

LIFE INSURANCE (A) COMMITTEE

Reference:

1992 Proc. II p. 663
1992 Proc. I p. 859

Mike Weaver, Chair—Ala.
David J. Lyons, Vice Chair—Iowa

CONTENTS

December 8, 1992 Minutes	779
Insurable Interest Working Group December 7, 1992 Minutes	
(Attachment One)	782
Final Guidelines on Corporate Owned Life Insurance (Attachment One-A)	783
Revised Discussion Draft of Living Benefits Model Act	
(Attachment One-B)	784
Statement of William J. Freeman, Executive Director, National Association	
of People with AIDS (Attachment One-C)	786
Life Disclosure Working Group December 6, 1992 Minutes (Attachment Two)	788
Discussion Draft of Proposed California Ledger Illustration Law	
(Attachment Two-A)	789
Preliminary Report of the American Academy of Actuaries Task Force	
on Life Illustrations (Attachment Two-B)	792
Life Disclosure Working Group November 8, 1992 Minutes	
(Attachment Two-C)	794
November 24, 1992 Conference Call Minutes (Attachment Three)	795
Guide to Buying Life Insurance After Age 60 (Attachment Three-A)	796
Life Insurance Disclosure Model Regulation Amendment	
(Attachment Three-B)	800
September 21, 1992 Minutes (Attachment Four)	800
Consumers' Letter Regarding Limited Benefit Life Insurance	
Policies (Attachment Four-A)	802
Buyer's Guide to Life Insurance for Seniors Drafting Group	
September 20, 1992 Minutes (Attachment Four-B)	803
Insurable Interest Working Group September 20, 1992 Minutes	
(Attachment Four-C)	804
Final Guidelines on Gifts of Life Insurance To Charitable	
Institutions (Attachment Four-C1)	805
Discussion Draft of Living Benefits Model Act (Attachment Four-C2)	807
Insurable Interest Working Group July 7, 1992 Conference Call	
Minutes (Attachment Four-C3)	809
Letter From U.S. Senator Howard Metzenbaum Regarding	
Consumer Disclosure (Attachment Four-D)	810
Memo from Carole Gates Regarding Proposed Amendments to Long-Term	
Care Model Regulation (Attachment Four-E)	811

AGENDA

1. Report of Insurable Interest Working Group
2. Report of Life Disclosure Working Group
3. Report of Life and Health Actuarial (Technical) Task Force
4. Any Other Matters Brought Before the Committee

MINUTES

The Life Insurance (A) Committee met in Salon III of the Marriott Marquis in Atlanta, Ga., at 1 p.m. on Dec. 8, 1992. A quorum was present and Mike Weaver (Ala.) chaired the meeting. The following committee members or their representatives were present: David J. Lyons, Vice Chair (Iowa); John Garamendi (Calif.); Robert M. Willis (D.C.); James H. Brown (La.); Harold T. Duryee (Ohio); Georgia D. Flint (Texas); Harold C. Yancey (Utah); and Steven T. Foster (Va.).

1. Report of Insurable Interest Working Group

Commissioner Mike Weaver (Ala.) called on Commissioner Harold Yancey (Utah) to give the report of the Insurable Interest Working Group. Commissioner Yancey noted that there were two items addressed by the committee. The first was the adoption of a Guideline on Corporate Owned Life Insurance. Commissioner Yancey noted that with one minor modification, the June 4, 1992, draft, as modified by the advisory committee, was adopted.

Commissioner Yancey explained that the second item was the receipt of comments on viatical settlements. He noted that it was always the intent of the working group to hear from all interested parties and that this was the first time the group had the opportunity to hear from representatives of the viatical settlement industry and from representatives of people with AIDS and other terminal illnesses. He noted that the input from these representatives was and will be helpful as this issue is further evaluated.

Commissioner Yancey recommended that a new working group and advisory committee comprised of a broad group of interested parties be established next year to continue evaluating the appropriate regulatory response to this emerging industry.

Upon motion duly made, seconded and unanimously adopted, the minutes of the Insurable Interest Working Group were adopted (Attachment One).

2. Report of Life and Health Actuarial (Technical) Task Force

John Montgomery (Calif.) presented the following recommendations from the Life and Health Actuarial (Technical) Task Force for approval.

