



Consumer Federation of America

February 27, 2019

Brent Fields, Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

**Re: File No. S7-23-18, Updated Disclosure Requirements and Summary
Prospectus for Variable Annuity and Variable Life Insurance Contracts**

Dear Secretary Fields:

We are writing on behalf of the Consumer Federation of America (CFA)¹ in response to your request for comment on a proposal to permit the sale of variable annuities and variable life insurance contracts from a summary prospectus.² CFA agrees that permitting the sale of variable annuities from a concise, user-friendly document, where the statutory prospectus is available online, has the potential to at least modestly improve investors' ability to make informed purchase decisions regarding these often complex and opaque investment products. Moreover, we agree that this is a worthy goal, given the regularity with which variable annuities feature in stories of abusive broker-dealer sales practices.³ However, improvements are needed to ensure that the proposal achieves its stated goal.

The Release does a good job of highlighting just how daunting of a task the Commission has undertaken. It notes, for example, that variable contracts "are generally more complex than other retail investment products, such as mutual funds," because they: "combine both investment and insurance features"; "frequently offer a menu of optional benefits that an investor may select to customize the contract to meet his or her individual needs"; and have complex fee structures, with fees typically charged at the contract level, on underlying investment options, and for certain transactions (such as surrender fees).⁴ What's less clear from the Release is whether, or to what extent, providing a summary disclosure document that by definition cannot fully convey these complexities will lead to informed investor decision-making. Given the well-documented low level of financial literacy among investors, it may simply not be reasonable to expect that

¹ The Consumer Federation of America is a non-profit association of nearly 300 consumer groups that was established in 1968 to advance the consumer interest through research, advocacy, and education.

² In the interests of brevity, we will abbreviate to "variable annuities" on second reference.

³ See, e.g., Bob Veres, "The Real Cost(s) of Suitability," *INSIDE INFORMATION*, Vol. 28, No. 4, April 2018, <https://bit.ly/2RM0r4Z>; also, Bob Veres, "The Awful Consequences of Non-Fiduciary Advice," *INSIDE INFORMATION*, Vol. 27, No. 9, September 2017, <http://bit.ly/2f81yXb>.

⁴ Release at 8.

even the best disclosure document will be able to clearly convey key information in a way that most investors will be able to understand.

Moreover, serious short-comings in the proposed approach undermine the summary's likely effectiveness. As a review of the Commission's illustrative mockup makes clear, the summary jumbles together information that is relevant at different stages of the investment decision: when deciding whether to purchase an annuity, when deciding which annuity to purchase, and when deciding what riders to include and what portfolio securities to select. Despite the Commission's goal of producing a plain English document, it uses language in many areas that is not likely to be easily understood by the typical investor. Even using small type in a text-dense format, the mockup ends up being 16 pages, which is longer than most investors are likely to read. In short, unless the Commission takes additional steps to improve the clarity and usability of the proposed disclosures, the benefits to investors are, in our view, likely to be minimal at best.

Usability testing would help to confirm whether the summary prospectus is likely to be well understood by investors, but the Commission has regrettably developed and released this proposal without engaging in any such testing. It should do so before finalizing a rule. If that testing shows, as we expect it would, that the summary disclosure is too dense, poorly structured, and difficult to understand, improvements to the proposed disclosure should be adopted before finalization of a rule. This could best be achieved, in our view, by working with disclosure design experts to conduct an iterative process of testing, using standard qualitative disclosure effectiveness testing techniques, and revision based on the results of that testing. The goal should be to develop a standardized summary document that is effective in conveying to investors the key information necessary to make an informed purchase decision.

Unless the document is designed to be more investor-friendly, the benefits of the proposed disclosure are likely to flow almost exclusively to industry, in the form of reduced costs associated with printing and mailing the statutory prospectus. Even if the disclosures are significantly improved, however, investors are likely to derive far greater benefit from the accompanying proposal to require annuity disclosures to be filed using Inline XBRL. We congratulate the Commission for including this critically important provision in the rule proposal. Requiring disclosures to be filed in a machine-readable format should enable third-party analysts to develop side-by-side comparisons of annuities products. This has the potential to provide more useful comparative information to both the individual investors who purchase annuities and the brokers who sell them. That, in turn, should drive greater competition among annuities based on cost and quality, as it has in other markets.

