option, and required fair value disclosures), which we believe would meet the objectives of the Board. If the Board were to revise the Proposed ASU to incorporate these recommendations, we would agree with the proposed measurement of market risk benefits.

Deferred Acquisition Costs

Question 15—Scope: Should the scope of the proposed amendments be expanded to include investment contract acquisition costs currently amortized using the interest method in Subtopic 310-20, Receivables—Nonrefundable Fees and Other Costs?

No. We do not believe that the scope should be expanded to include investment contract acquisition costs, and agree with the points raised in the ACLI comment letter.

Question 16—Amortization: Do you agree with the proposed amendments that would simplify the amortization of deferred acquisition costs? If not, what other simplified and reasonably estimable amortization approach or approaches do you recommend and why?

Yes. In addition, while we recognize the Proposed ASU does not explicitly change the amortization of value of business acquired assets, we recommend transition guidance be added to allow the simplified amortization model to be applied to the value of business acquired assets. This would alleviate the requirements to evidence preferability and apply the guidance retrospectively at transition.

Question 17—Impairment: Do you agree that deferred acquisition costs should not be subject to impairment testing? If not, what alternative or alternatives do you recommend and why?

Yes. We agree with the Board's decision not to require impairment testing for deferred acquisition costs, as we believe this is consistent with the Proposed ASU that has de-linked profits from the amortization of deferred acquisition costs. We believe that the benefits under the proposed simplified amortization model would essentially be eliminated if an impairment model were required, as an impairment model would require a profit analysis that would reintroduce complexities and elements of uncertainty, in addition to added operational and audit costs. Further, as noted in the Board's basis for conclusions, it would be challenging to propose an impairment model that would be both conceptually sound and not operationally burdensome. Moreover, we understand the theoretical merit of the Board's view that long-duration contracts are similar to financing arrangements, and deferred acquisition costs should be treated consistently with deferred borrowing costs.

Presentation and Disclosure

Question 18—Proposed requirements: Do you agree that the presentation and disclosure requirements included in the proposed amendments would provide decision-useful information? If not, which presentation and/or disclosure requirement or requirements would you change and why?

No. We are concerned with the volume of proposed disclosure requirements and share the industry's views, as documented within the ACLI comment letter.

Question 19—Additional requirements: Are there any additional presentation or disclosure requirements that would provide decision-useful information? If so, please describe them and explain why.

Yes. As noted in our response to question 13, we believe stakeholder concerns about the use of a consistent accounting model for market risk benefits can be addressed through fair value disclosures. As a result, we recommend the disclosure requirements within ASC 825-10-50-10 be required for life-contingent benefits that are measured using the insurance accrual model.

Effective Date and Transition

Question 20—Implementation date: The Board is interested in understanding the key drivers affecting the timing of implementation. What are those key drivers, and how do they affect the time it will take to implement the proposed amendments? Should the effective date be the same for both public entities and nonpublic entities?

We believe the Proposed ASU, as written, will result in significant operational efforts for implementation, and we share the industry's views documented within the ACLI comment letter. Further, we would support a one-year deferral of the effective date for nonpublic entities, consistent with other recently issued standards.

Question 21—Transition methods: Are the proposed transition provisions operable and do they provide decision-useful information? If not, what would you recommend and why?

No. As it relates to market risk benefits, we have significant concerns with the transition provision as it is inoperable. As proposed, companies would be required to retrospectively fair value the market risk benefits. Retrospective fair valuing of market risk benefits would require risk-neutral valuations for every contract as of the day they were issued, with the assumptions that were applicable at that time. We estimate that it would be impractical to retrospectively fair value a large portion of our market risk benefits, as this would require contemporaneous documentation of all assumptions for these contracts that date back to the 1970s. Due to the complexity of valuing these benefits, full Monte Carlo simulations would be required with assumption sets that were applicable at the date of issue. Therefore, documentation for this volume of assumptions would not be available for benefits that are currently measured under the insurance accrual approach. Furthermore, the complexity inherent in the risk-neutral valuations would preclude a practical expedient that would allow an estimate of these assumptions using readily available objective information (similar to what is permitted for the transition of the liability for future policy benefits within the Proposed ASU).