Recommendations:

1. Recommend deletion of Project 2p "Reserves for Companies in Rehabilitation" in December 1992 because work on that project was completed.
2. Recommend addition of Project 2r "Cost of Collection in Excess of Loading" to the agenda of the Life and Health Actuarial (Technical) Task Force as a Number Two Priority project in December 1992. If this addition to its agenda is adopted, the actuarial task force also recommends that the proposed actuarial guideline entitled "Guideline Concerning the Liability for the 'Cost of Collection' on Premiums and Annuity Considerations" be exposed for comments in December 1992. (See Attachment One-E to Life and Health Actuarial Task Force report in this volume of the *NAIC Proceedings*.)
3. Recommend addition of Project 2s "Immediate Payment of Claims" to the actuarial task force's agenda as a Number Two Priority project in December 1992. If this addition to its agenda is adopted, the actuarial task force also recommends that proposed Actuarial Guideline HHH entitled "Reserve for Immediate Payment of Claims" be exposed for comments in December 1992. (See Attachment One-G to Life and Health Actuarial Task Force report in this volume of the *NAIC Proceedings*.)
4. Recommend the Nov. 25, 1992, draft report of the Advisory Committee on Revision of Annuity Nonforfeiture Law for exposure for comments in December 1992. (See Attachment One-H and Project 3h "Revision of Annuity Nonforfeiture Law," under "Synopsis of Projects," elsewhere in this report.)
5. Recommend that Project 4l "Whole Life Policies Without Cash Values or Paid Up Benefits" be placed "on hold" in December 1992.
6. Recommend deletion of Project 4r "Joint Life Last Survivor Policies - Nonforfeiture and Valuation" in December 1992, because of apparent absence of current importance for that project.
7. Recommend deletion of Project 4u "Update of Actuarial Guideline XVII" in December 1992, because of apparent absence of current importance for that project.
8. Recommend deletion of Project 4v "Plan Type Designation under Guaranteed Interest Contracts" in December 1992, because of completion of work on that project.

9. Recommend that a proposed change in Schedule S – Part 4 of the life annual statement blank be exposed for comments in December 1992. (Please see Attachment One–J to Life and Health Actuarial Task Force report in this volume of the *NAIC Proceedings* and Project 5 “Reinsurance,” under “Synopsis of Projects,” elsewhere in this report.)

10. Recommend deletion of Project 15 “Valuation vs. Policy Form Approval” in December 1992, because of completion of work on that project.

11. Recommend addition of a new Project 16 “Interpretations” on December 1992 as a Number Two Priority project. If this new project is authorized, the actuarial task force also recommends that Actuarial Guideline No. XII be withdrawn in December 1992. If the new project is added and Actuarial Guideline No. XII is withdrawn, the actuarial task force recommends deletion of this new project in December 1992 on account of completion of work on that project.

Mr. Montgomery also presented the following recommendations of the Life and Health Actuarial (Technical) Task Force’s Joint Meeting of Life and Accident and Health Matters.

1. Recommend addition of Project 1a “Use of Nonadmitted Assets for Asset Adequacy Analysis” as a Number One Priority project in December 1992, to the agenda of the Life and Health Actuarial (Technical) Task Force for both the Life Insurance (A) Committee and the Accident and Health (B) Committee. If this project is duly authorized, the Actuarial Task Force also recommends that proposed Actuarial Guideline FFF, entitled “Use of Nonadmitted Assets for Asset Adequacy Analysis,” be exposed for comments in December 1992 (See Attachment Three–A to Life and Health Actuarial Task Force report in this volume of the *NAIC Proceedings*).

2. Recommend addition of Project 1b “Guidelines for Regulatory Review of Cash Flow Analyses” as a Number One Priority project in December 1992 to the agenda of the actuarial task force for both the Life Insurance (A) Committee and the Accident and Health (B) Committee.

Upon motion duly made and seconded, the preceding recommendations of the Life and Health Actuarial (Technical) Task Force were adopted.

3. Report of the Life Disclosure Working Group

Commissioner Weaver first provided a brief history of the formation and activities to date of the working group. He stated that at this meeting the working group had received commentary from a number of individuals representing various organizations which also are evaluating policy illustrations and other related disclosure issues. He stated that it was the consensus of the working group that the Executive (EX) Committee should be given a recommendation to continue the work of this working group as part of the 1993 A Committee charges and a motion to that effect was unanimously adopted. Upon motion duly made, seconded and unanimously adopted, the minutes of the Life Disclosure Working Group were adopted (Attachment Two).