The Commission Should Rethink Its Approach to Layered Disclosure

CFA strongly supports a "layered" approach to disclosure. However, we are not convinced that the Commission has taken the most effective approach, either in this proposal to create a summary disclosure document for variable annuities or in the existing summary prospectus for mutual funds. In both cases, disclosures would be provided in two layers – a summary prospectus and the statutory prospectus (or three if you include the Statement of Additional Information). Almost by definition, the summary will not provide sufficient

information to support a fully informed investment decision, a fact the Commission acknowledges when it urges investors to read the full prospectus before making an investment. Meanwhile, the full prospectus is typically too long, dense, and full of technical jargon for the average investor to read and understand. The result is that the layered approach, as currently conceived, is unlikely to achieve its intended goal of improving investor decision-making, even for less complex investments, like mutual funds. The shortcomings are even more acute in the context of variable contracts, because of annuities' inherent complexity. If our assessment of the ineffectiveness of these disclosures is correct, then the only real benefit to this layered approach is to save industry money and, perhaps, to enable investors to make inadequately informed decisions more quickly.

We believe a different approach to layered disclosure has the potential to benefit investors and industry alike. Under our suggested approach to documents, such as this, that are designed to be relied on for an initial investment decision, layers would be based on the sequence of decisions investors make. The first layer would be designed to provide the investor with the information she needs to determine whether that particular type of investment (e.g., variable annuity, mutual fund, ETF, etc.) is a good option for her in light of her investment goals, financial situation, time horizon, risk tolerance, etc.⁵ A second layer would help the investor determine whether the particular investment being recommended, or which of several alternatives under consideration, is the best match for her. And a third layer would help the investor to make decisions at the time of purchase, such as which share class, riders, and portfolio companies to select. To the extent possible, all of these layers should be written from the investor's viewpoint to highlight information that would assist in making the specific decision she has before her at that stage of the investment process.

Applying that approach to the variable annuity summary proposal, the first layer of disclosure under our proposed approach would be designed to answer the question: how do you know if a variable annuity is right for you? It should be provided to the investor as soon as the broker decides to recommend a variable annuity. Ideally, the NAIC annuity buyer's guide for variable annuities would serve this purpose.⁶ Unfortunately, although it contains some useful information, it is not written in a way that is likely to be well understood by typical investors, it does not focus narrowly on the key information that needs to be highlighted at this specific stage of the process, and it does not present the information in a way that is intended to walk the investor through the purchase decision. As a result, it is too long, too dense, and too technical to effectively serve this purpose. In contrast, FINRA's Variable Annuities fact sheet for investors does a far better job of highlighting key information in a readable format and understandable language.⁷

The SEC's mock-up of a variable annuity summary prospectus includes information that is useful in answering this basic question, is an annuity right for me?⁸ Indeed, the SEC's mockup

⁵ With annuities, this might require two layers: one to determine whether an annuity is a good option, and one to determine which of the many types of annuity (immediate or deferred, variable or fixed index, etc.) is the best fit.

⁶ NAIC, Buyer's Guide for Deferred Annuities Variable, <https://bit.ly/2GpOETM>.

⁷ FINRA, Variable Annuities, <https://bit.ly/2Uaj934>.

⁸ Appendix A: Hypothetical Initial Summary Prospectus Prepared by SEC Staff—For Illustrative Purposes Only, at 3.

does a far better job than the NAIC variable annuity buyer's guide in this regard. We appreciate, for example, that the very first topic in the mockup – “What is this contract, and what is it designed to do?” – provides a brief summary of critical information that helps to answer the first question the investor is faced with. It states that the annuity is: “designed to provide long-term accumulation of assets”; “can supplement your retirement income by providing a stream of income payments”; and “offers death benefits to protect your designated beneficiaries.” Moreover, it takes the crucial next step of putting the information in context for the investor, stating that the annuity “may be appropriate if you have a long investment time horizon” and “is not intended for people who may need to make early or frequent withdrawals or intend to engage in frequent trading in the portfolio companies.”

