



Richard D. Levy
Executive Vice President & Controller

MAC D1053-409
301 S. College St
Charlotte, NC 28202
704 383-6557
415 975-6871 Fax
richard.d.levy@wellsfargo.com

December 15, 2016

Via electronic mail

Mr. Russell Golden, Chairman
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

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

Dear Mr. Golden:

Wells Fargo & Company is a diversified financial services company with over \$1.9 trillion in assets providing banking, insurance, trust and investments, mortgage banking, investment banking, retail banking, and consumer finance services. We appreciate the opportunity to comment on the exposure draft: Proposed Accounting Standards Update, *Financial Services—Insurance (Topic 944): Targeted Improvements to the Accounting for Long-Duration Contracts*.

Wells Fargo has reinsurance subsidiaries that offer various reinsurance solutions, with focus on two primary products – life insurance surplus relief and variable annuity (VA) full risk transfer. Our VA product has approximately \$14.7 billion of notional account value in-force. In VA contracts written in 2008 and earlier, we reinsure the base variable annuity contract as well as the associated riders. Since 2008, the industry has executed very few VA reinsurance agreements. Since 2013, we have offered a guaranteed life-time withdrawal benefit (GLWB) rider-only reinsurance solution. Our GLWB contracts are structured as life-contingent coverage where we only pay claims once the contract account value reaches zero, with payments continuing throughout the annuitant's life. Our liability ceases with the death of the annuitant or joint annuitants. When a direct insurance carrier provides a return of premium feature in their policy, we specifically carve out that cash settlement feature from our reinsurance treaties.

Guaranteed minimum benefits (GMXBs) include benefit features that are fully life-contingent, such as death benefits (GMDB) and payments based on living-only benefits (GMIB); benefit features that are fully non-life-contingent, such as withdrawal-only (GMWB) or accumulation benefits (GMAB); and benefit features with elements of both life- and non-life-contingent features, such as withdrawal-for-life benefits (GLWB). Our comments on the proposed guidance are limited to the proposed accounting for GMXB contracts.

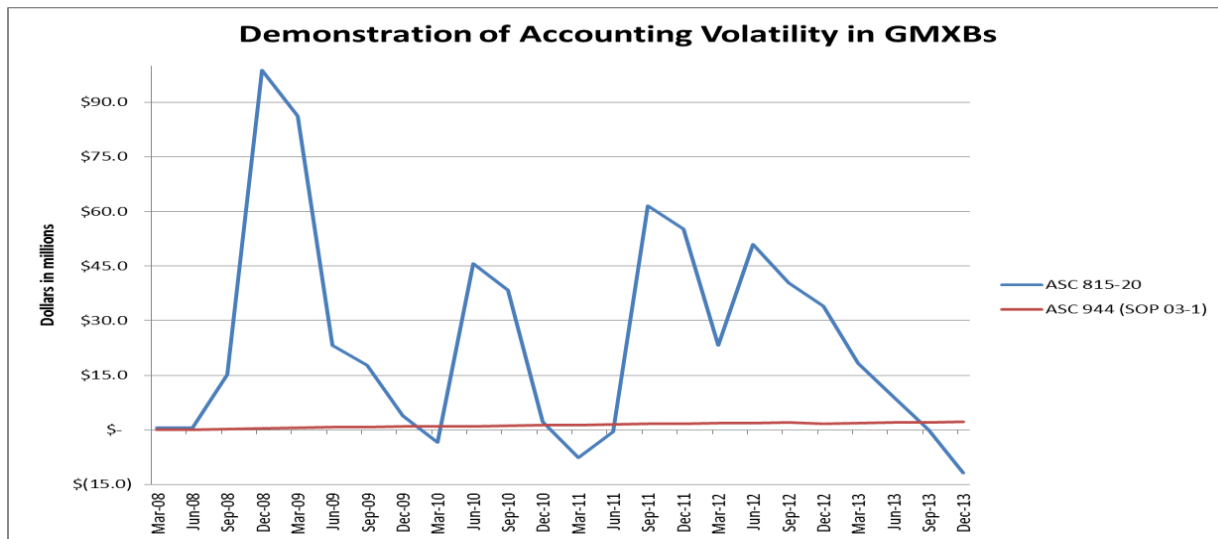
While we support targeted improvements to accounting for long-duration insurance contracts, we are concerned the proposed guidance for market risk benefits associated with GMXBs overemphasizes the utility of fair value measurement. Current accounting guidance for GMXBs appropriately distinguishes

Mr. Russell Goldman, Chairman
 December 15, 2016
 Page 2

between life-contingent and non-life-contingent benefits. We account for life-contingent benefits using the reserving method in accordance with ASC 944¹ and non-life-contingent benefits as bifurcated embedded derivatives in accordance with ASC 815.² We believe this reflects the economic substance of the benefits that we offer through our contracts.

To illustrate this point, Graph 1 below is representative of one of our actual in-force GMXB products issued in 2008. The graph demonstrates the gradual reserve build associated with the insurance liability for the life-contingent benefits versus the volatility of the fair value measurement of the non-life-contingent benefits. While the period in the graph below depicts a very volatile time in the markets, it clearly demonstrates the significant volatility that could be associated with a fair value measurement of a very long duration set of cash flows associated with a life-contingent payout. As shown in the graph, the fair value amount began at zero and grew to over \$100 million before eventually descending to a negative value (asset) by the end of 2013. Under both calculations, no actual GLWB claims have been paid. Although this graph only demonstrates one contract in our reinsurance business, our experience was consistent with the entire insurance industry over that period of time and could be experienced again in the future and exacerbated across all GMXB products if the proposed accounting changes are adopted for market risk benefits.