Having no further business, the Life Insurance (A) Committee adjourned at 1:40 p.m.

[Editor’s Note: The minutes of the Life Insurance Committee’s Nov. 24, 1992, conference call and its Sept. 21, 1992, meeting are published here as Attachments Three and Four, respectively.]

Mike Weaver, Chair, Ala.; David J. Lyons, Vice Chair, Iowa; John Garamendi, Calif.; Robert M. Willis, D.C.; James H. Brown, La.; Harold T. Duryee, Ohio; Georgia D. Flint, Texas; Harold C. Yancey, Utah; Steven T. Foster, Va.;

ATTACHMENT ONE

Insurable Interest Working Group
of the Life Insurance (A) Committee
Atlanta, Georgia
December 7, 1992

The Insurable Interest Working Group of the Life Insurance (A) Committee met in the London/Zurich Room of the Marriott Marquis in Atlanta, Ga., at 11 a.m. on Dec. 7, 1992. A quorum was present and Harold C. Yancey (Utah) chaired the meeting. The following working group members were present: Mike Weaver (Ala.); John Garamendi (Calif.); and Steven T. Foster (Va.).

Commissioner Harold Yancey (Utah) noted that the first item on the agenda was consideration of adoption of a guideline on Corporate Owned Life Insurance. George Coleman (Prudential) asked for clarification as to which version of the guideline was under consideration. Commissioner Yancey clarified by stating that the version under consideration was the NAIC draft dated June 4, 1992, as modified by the advisory committee.

Robert Corn (NAIC/SSO) commented that the draft as modified indicated that citations to state statutes relating to insurable interests of employers in their employees are attached to the guideline. He noted that originally the guideline indicated that citations could be obtained by contacting the legal department of the NAIC. Mr. Corn recommended changing back to the original language since the information compiled by the NAIC changes over time as additional states adopt statutes. The advisory committee and working group concurred with this suggestion and upon motion duly made, seconded and unanimously approved, the NAIC draft dated June 4, 1992, as modified by the advisory committee with the one exception noted above, was adopted (Attachment One-A).

Commissioner Yancey stated that the next agenda item was to receive comments on viatical settlements. Commissioner Yancey first provided a brief outline of the development of the discussion draft of the Living Benefits Model Act dated July 21, 1992, and corrected Sept. 29, 1992 (Attachment One-B). He stated that the purpose of this portion of the meeting was to receive additional input from interested parties with a view toward revising the draft for further review and discussion as part of the Life Insurance (A) Committee's 1993 charges.

Commissioner Yancey then recognized Brian Pardo (Life Partners, Inc.) who provided an overview of his company's involvement in the viatical settlement market. Mr. Pardo raised numerous concerns over the proposed draft and recommended that a new advisory group comprised of a broad spectrum of interested parties be formed to develop a proposal that would have consensual support among all interested parties.

Commissioner Yancey then called on Rob Worley (Living Benefits, Inc.) who serves as chair of the National Association of Viatical Settlement Companies. Mr. Worley indicated that he was not opposed to the regulation of viatical settlement companies but that greater input from a broader group of interested and affected parties needed to be included as part of the process.

Commissioner Yancey then called on Bill Freeman, Executive Director of the National Association of People With AIDS, who orally presented a prepared text on the concerns of his constituency. A copy of Mr. Freeman's statement is Attachment One-C.

Commissioner Yancey then recognized Rick Bandas (Life Partners Inc.) who shared Mr. Pardo's opinion that the model as proposed has considerable potential problems and needed additional careful study. Mr. Bandas stated that competition and the free market provided the most efficient way to arrive at a fair price and that he was not in favor of regulating discount rates or the prices that are required to be paid to viaticate life insurance policies.

Commissioner Yancey then recognized David Petersen, president of Affordable Care, a non-profit association which provides financial advice and counseling to the terminally ill. Mr. Petersen noted additional areas of concern such as preclusion from assigning group insurance for value, and inclusion in conversion policies of new contestable and suicide clauses which negatively impact a policyholder's ability to viaticate the policy. Mr. Petersen also expressed concern that no representatives of the terminally ill community had been included in the drafting of the discussion draft of the model law.