This is exactly the type of information that we would include in a first layer of disclosure under our proposed approach. Unfortunately, this information comes three pages into the Commission's 16-page mockup of a summary prospectus, after the cover, table of contents, and glossary of essential terms. Moreover, because the Commission's mockup intermixes information that is general to variable annuities and specific to the annuity contract under consideration, other information that is relevant to this initial decision of whether a variable annuity is an appropriate choice comes even further down in the document. That includes information on the risks, limitations, types of fees (including surrender fees and their impact), and tax implications associated with variable annuities. Devoting a separate layer of the disclosure to this initial, more general information would allow consolidation of the information that's relevant to the first-order decision, whether a variable annuity is a good option. It would also result in a much shorter first document, ideally no more than a few pages.

One benefit of this approach is that it would make it easier for the investor to focus on one decision at a time. In addition, separating out this initial information in a separate layer of disclosure, and presenting it as early as possible in a more user-friendly format (e.g., larger type, more white space, question-and-answer, second person), could significantly increase the likelihood that investors would actually read the information. Depending on how he answers the questions posed in the initial layer of disclosure, the investor may have no need to read any further (because he needs greater liquidity than the annuity provides, for example, has a short time horizon, or is investing in an individual retirement account and won't benefit from the tax deferral). Or he may decide that a variable annuity is just what he is looking for, because he wants a tax advantaged investment that allows for both accumulation of assets and a steady stream of income later in life.

Once the investor has decided she wants to purchase a variable annuity, the next layer under our proposed approach to layered disclosure would be designed to help her choose a particular annuity. In order to ensure that it can be factored into the investor's purchase decision, that information should be provided no later than the point at which the broker recommends a particular annuity to the investor. In order to help the investor determine whether the particular variable annuity she is considering is a good option, or which of several options under consideration is the best match for her, this document would focus on the particular features of the annuity being recommended. This would include, for example, information on: the specific fees and costs associated with the annuity; the terms and conditions of the surrender period, if any; the insurance company's solvency rating; standard and optional death benefits, optional

living benefits, other available riders and their costs; and the portfolio companies available under the contract.

The information provided at this stage should be presented in a manner that helps the investor answer two questions: Does this annuity have the features I am looking for? How does it compare to other available options? Ideally it would be provided in a form that would allow for side-by-side comparisons of different products. Here again, by consolidating the information and presenting it at the time when that investment decision is being made, this approach has the potential to better assist the investor in making an informed choice than a document in which general and specific information is jumbled together and that arrives only after the purchase decision has been made.

Once the investor chooses an annuity to purchase, a third layer of disclosure would be designed to help the investor make decisions necessary to the purchase decision. These include such questions as: Which share class is right for me? Which, if any, riders do I want to purchase? How would that affect my costs? Which portfolio companies should I choose to invest in? This disclosure should be provided no later than the point of sale, and earlier if possible, to ensure the investor has an opportunity to consider these questions before making a final decision. Also included either in this third layer of disclosure, or perhaps in a separate variable annuity owner's guide, would be the information from the proposed summary that has less to do with supporting an informed investment decision, and instead is designed to guide the investor through actions he might take when he owns a variable annuity. This could include, for example, information like that provided in the section on "Surrendering Your Contract or Making Withdrawals."