Due to the challenges stated above, we do not believe the proposed retrospectively-determined value would represent the true fair value of these benefits, and therefore they would not be meaningful for financial statement users. We thus recommend providing a practical expedient to prospectively fair value market risk benefits for which it is impractical to retrospectively apply the proposed guidance at transition. Specifically, we recommend setting the fair value of these market risk benefits at the time of transition to zero. While we understand there might be concerns with recording the fair value of these benefits at zero (and thereby reversing the existing insurance accrual reserve), the proposed guidance, as written, could result in the establishment of a significant net asset at the time of transition, depending

on capital market conditions, product design, and the resulting calculation of attributed fee ratios. Moreover, our proposed treatment is consistent with existing U.S. GAAP. ASC 815-15-30-5 specifies that for a non-option embedded derivative in a hybrid instrument acquired after inception, the fair value should generally be equal to zero and the initial accounting should not be affected by whether the hybrid instrument was purchased at inception or in a secondary market. In addition, we note that this guidance was required to be applied upon adoption of SFAS No. 133, and therefore would be consistent with our recommendation. Should the Board nonetheless decide to proceed with the requirement to retrospectively fair value these benefits at the time of transition, we would then recommend a practical expedient that would approximate the interest rate impact on the attributed fee ratios at the contract issue date and use current estimates for all remaining assumptions.

For all other transition provisions within the Proposed ASU, we share the concerns of the industry, as documented within the ACLI comment letter.

Question 22—Transition disclosure: Do the proposed transition disclosure requirements provide decision-useful information? If not, what would you recommend and why?

No. We share the concerns of the industry, as documented within the ACLI comment letter, relating to the level of disaggregation and disclosure requirements under ASC 250-10-50-1(b)(2) and ASC 250-10-50-3.

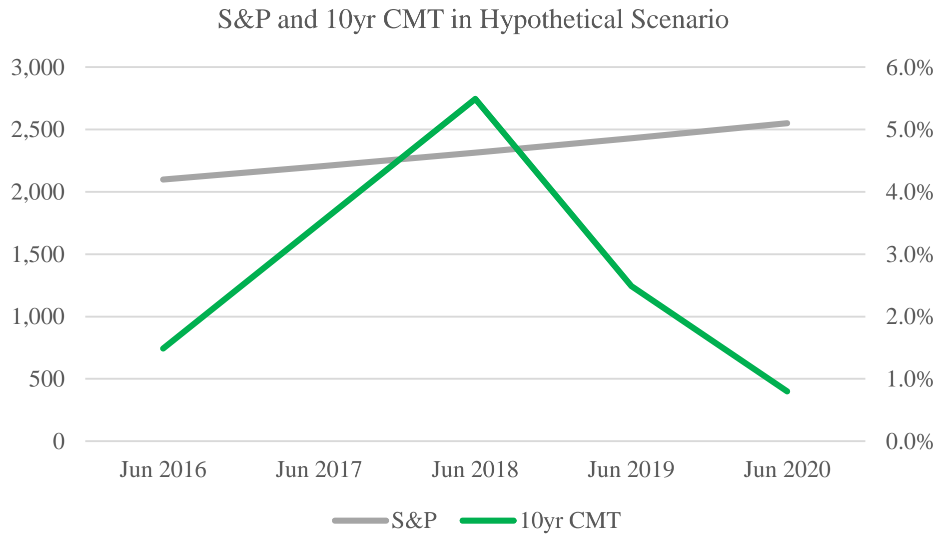
Costs and Complexities

Question 23—Costs and complexities: Describe the nature of the incremental costs of adopting the proposed amendments, distinguishing between one-time costs and ongoing costs. Explain which aspects of the proposed amendments are driving those costs and include ideas to make the proposals more cost effective.

While we agree with the Board that the benefits related to the proposed changes to the frequency of assumption updates and the amortization of deferred acquisition costs outweigh the one-time and ongoing incremental costs, we are concerned with the one-time and ongoing incremental costs related to market risk benefits, discount rate, retrospective unlocking of cash flow assumptions, changes to the accounting model for closed blocks, disclosures, and transition.

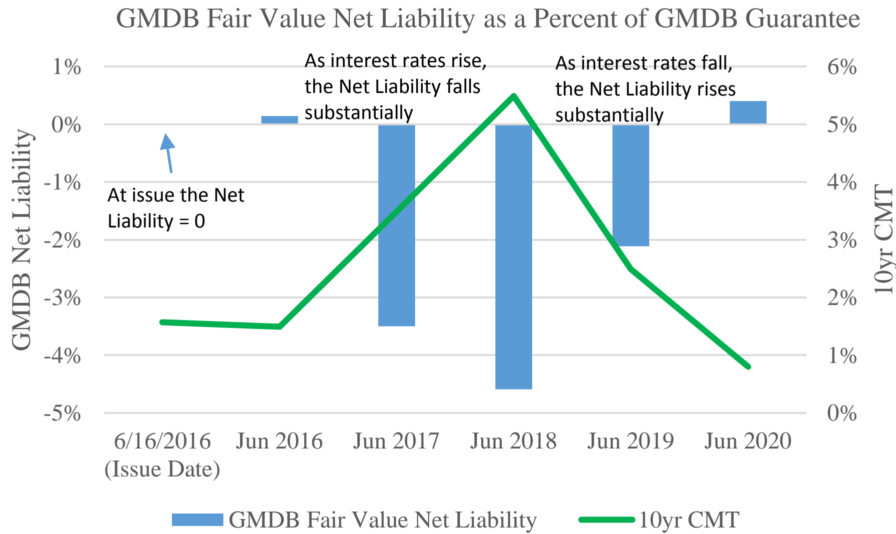
EXHIBIT 1:

In the first examples we analyze two individual policies with life-contingent benefits, one with only a GMDB and one with a GLWB, under a hypothetical scenario for several years. The hypothetical scenario reflects a gradually rising Standard & Poor's ("S&P") level with highly volatile interest rates, reflected below using the 10-Year Treasury Constant Maturity Rate ("CMT").



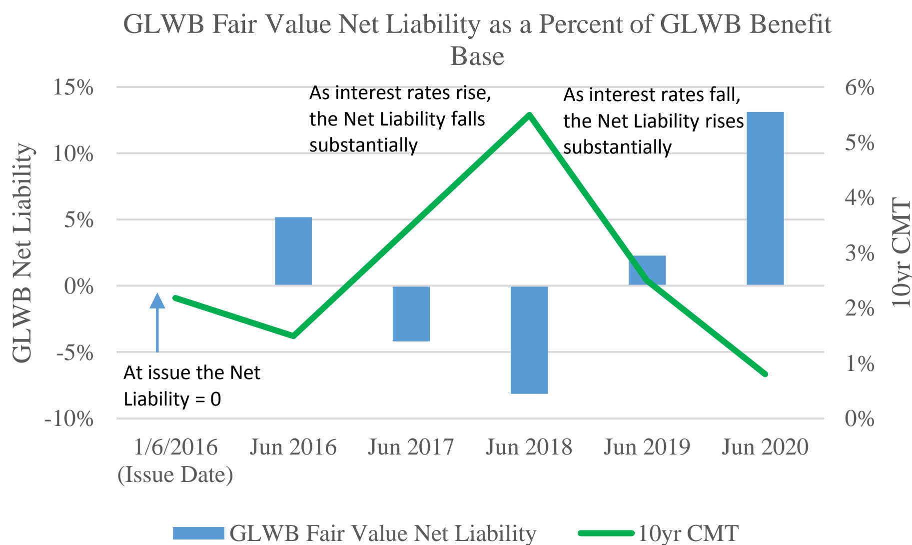
The first policy analyzed was issued on June 16, 2016 to a 77-year-old policyholder whose only guaranteed benefit is a Return of Premium GMDB. The policy's investment allocation is approximately 88% in equities. On June 30, 2016, their GMDB guarantee is $150,000 and their account value is $151,242.

Even given this policyholder's elevated age at issue, the life expectancy is over 10 years, and therefore we would not expect to pay a claim for many years into the future. However, as seen in the below chart, the volatility that materializes from the fair value model due to interest rate changes is significant despite the long duration of the expected claims.