Commissioner Yancey then recognized Glen Pomeroy, Commissioner-elect from North Dakota. Mr. Pomeroy noted that there are regulatory concerns from both a securities and an insurance perspective. He felt that a fair minimum floor for payouts is something that he would be in favor of establishing and that competition and the market could establish pay-out amounts above the minimum floor.

Commissioner Yancey then noted that there was no intent to preclude anyone from participating in the work of the working group. He noted that the committee first had to identify who the various interested parties were and that he appreciated the attendance and input of those present. He stated that he wanted to make the option to viaticate policies as accessible as possible and encouraged those who wanted to participate in an advisory capacity next year to send him a letter stating this intent.

Having no further business, the Insurable Interest Working Group of the Life Insurance (A) Committee adjourned at 11:55 a.m.

ATTACHMENT ONE-A

Guidelines On Corporate Owned Life Insurance
Adopted by the Life Insurance (A) Committee
Draft: 12/7/92

Corporate owned life insurance (COLI) is life insurance a corporate employer buys covering one or more employees. With COLI, the employer is generally the applicant, owner, premium payer and beneficiary of the policy. COLI can be acquired on an individual or group basis and can take many forms. For example, it can be used to indemnify the employer for the loss of earnings or costs of replacing a key employee who becomes disabled or dies, or to finance the cost of a stock redemption agreement or a deferred compensation plan. COLI has also increasingly been used as a financing vehicle for broad-based welfare benefit plans, such as health benefit plans.

This relatively new application of the principals of corporate owned life insurance to retiree health benefits is largely attributable to the promulgation of Statement 106 by the Financial Accounting Standards Board (FASB). Under FASB 106, post-retirement benefits, including retiree health benefits, are required to be accrued as they are earned over the working lifetime of the employee, rather than as they are paid after retirement. Unfunded accrued benefits create a growing balance sheet liability. COLI or a variation thereof, Trust Owned Life Insurance (TOLI), where the insurance is purchased by a trust, typically a VEBA trust established under Section 501(c)(9)IRC, create a balance sheet asset which the employer can use to finance the cost of the benefit.

COLI and TOLI are attractive methods of financing liabilities such as an employer's obligations under a retiree health benefit plan. When for example, retiree health benefits are provided through an insured health benefit plan, the policy's cash values can be used to finance the after-tax cost of the health insurance premiums for the retired employees. When an insured retired employee dies, the policy death benefit allows the company to recover part or all of the costs of the plan. The policy values and death benefit also represent a source of funds which can be used to pay premiums for other employees who are covered under the plan.

When an employer provides health benefits to retired employees on a self-insured basis, the cash values and death benefits of the coverage are used to finance the coverage. Moreover, contributions to the VEBA Trust may, within well defined limits, be deductible to the employer.

Because of COLI's and TOLI's attractiveness in financing an employer's obligation under a plan established to provide broad-based welfare benefits to retirees, there has been increased interest in the use of COLI and TOLI for this purpose. There has also been increased interest in assuring that COLI and TOLI arrangements satisfy insurable interest requirements.

Business entities traditionally have been found to have insurable interests in the lives of their officers, managers and key employees. This is because the business may reasonably expect to benefit from the continuance of their lives or to suffer a loss if these individuals die. Many states have also recognized an insurable interest in the lives of non-key employees, particularly in the context of financing broad-based welfare benefit plans.

Some states have enacted laws that either specifically recognize an insurable interest in a COLI-TOLI arrangement, including those whose purpose is the financing of broad-based welfare plan arrangements. Other states have found such insurable interests in their common law; in interpretations of existing statutes and case law without specific COLI-TOLI enabling language.

Citations to state statutes relating to insurable interests of employers in their employees can be obtained by contacting the Legal Department of the NAIC.