Although it works in a paper-based disclosure system, as we have described above, this approach to layered disclosure would have even greater potential when delivered electronically. Presenting the information in web form would allow for links to be embedded to provide more detail on certain topics (e.g, the accumulation versus payout phases, the different types of death benefits, the tax implications, cash withdrawals and surrender fees, etc.) without cluttering up the central disclosure document. Definitions of key terms could be available either through hyperlinks in text, or by providing definitions in pop-out windows when the cursor is placed over the word, with the result that a glossary of intimidating terms wouldn't stand between the reader and the key content essential to the investment decision. And there would be more leeway to present the key information in user-friendly ways – with more white space, for example, with separate tabs for different topics within the "document," or with more use of graphics or videos to illustrate the text. Given the inevitable transition underway toward an Internet-based system of disclosure, it is disappointing that the Commission continues to approach the idea of layered disclosure with a mentality shaped by the tradition of paper documents.⁹

We do not claim to have worked out all the details of such an approach. How best to divide up the information and how to present it are topics that deserve greater consideration than we've given them in this abbreviated discussion. Moreover, the Commission would need to test

⁹ CFA strongly believes that investors should continue to have the choice of how they prefer to receive disclosures – whether in paper or electronically. But we also firmly believe that the transition to a largely Internet-based system is inevitable in the not too distant future. That reality, and the possibilities that arise in a web-based disclosure system, should shape how the Commission approaches new disclosure initiatives, such as this.

our proposed approach to layered disclosure, as well as its own proposed approach, to reliably determine which actually works best to support informed investment decision-making. It would appear that the Commission has designed this proposal based on the assumption that the mutual fund summary prospectus represents a successful approach to layered disclosure. However, the Commission has not, to our knowledge, ever tested the actual effectiveness of that approach in promoting informed investment decision-making. Nor does the Commission appear to have adequately considered other possible approaches, such as the one we have outlined here, in developing this proposal. Our own view is that evidence strongly suggests that a more radical rethinking of the Commission's approach to disclosure is needed if the goal truly is to support informed investment decision-making and not just reduced industry costs.

The Proposed Summary is Consistent with Some, But Not All, of Our Principles for Effective Disclosure

In a previous letter to the Commission, we outlined basic principles for effective disclosure.¹⁰ This portion of the letter assesses the current rule proposal against those principles (which are shown in bullet-point throughout this section). As discussed below, the proposal is consistent with those principles in some important areas, but fails to measure up in others.

- For investors to make good use of disclosures, they need to know the information is available to them. Delivery methods, such as “access equals delivery,” that require investors to seek out the information all but guarantee that only the most financially sophisticated and technologically adept individuals will receive information that the Commission deems to be essential to an informed investment decision. If that occurs, everything else the Commission does to improve disclosure quality would be rendered meaningless.

We appreciate that the proposal would require that the summary prospectus be either sent or given to the investor. In discussing electronic delivery, however, the Release notes simply that, “Investors that have elected electronic delivery of materials associated with their variable contract typically receive an email that contains a link to the website where the materials are available.”¹¹ We would urge the Commission to make clear that delivery of an email that fails to include specific information on where to find the information on the website, i.e., either a direct link or an exact url, would *not* satisfy the delivery requirement.¹² Instead, electronic delivery in this context must require that the investor receive an email including either an attachment containing the summary itself, a direct link to the document, or the exact url where the materials can be found.

Moreover, where the investor receives an email containing notice of the summary's availability that includes a direct link or url, rather than an attachment containing the summary

¹⁰ Letter from CFA Director of Investor Protection Barbara Roper to SEC Secretary Brent Fields regarding File No. S7-12-1, “Request for Comment on Fund Retail Investor Experience and Disclosure,” Oct. 31, 2018, <https://bit.ly/2FVrS5H>.

¹¹ Release at 18.

¹² We note this because the Commission has previously taken the position in its crowdfunding rules that such a vague and imprecise notice would satisfy the electronic delivery requirement in that context.

itself, that notice should be designed to maximize the likelihood that investors will actually read the disclosure. The Release does not give adequate consideration to how this would be achieved. We have seen examples over the years of well-designed notice documents for mutual fund disclosures that fully meet that standard, but we cannot safely assume that all companies will approach this equally well, particularly in a corner of the market that has thrived on opacity. As the Commission mentions more than once in the Release, variable contracts are particularly complex investment products. We need to make it as easy as possible for investors to get and read the key information relevant to their investment decision.