Graph 1



The resultant periodic volatility is uneconomic as it will never be realized. Companies will likely choose to hedge this volatility. However, such long duration hedging instruments will be limited, very costly and will likely not be very effective at offsetting the volatility. Accordingly, companies will be forced to make uneconomic decisions that carry significant costs to address the impacts of an accounting model that does not reflect the economic substance of these products. We believe the measurement of the liability under existing insurance accounting is more representative of the economics of a long-term benefit liability compared to the significant volatility that would be recognized under a fair value measurement approach.

¹ Accounting Standards Codification 944, *Financial Services - Insurance* (ASC 944) (formerly, Statement of Position 03-1 – *Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts*)

² Accounting Standards Codification 815, *Derivatives and Hedging*

Mr. Russell Goldman, Chairman
December 15, 2016
Page 3

Valuations become more difficult with longer durations and ultimately could be misleading. Given the extremely long-term nature (40+ years) of GMXB products, significant and complex judgments will be necessary in order to select relevant inputs and assumptions.³ The benefit liability will be very sensitive to small changes in market assumptions during the accumulation phase which bears little relationship to the claim payments the insurer will ultimately pay. Consequently, this volatility will produce short-term results that are not reflective of the benefits that will be provided years into the future. It is also worth noting that these contracts are not traded and the fair value measurement and the insurance accounting liability will eventually converge to the same amount upon the initial claim date when the annuitant's account value reaches zero.

While FASB's intent is to create consistent accounting for similar products, the proposed accounting for market risk benefits will result in inconsistent treatment of similar benefits on separate account and general account products. For example, some general account products provide annuity and death benefits with exposure to both interest rates and equity markets. Under current guidance, the non-life-contingent component of both separate and general account products may require fair value measurement through earnings. However, under the proposed guidance, the life-contingent benefits of the general account products will continue to be accounted for as insurance. In addition, the entire change in fair value of the general account product (non-life contingent component) will be recognized in earnings while the own-credit component of the change in fair value of the separate account product (both life and non-life components) will be recognized in other comprehensive income.

Current accounting for GMXB products produces results that reflect the economic substance of the benefits provided to our customer (i.e., direct insurer) and better reflects the long-term, non-liquid nature of the insurance liability. Accordingly, we encourage the FASB to retain existing accounting guidance whereby life-contingent benefits are accounted for as insurance and non-life-contingent benefits are measured at fair value through earnings. As an alternative for supporters of fair value measurements, disclosures of the fair values of life-contingent benefits that are not measured at fair value could be provided in the notes to the financial statements. This disclosure-only alternative would enable users of the financial statements to compare the fair value of all GMXB products across companies without introducing unnecessary volatility in the financial statements as well as incurring significant incremental costs associated with hedging the volatility.

We encourage the FASB to clarify the guidance related to reinsurance contracts. The proposed guidance only permits consideration of the underlying insurance contract and does not contemplate that a reinsurance treaty may carve out specific risks.⁴ As mentioned above, we structure our treaties to primarily reinsure the longevity risk of a GLWB rider once the account value reaches zero. We believe the proposed guidance should permit analysis on the benefit provided to the direct insurer, which may primarily represent longevity risk, rather than mirroring the accounting of the direct insurer.

If the FASB continues to move forward with the requirement to measure all market risk benefits at fair value, we foresee issues with the proposed transition guidance which requires retrospective application using actual historical information at the level of aggregation at which the reserves are calculated. If actual historical information is not available, companies will be allowed to use estimates derived from objective information from the previous periods. Due to the long duration that could exist since a contract's inception, the use of estimates under the proposed transition guidance could lead to different

³ Examples include: own credit spread, liquidity premiums, equity correlation, policyholder behavior assumptions, margins and long-dated volatility assumptions, among others.

⁴ Paragraph 944-40-25-40

Mr. Russell Goldman, Chairman
December 15, 2016
Page 4

approaches by the industry in determining the reserve valuations at implementation. Accordingly, we encourage the FASB to permit a prospective adoption for new market risk benefits. We believe that grandfathering is a reasonable transition alternative given recent precedent with accounting changes for other long-term contracts. Most recently, the FASB grandfathered accounting for leveraged leases, noting that retrospective application would have been too costly and complex, which we believe is a similar argument for market risk benefits GMXB contracts.

While we support targeted improvements to long-durations insurance contracts, we have several concerns with the proposed accounting for GMXB contracts. We believe the proposed guidance will generate financial results that do not reflect the economic characteristics provided through a reinsurance contract. Additionally, although the FASB aims for consistent measurement across all GMXBs, we are concerned that the proposed accounting will result in more diversity in practice than exists today due to the varying judgments required in measuring the fair value of these types of illiquid, long-duration contracts. We encourage the FASB to revisit the proposed guidance and incorporate our recommendations.

* * * * *

We appreciate the opportunity to comment on the issues contained in the proposed guidance. If you have any questions, please contact me at 704-383-6557 or Mario Mastrantoni at 704-383-9678.

Sincerely,

/s/ Richard D. Levy

Richard D. Levy
Executive Vice President & Controller