States considering a legislative response to insurable interest concerns regarding employers and their employees should consider the following elements for inclusion in their law:

1. The law should recognize that employers have a lawful and substantial economic interest in the lives of key employees and in other employees who have a reasonable expectation of benefiting from an employee welfare benefit plan.
2. Employers should be required to notify eligible employees of their proposed participation in the plan and the employees should be given an opportunity to refuse to participate.
3. For non-key or non-managerial employees, the amount of coverage should be reasonably related to the benefits provided to the employees.
4. With respect to employer provided pension and welfare benefit plans, the life insurance coverage purchased to finance the plans should only be allowed on the lives of those employees and retirees who, at the time their lives are first insured under the plan, would be eligible to participate in the plan.

LIVING BENEFITS MODEL ACT
Discussion Draft: 7/31/92, corrected 9/29/92

Table of Contents

Section 1.	Short Title
Section 2.	Definitions
Section 3.	License Requirements
Section 4.	License Revocation
Section 5.	Approval of Living Benefits Contract
Section 6.	Reporting Requirements
Section 7.	Examination
Section 8.	Disclosure
Section 9.	General Rules
Section 10.	Authority to Promulgate Standards
Section 11.	Effective Date

Section 1. Short Title

This Act may be cited as the Living Benefits Act.

Section 2. Definitions

A. "Living benefits provider" means an individual, partnership, corporation or other entity that enters into an agreement with a person owning a life insurance policy insuring the life of a person who has a catastrophic or life threatening illness or condition, under the terms of which the living benefits provider pays compensation or anything of value, which compensation or value is less than the expected death benefit of the insurance policy, in return for the policyowner's assignment, transfer, sale, devise or bequest of the death benefit or ownership of the insurance policy to the living benefits provider. Living benefits provider does not include:

- (1) Any bank, savings bank, savings and loan association, credit union or other licensed lending institution which takes an assignment of a life insurance policy as collateral for a loan; or
- (2) The issuer of a life insurance policy which makes a policy loan, permits surrender of the policy or pays other policy benefits, including accelerated benefits, in accordance with the terms of the policy.

B. "Living benefits contract" means a written agreement entered into between a living benefits provider and a person owning a life insurance policy insuring the life of a person who has a catastrophic or life threatening illness or condition. The agreement shall establish the terms under which the living benefits provider will pay compensation or anything of value, which compensation or value is less than the expected death benefit of the insurance policy, in return for the policyowner's assignment, transfer, sale, devise or bequest of the death benefit or ownership of the insurance policy to the living benefits provider.

Section 3. License Requirements

A. No individual, partnership, corporation or other entity may act as a living benefits provider or enter into or solicit a living benefits contract without first having obtained a license from the Commissioner.

Drafting Note: Insert the title of the chief insurance regulatory official wherever the term "commissioner" appears.

B. Application for a living benefits provider license shall be made to the Commissioner by the applicant on a form prescribed by the Commissioner, and the application shall be accompanied by a fee of \$[insert amount].

C. Licenses may be renewed from year to year as of May 1 of each year upon payment of the annual renewal fee of \$[insert amount]. This fee shall be due on or before the first day of April for the succeeding year. Failure to pay the fee within the terms prescribed shall result in the automatic revocation of the license.

D. The applicant shall provide such information as the Commissioner may require on forms prepared by the Commissioner. The Commissioner shall have authority, at any time, to require the applicant to fully disclose the identity of all stockholders, partners, officers and employees, and the Commissioner may, in the exercise of discretion, refuse to issue a license in the name of any firm, partnership or corporation if not satisfied that any officer, employee, stockholder or partner thereof who may materially influence the applicant's conduct meets the standards of this Act.

E. A license issued to a partnership, corporation or other entity authorizes all members, officers and designated employees to act as living benefit providers under the license, and all those persons must be named in the application and any supplements to the application.

F. Upon the filing of an application and the payment of the license fee, the Commissioner shall make an investigation of each applicant and shall issue a license if he finds that the applicant:

- (1) Is competent and trustworthy and intends to act in good faith in the capacity involved by the license applied for;
- (2) Has a good business reputation and has had experience, training or education so as to be qualified in the business for which the license is applied for; and
- (3) If a corporation, is a corporation incorporated under the laws of this state or a foreign corporation authorized to transact business in this state.

G. The Commissioner shall not issue any license to any nonresident applicant, unless a written designation of an agent for service of process is filed and maintained with the Commissioner or the applicant has filed with the Commissioner, such applicant's written irrevocable consent that any action against the applicant may be commenced against the applicant by the service of process on the Commissioner of Insurance.