It is extremely disappointing, in this regard, that the Commission's proposal would actually make it less likely that investors would receive information necessary to make an informed decision about which of the underlying portfolio companies to invest in. Where companies rely on the summary prospectus to fulfill their annuity disclosure obligations, the proposed rule would eliminate the requirement that they also send summary prospectuses for underlying portfolio securities. In short, having previously determined that the mutual fund summary prospectus represents a bare minimum of key information investors should consider when selecting a fund, the Commission now proposes an approach that increases the likelihood that variable annuity investors will base their choice of portfolio companies on even less information, consisting of fund type, expense ratio, and performance history.

The Release justifies this approach based on: 1) the fact that some information about underlying portfolio companies will be provided in the summary; and 2) a concern that investors may be overwhelmed by the volume of material they receive if summaries for underlying portfolio companies are required to be delivered. But it fails to consider the impact on investor decision-making. Does the Commission really believe that this is adequate information on which to base an investment decision? Or does the Commission believe that investors will take the initiative to track down information on underlying portfolio companies despite this new hurdle? Information reported elsewhere in the Release suggests that a majority of investors will not seek out the information online. The Release reports, for example, that only a small percentage of variable annuity investors have chosen to receive disclosures electronically.¹³ Investors who choose to receive their disclosures in paper are highly unlikely, in our view, to seek out these summaries online.

At an absolute minimum, electronic versions of the summary should be required to include direct links to the portfolio company summaries in the appendix listing those portfolio companies. Investors who choose to receive their disclosures in paper form should be given the choice, at the outset, regarding whether they prefer to receive summaries for underlying portfolio companies in paper or online. Where investors meet in person with the seller when purchasing an annuity, the seller should be required to present them with the relevant summaries either prior to that meeting or as they walk them through the process of deciding how their money will be allocated among the available portfolio companies. Assuming the Commission doesn't abandon this aspect of the proposed rule entirely, as we recommend, the Commission should at least monitor whether and to what extent its proposal reduces the information investors rely on in making those important investment decisions.

¹³ Release at 303.

- For investors to make good use of disclosures, they need to receive the information early enough (e.g., point of recommendation) to incorporate it in their decision-making process. Disclosure that arrives after a decision has already been made (e.g., point of sale) or worse, after a purchase has already been made, defeat the purpose of disclosure as a decision-making tool.

One potential benefits of a layered approach to disclosure is that, by reducing printing and mailing costs, it makes it more affordable to provide disclosure earlier in the process. Providing disclosures as early as possible is essential to increase the likelihood that the information will be incorporated into the investor’s purchase decision. Unfortunately, the Commission appears to have given little if any consideration to changing the timing of the disclosure even as it proposes to change the format of that disclosure. By leaving in place the existing requirements with regard to disclosure timing, the Commission all but guarantees that most investors will not benefit from the proposal by making more informed investment decisions.

Some might argue that the availability of a free-look period for annuities reduces the need to provide timely, pre-sale disclosure, since investors have an opportunity to change their mind and rescind the sale.¹⁴ This ignores basic human psychology. At the very least, a combination of inertia and reluctance to rethink a decision once made all but ensures that investors will only rarely avail themselves of this opportunity. Behavioral finance suggests the effect may be even stronger. According to research in this area, choice-supportive bias is likely to cause consumers to ascribe benefits to their purchases in order to confirm that they made the right decision, and this tendency increases with age.¹⁵

Similarly, the availability of other information – including marketing brochures and state-mandated buyer’s guides – does not obviate the need for timely delivery of mandated disclosures. Marketing materials are, by definition, designed to promote a sale, not provide the unbiased information needed for a carefully considered purchase decision. And the NAIC buyer’s guides, as currently drafted, are not at all consumer-friendly in their content, language, or presentation. The failure to provide timely disclosure also makes the investor more reliant on the seller for recommendations, which, in the absence of a strong best interest standard, increases the likelihood that they will be steered into higher-cost products loaded up with features they do not need. This is a problem that runs rampant in the annuities market, as we have discussed at length in earlier letters to the Commission.¹⁶ In short, the Commission’s failure to address the disclosure timing issue in this proposal is a huge missed opportunity – one more reason the proposed rule does more to benefit annuity sellers than investors.