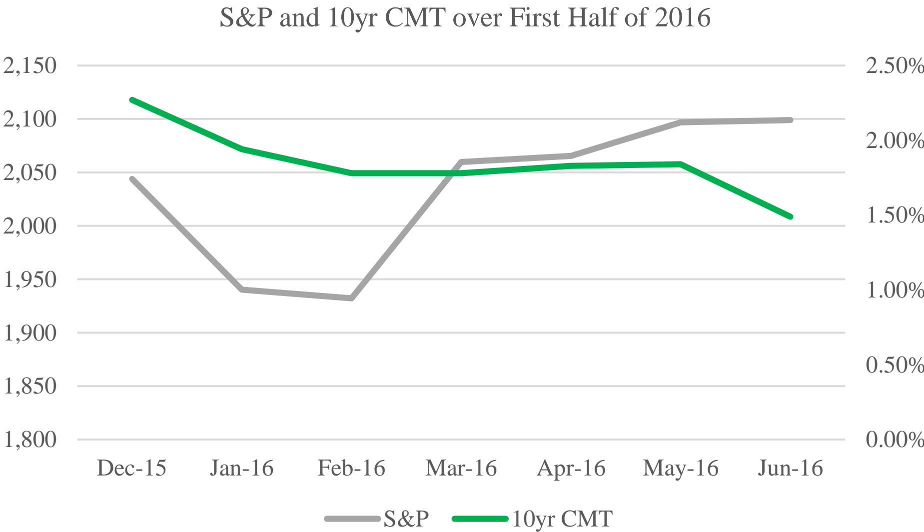


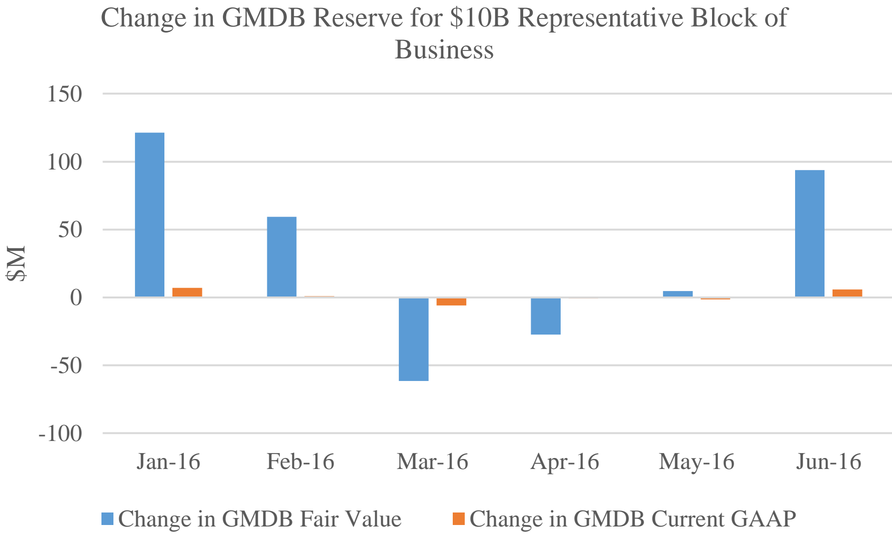
The second policy analyzed was issued on January 6, 2016 to a 68-year-old policyholder with a GLWB rider election. This policy's investment allocation is split approximately in half between equity and fixed-income investments. The GLWB benefit base is $250,000 and the account value at June 30, 2016 was $256,027.

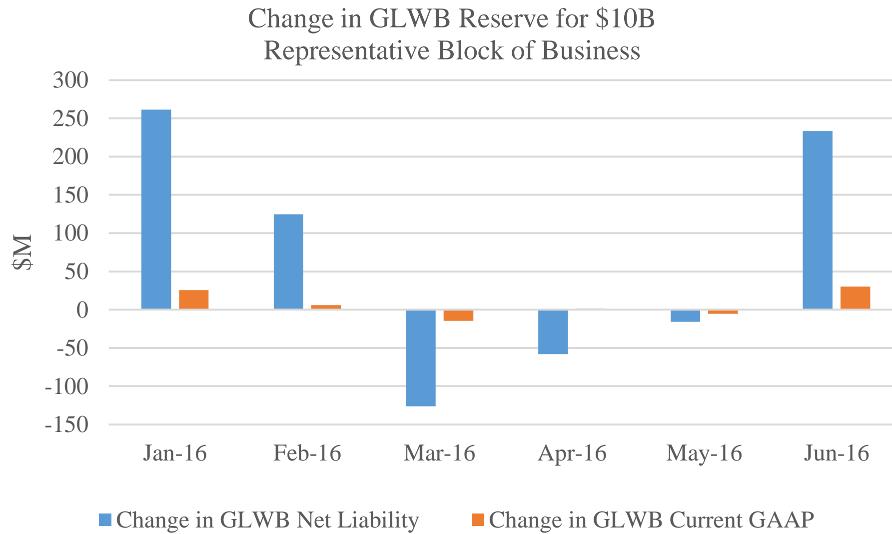
With GLWB policies, there is no claim paid to the policyholder unless their account value is depleted prior to death. Whether or not the account value is depleted is entirely dependent on the performance of the account value and the policyholder's partial withdrawal behavior. Additionally, once the account value goes to zero, the sum of the benefit payments made to the policyholder is solely determined by their mortality (i.e., payments are made from the company to the policyholder for as long as they are alive). As a result, GLWB policies are not likely to have their account value depleted until 15-30 years after issue, depending on partial withdrawal behavior and account value performance. However, as seen in the below chart, the volatility that materializes from the fair value methodology is extreme despite the fact that the benefits are not anticipated to be paid until far into the future.



The volatility seen at the individual policy level is further amplified when analyzing a large block of business. The below analysis reflects the reserve balances for representative blocks of GMDB and GLWB businesses during the first half of 2016, as measured under the fair value and existing U.S. GAAP insurance accrual methodologies. Each representative block of business totals $10 billion in account value.







As seen in the above examples, measuring these life-contingent benefits at fair value causes the liabilities to fall and rise with interest rate movements, even though interest rates have no influence on the benefit payment, other than the second-order effect of interest rate influence on the policyholder's fixed-income investments. In contrast, measuring these benefits using the current insurance accrual method results in significantly less volatility, which we believe better reflects the future cash flows that will ultimately be paid to the policyholder.