Section 4. License Revocation

A. The Commissioner shall have the right to suspend, revoke or refuse to renew the license of any living benefits provider if the Commissioner finds that:

- (1) There was any misrepresentation in the application for the license;
- (2) The holder of the license is otherwise shown to be untrustworthy or incompetent to act as a living benefits provider;
- (3) The licensee demonstrates a pattern of unreasonable payments to policyowners;
- (4) The licensee has been convicted of a felony or any misdemeanor of which criminal fraud is an element; or
- (5) The licensee has violated any of the provisions of this Act.

B. Before the Commissioner shall deny a license application or suspend, revoke or refuse to renew the license of a living benefits provider, the Commissioner shall conduct a hearing in accordance with [cite the state's administrative procedure act]. In lieu of revoking or suspending the license for any of the causes enumerated in this section, the Commissioner may, after the hearing, subject the licensee to a penalty of not more than \$[insert amount] for each violation, when the Commissioner finds that the public interest would not be harmed by the continued operation of the provider.

Section 5. Approval of Living Benefits Contract

No living benefits provider may use any living benefits contract in this state unless it has been filed with and approved by the Commissioner. Any living benefits contract form filed with the Commissioner shall be deemed approved if it has not been disapproved within sixty (60) days of the filing. The Commissioner shall disapprove a living benefits contract form if, in the Commissioner's discretion, the contract or provisions contained therein are contrary to the interests of the public, or otherwise misleading or unfair to the policyowner.

Section 6. Reporting Requirements

Each licensee shall file with the Commissioner on or before March 1 of each year an annual statement containing such information as the Commissioner by rule may prescribe.

Section 7. Examination

The Commissioner may, when the Commissioner deems it reasonably necessary to protect the interests of the public, examine the business and affairs of any licensee or applicant for a license. The Commissioner shall have the authority to order any licensee or applicant to produce any records, books, files or other information reasonably necessary to ascertain whether or not the licensee or applicant is acting or has acted in violation of the law or otherwise contrary to the interests of the public. The expenses incurred in conducting any examination shall be paid by the licensee or applicant.

Section 8. Disclosure

A living benefits provider shall disclose the following information no later than the date the living benefits contract is entered into:

- A. Possible alternatives to living benefits contracts for persons with catastrophic or life threatening illnesses, including, but not limited to, accelerated benefits offered by the issuer of the life insurance policy;
- B. Tax consequences that may result from entering into a living benefits contract;
- C. Consequences of interruption of assistance as provided by medical or public assistance programs; and

D. The policyowner's right to rescind a living benefits contract within thirty (30) days of its execution as provided in Section 9C.

Section 9. General Rules

A. A living benefits provider entering into a living benefits contract with any person with a catastrophic or life threatening illness or condition shall first obtain:

(1) A written statement from a licensed attending physician that the person is of sound mind and under no constraint or undue influence; and

(2) A duly witnessed and authorized document in which the person consents to the living benefits contract, acknowledges the catastrophic or life threatening illness, represents that he or she has a full and complete understanding of the living benefits contract, that he or she has a full and complete understanding of the benefits of the life insurance policy, releases his or her medical records, and acknowledges that he or she has entered into the living benefits contract freely and voluntarily.

B. All medical information solicited or obtained by any licensee shall be subject to the applicable provision of state law relating to confidentiality of medical information.

C. All living benefit contracts entered into in this state shall contain an unconditional refund provision of at least thirty (30) days.

Section 10. Authority to Promulgate Standards

The Commissioner shall have the authority to:

A. Promulgate regulations implementing this Act; and

B. Establish standards for evaluating reasonableness of payments under living benefits contracts. This authority includes, but is not limited to, regulation of discount rates used to determine the amount paid in exchange for assignment, transfer, sale, devise or bequest of a benefit under a life insurance policy.

Section 11. Effective Date

This act shall take effect on [insert date]. No living benefits provider transacting business in this state may continue to do so after [insert date] unless it is in compliance with this Act.