- For disclosures to be effective, investors need to review them. Disclosures that are long and densely packed with technical jargon are unlikely to be read, no matter when or how

¹⁴ Release at 30, fn 65.

¹⁵ See, e.g., Mara Mather and Marcia K. Johnson, *Choice-Supportive Source Monitoring: Do Our Decisions Seem Better to Us as We Age?*, *Psychology and Aging*, Vol. 15, No 4, 596-606, 2000.

¹⁶ See, e.g., Letter from Barbara Roper and Micah Hauptman, Consumer Federation of America, to the Honorable Jay Clayton, Chairman, Securities and Exchange Commission, regarding Standard of Conduct for Broker-Dealers and Investment Advisers, Sept. 14, 2017, <https://bit.ly/2LSFkLg>, at 29-32.

they are delivered. The Commission’s staff of subject matter experts – with their extensive knowledge of the securities markets and securities law – are well positioned to identify the information investors should know to make an informed investment decision. But they are not necessarily the best situated to understand how to convey that information to a non-expert investor, either in terms of language or design.

The proposal obviously represents a good-faith effort on the part of the Commission to adopt a streamlined, plain English summary of key information investors should know when investing in a variable annuity. And it clearly represents an improvement over the statutory prospectus in this regard, but that is an exceedingly low bar against which to measure its success. We are concerned that the proposal as currently conceived fails to fully achieve its goal of improving the clarity and readability of variable annuity disclosures. As is illustrated by the Commission’s mockup, summary prospectuses adopted in reliance on this rule are likely to be too long, too dense, and too laden with technical jargon to be widely read or easily understood by typical annuities investors.

We readily acknowledge that these are not easy problems to solve. The 16-page length necessary to fit all the information the Commission requires is likely to dissuade many investors from reading the document. And the small type and text-dense design exacerbate that problem by making the Commission’s illustrative mockup visually unappealing. But increasing the type size and adding white space and other design elements to make the document more visually appealing would make it longer still. We’ve sought to address that challenge in our alternative approach to layering, discussed above, by dividing the summary into several documents that would be provided to the investor sequentially over the course of the investment decision. The goal of our approach is similar to the goal behind this proposal: to provide investors with the information they need in more consumable amounts. But in reviewing the Commission’s proposal, we concluded that two layers is not sufficient to achieve that goal, particularly when the summary jumbles together information that is needed at different stages of the investment decision.

Similarly, despite the Commission’s effort to come up with plain English descriptions of key features, the document is written at a level that is likely to be far above the average annuities investors’ comprehension. This problem, which is not unique to this document, reflects a basic failing in the way the SEC and other financial regulators typically approach the development of disclosures for the retail market. As a group of consumer representatives wrote in an earlier letter to the National Association of Insurance Commissioners (NAIC): “Disclosures tend to be written, reviewed and approved by insurance subject matter experts – typically regulator or industry lawyers, actuaries and market regulation staff. Few of these people have subject matter expertise in consumer readability, cognition, information biases or learning. Few have expertise in testing of consumer information and disclosures or training in these fields. The results have often been a disclosure that is unhelpful to a consumer, but provides a liability shield for insurers.”¹⁷ Substitute securities for insurance in the above quote, and the same could be said for securities disclosures, such as the current proposal, that are designed for the retail market.

¹⁷ Letter from NAIC Consumer Representatives Brenda Cude, Birny Birnbaum, and Silvia Ye to members of the NAIC Executive Committee Task Force on Consumer Information, Education and Disclosure, Nov. 7, 2018.

In order to overcome that basic shortcoming, the Commission should work with outside experts to review and revise the proposed variable annuity summary to come up with an approach that is both visually appealing and comprehensible for typical annuity investors. Ideally, it would have undertaken that review before issuing the current proposal. Having missed that opportunity, however, it should certainly undertake that effort to improve the design and language of the summary prospectus before finalizing this rule proposal. If the Commission fails to accept our recommendation on this point, it should at an absolute bare minimum, make clear that it plans to conduct such a review of summaries developed in reliance on the rule and use that review to develop improvements to the design and language of the summary before finalizing a rule to mandate its adoption.