ATTACHMENT ONE-C

William J. Freeman, Executive Director
National Association of People with AIDS
December 7, 1992
Atlanta, Georgia

Good Morning. My name is Bill Freeman, and I am the Executive Director of The National Association of People with AIDS (NAPWA). NAPWA serves as the national consumer voice for the 2-3 million people currently living with HIV disease in the United States. My purpose today is to advocate for the needs of our constituents, most of whom count longevity in months because their immune systems have become irreversibly compromised by HIV infection. I represent those who are terminally ill due to HIV and AIDS. However, since the financial challenges facing anyone living with a terminal illness are the same challenges facing those living with AIDS, my comments can also be taken to represent the interests of all those who are terminally ill.

The message that I bring to you today is that we who advocate for the terminally ill want to preserve as much choice as possible for them. In particular, we wish to preserve the right of the terminally ill to sell their life insurance policies for cash to the company that will pay the highest amount for those policies. Our position is not based on an abstract notion of individual choice, but on the immediate reality of what it means to live with AIDS.

What is it really like to live with HIV infection or AIDS in the United States in 1992? To answer this question, NAPWA conducted the first-ever study among individuals living with HIV/AIDS to identify the needs and problems affecting them. The summary of our findings were recently released in "HIV in America: A Profile of the Challenges Facing Americans Living With HIV Disease. The report details the common challenges faced by persons living with HIV and specifically the end stage medical condition known as AIDS."

From April to June of this year, NAPWA distributed more than 30,000 surveys to people living with HIV disease throughout the United States. We received responses from 45 states, Puerto Rico and the District of Columbia. Eighty-eight percent of survey

respondents were men, 12% women. Nearly four-fifths (78.2%) were white, 12% African-American, 6.9% Latino, and 21% Native American. The mean age of respondents was 36 years old, and 93.3% were between the ages of 20 and 50 though the ages range from two to 70. Nearly half have been diagnosed with AIDS or ARC (AIDS-related complex), and the rest are asymptomatic HIV positive.

Our findings are staggering. When asked to rank their greatest needs, an overwhelming percentage of our respondents cited financial assistance. Nearly 3 out of 10 respondents are living on less than \$500 a month, and another 3 in 10 live on between \$500 and \$1,000 a month. Over a third of those who work full-time say they still need financial assistance.

More than half of those surveyed said that they had significant trouble finding enough money to pay for medicine, clothing and transportation. Paying rent and buying food were financial hardships for nearly half of those surveyed.

Health insurance, access to medicine, and health care in general were the next highest ranked categories of need. More than 32% of those who are fully employed say they lack health insurance and medicines, and 16.7% need greater access to adequate health care. The primary barrier to health care access is a lack of money. With limited income and progressive infections, many of our constituents quickly exhaust their ability to pay health care premiums and subsequently become dependent on means-based entitlement programs. Stories of the inferior quality of care provided by these programs are abundant. It is common for terminally ill AIDS patients to wait weeks to be seen by a doctor, or to wait hours (and a 24-hour wait is not uncommon) to be seen by a physician.

Given these realities—the realities of living with AIDS—people with a terminal illness must have every means available to them to extend the quality and quantity of their lives. It is estimated that as many as 50% of those living with AIDS have life insurance. The option of converting insurance policies into cash allows people with AIDS to live independently in their homes or apartments and to receive optimal health care through the continuation of private payer health insurance. Too often people with AIDS are reduced to living in shelters for the terminally ill and must bear the additional burden of reliance on the already overburdened patch-work of community services.

For those with life insurance policies, NAPWA advocates that they be allowed to sell their policies for a direct cash payment for their immediate use. In particular, we ask the National Association of Insurance Commissioners to recognize that a move to eliminate the option of selling insurance policies would be inconsistent with its desire to protect the terminally ill. The proceeds from selling a policy for a cash payment make the real difference between life with dignity and life with destitution for a person with AIDS. There is no dignity in facing the last days of one's life as part of the indigent poor.

In the proposed regulations, we endorse the requirement for full disclosure to the prospective seller of all the ramifications of the sale of one's life insurance. We also endorse the registration of all companies purchasing insurance policies from the terminally ill. We endorse background checks of all companies and their officers to prevent those who have been convicted of violations such as securities or insurance fraud from conducting business in the viatical settlement industry.