- While getting investors to review disclosures is important, the real test of disclosure effectiveness is whether investors are able to use the disclosures to make an informed decision. An attractively designed, hyperlinked summary document that investors are willing to read is a step forward, but it only gets you halfway there. If investors do not glean sufficient understanding of the information provided to make an informed investment decision, the disclosure cannot be deemed to be a success.

The primary purpose of this rule proposal, according to the Release, is “to help investors make informed investment decisions regarding variable annuity and variable life insurance contracts.”¹⁸ We are frankly skeptical that it will achieve its goal. Even if the summary prospectus ends up being widely read by investors before they make a purchase decision, we are concerned that it may not be widely understood by typical retail investors. Take, as one example, the discussion under key features of contract classes in the Commission’s hypothetical summary prospectus:

You can purchase one of several contract classes that have different ongoing fees and surrender charges. For example, this contract offers Class B with an 8-year surrender charge period or Class X with a 9-year surrender charge period and higher ongoing fees. If you purchase a Class X contract, XYZ will add an additional lump sum amount to your premiums.¹⁹

The investor who reads this section would have to: 1) look back to the glossary for a definition of a surrender charge if they aren’t familiar with that term; 2) scroll down to the key information table for an illustration of what a surrender charge might amount to for one type of contract class; 3) scroll down further still, to the section providing additional information on fees, to get a side-by-side comparison of the surrender charge percentages for the different contract classes offered. We doubt that most investors would be able to pull together the information provided in these different locations to make an informed choice regarding which option is best for them.

Information on other features and fees is similarly scattered throughout the document. For example, information on the riders that are available with one contract class but not the other are found in an entirely separate section of the document. And the example that is designed to help the investor compare costs across different contract classes and different products is buried 12 pages into the 16-page document. The investor would have to look back to the earlier

¹⁸ Release at 1.

¹⁹ Appendix A at 3.

discussion of contract classes to understand what the differences between the two different contract classes consist of to figure out whether the cost difference is justified by the added benefits. Furthermore, the table itself provides limited information. We certainly appreciate that the illustration is based on a representative purchase amount (\$100,000) and the most expensive combination of portfolio company operating expenses and optional benefits available for an additional charge, so that it doesn't understate potential costs. However, adopting this approach also fails to provide the investor with useful information on the range of total costs they might face, nor does it clearly illuminate the component costs that add up to that total. Nowhere does the summary prospectus provide a coherent narrative that would help the investor to determine which of the two contract classes, and which of the available features, are best suited to their needs.

These are just a couple of the most serious shortcomings in the proposed summary. In section after section, the document assumes knowledge that many if not most investors likely lack and uses terminology only relatively sophisticated investors are likely to understand. For example, the table showing minimum and maximum portfolio company operating expenses provides that information before and after any waivers or expense reimbursements, without explaining what that means. We suspect many investors would be confused by that. The section on the contract assumes investors will understand the difference between qualified and unqualified accounts. Also, expense information throughout is generally provided as a percentage, and dollar amount illustrations are provided in only a few cases. But research has shown that investors struggle to understand costs when they are presented as a percentage and tend to under-estimate those costs.

In short, we believe the proposed summary prospectus would need to be extensively rewritten, reorganized, and redesigned to achieve the stated goal of supporting informed investor decision-making. At the very least, the Commission should undertake rigorous qualitative disclosure effectiveness testing before finalizing this rule to determine whether the proposed disclosure effectively conveys key information to investors. If, as we expect, that testing shows that extensive revisions are needed, the Commission should work with disclosure design experts to revise the proposal based on an iterative process of testing and revision in order to develop an approach that does promote investors' ability to determine whether an annuity is the best option for them, whether the particular annuity under consideration is the best choice, and what contract class, riders, and portfolio investments to select when making that purchase.

- Even with the best disclosures, the investment decision-making process is likely to be overwhelming for many, if not most, investors. As the Commission looks at ways to modernize its disclosures, it should seek to develop a system that makes it as easy as possible for third parties to develop simple tools investors can use to narrow down their selections based on specific criteria.

CFA strongly supports the proposal to require variable contract registrants to submit certain information in the Inline XBRL format. This requirement has the potential to greatly benefit investors by allowing them, either directly or through their investment professionals, "to efficiently analyze and compare the available information about variable contracts" based on the factors that are of greatest interest to them. Similar benefits could flow from providing that

ability to data aggregators, financial analysts, Commission staff, and other data users. It is our hope that third-party data aggregators would develop online tools based on this data that enable investors to identify a small selection of annuities with the characteristics they are looking for and make side-by-side comparisons of those annuities to determine which offers the best mix of features and costs. Or tools could be developed that would help the investor determine which contract class of a particular annuity and which combination of riders would best meet their needs, along with a dollar amount estimate of their expected costs.

In short, this one step of requiring disclosures to be made in Inline XBRL has the potential to do more than the most innovative disclosure design changes to assist the many investors who lack the time and expertise to pore through disclosure documents to select the variable annuity and contract features that best meet their needs. If those tools develop and are widely embraced by investors, this step also has the potential to encourage competition in the variable annuity market based on quality and cost of the investment product rather than compensation to the seller. As such, this requirement has the potential to harness market forces to benefit, rather than harm, investors.

Even if this data-driven market competition develops as we hope, the full benefits are unlikely to reach all, or even most, annuities investors. We've seen, for example, how investors who purchase their mutual funds through brokers don't receive the same benefits from cost competition that direct purchasers receive, even after accounting for the cost of compensating the broker. This is even more likely to be the case for a product that is many times more complex than the typical mutual fund. The many investors who continue to rely heavily on recommendations from an annuity seller in making their purchase *could* benefit indirectly from the increased transparency and improved ability to compare products *if* the Commission adopts a tough best interest standard governing those recommendations.

Unfortunately, as we have discussed at length elsewhere, Regulation Best Interest as currently proposed doesn't do enough to hold brokers to a rigorous best interest standard or to rein in the incentives that encourage and reward harmful advice. If the Commission were to strengthen the standard in these key areas, requiring disclosures in Inline XBRL could play a central role in supporting compliance with the standard. Firms that are required to review their product menus to support compliance with a best interest standard could, for example, use Inline XBRL data in assessing their product line-ups. And registered reps who are required to recommend the best of the reasonably available investment options, and who aren't incentivized to recommend the annuities that are financially best for the firm, could use the Inline XBRL data to conduct the rigorous analysis required to determine which option is best for the customer and to document the basis for their recommendation.

Conclusion

The Commission has undertaken what appears to be a well-intended effort to improve variable annuity disclosures. For a variety of reasons, we believe the proposal is unlikely to achieve its intended goal. The summary is likely to be delivered too late to be incorporated in the investor's purchase decision. The document itself is too long, too dense, and too reliant on technical jargon to be widely read or easily understood by investors. It does not present a

coherent narrative that investors could use as they work their way through a series of decisions, including whether to invest in a variable annuity, which variable annuity to invest in, and which features of that annuity to select. We believe significant improvements are possible, and we strongly urge the Commission to work with disclosure design and testing experts to develop a document that better communicates key information to investors before finalizing this rule. Ultimately, however, we believe the most beneficial aspect of this proposal for investors is the requirement to disclose certain information using Inline XBRL, which should allow for better side-by-side product comparisons. Indeed, even as we urge the Commission to rethink its overall approach to the summary prospectus, we urge the Commission to move forward expeditiously with the Inline XBRL requirement. There is no reason why that aspect of the proposal need be delayed while the Commission conducts the extensive redesign and rigorous testing necessary to ensure that the summary itself actually supports informed investment decision-making.

Respectfully submitted,



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