However, we are concerned that proposed regulations may overreach in a number of areas. First, while we endorse registration of companies and necessary background checks, we do not want to see a burdensome registration process. An overly burdensome process will only provide a disincentive for companies to provide this option to the terminally ill. For example, the California registration process is exhaustive; yet since the state of California represents a large market of the HIV terminally ill, a number of viatical settlement companies have registered in California in order to do business. The state of Kansas has instituted the same registration requirements as California, yet not one viatical settlement company has registered in Kansas because the estimated market for their services is small and would not make the registration requirements cost-effective. Thus, our constituents in Kansas who are terminally ill are unable to consider the option of selling their insurance and enjoying the same benefits solely because of the restrictions in their state.

Our second concern relates to minimum payments. Naturally, we want to assure that our constituents receive the highest payout for their policy. We do not believe that mandating a minimum payment is an effective way to assure the best payout. We must remember that selling one's life insurance is not an abstraction but a very simple transaction. Like selling a car, people are going to look for the best price for their policy and go with that price. One company's payout will be selected. The natural dynamics of the marketplace force companies to strive for the efficiency that will allow them to offer the largest settlement. As the national association of those with HIV disease, NAPWA maintains a national resource listing of the viatical companies, and we encourage the terminally ill to compare company payouts in order to secure the best settlement for the individual.

While seemingly well-intended, regulating a minimum payout could very well have the negative impact that it is intended to solve. Viatical settlement companies take on very real risks when buying a policy. These risks are related to time and the rating of the underlying insurance company. The length of time that the viatical settlement company will hold the policy will naturally effect its carrying costs, since there is no way that the insured person's exact longevity can be determined—particularly as more effective therapies are being developed that offer the promise of extended life for people with AIDS. We fear that a regulated minimum payout would eliminate or severely restrict the ability of an individual with a longer life expectancy to sell his or her policy for a deeper discount; no company would be able to finance a settlement for an individual with several years of life expectancy.

The second challenge that viatical settlement companies face is the rating of the underlying insurance company. The policy of an "A" rated insurance company will be bought at a small discount because of a lesser risk, while a "D" rated insurance company will necessitate a larger discount percentage. A minimum payout will greatly discourage if not eliminate outright the terminally ill person's option of selling a less optimally rated insurance policy.

In closing, we ask that as you consider draft model regulations to address the sale of insurance policies for the terminally ill that you do not establish restrictions that will unintentionally restrict or eliminate the options available to the terminally ill.

As one of the respondents to our needs assessment stated: "Every month I decide either to eat or buy medication." Clearly this is a choice that no one should ever be forced to make. With the option of converting a life insurance policy into cash, fewer people will be forced to make this choice.

ATTACHMENT TWO

Life Disclosure Working Group
of the Life Insurance (A) Committee
Atlanta, Georgia
December 6, 1992

The Life Disclosure Working Group of the Life Insurance (A) Committee met in the McKenzie Room of the Marriott Marquis in Atlanta, Ga., at 10 a.m. on Dec. 6, 1992. A quorum was present and Mike Weaver (Ala.) chaired the meeting. The following working group members were present: John Garamendi (Calif.); David Lyons (Iowa); Harold Duryee (Ohio); and Steven T. Foster (Va.).

Commissioner Mike Weaver (Ala.) began the meeting by asking the members to review the Nov. 8, 1992, minutes of the Life Disclosure Working Group (Attachment Two-C).

Commissioner Weaver then called upon John Montgomery (Calif.) to comment on the material he had distributed. Mr. Montgomery noted that the issue of policy sales illustrations is an agenda item of the Life and Health Actuarial (Technical) Task Force as well as the Life Disclosure Working Group. He stated that the material he distributed consisted of a legislative proposal and comments received in response. He said that rather than pursuing legislation in California at the present time, the department had decided to wait and see what the NAIC adopts in response to concerns regarding policy illustrations. At the request of the chair, Mr. Montgomery gave a detailed review of the draft legislation's provisions and noted that the draft was the work product of the Actuarial Department of the California Department of Insurance. A copy of the draft is Attachment Two-A.

Tony Higgins (N.C.) noted that considerable work and effort had been expended in the mid-1980s to revise the Model Life Insurance Disclosure Regulation to address concerns with policy illustrations, particularly with respect to universal life insurance. It was suggested that these revisions should be used as a starting point for evaluating additional steps to take in response to new and increasing concerns currently being expressed regarding policy illustrations. The NAIC staff was directed to provide copies of the revisions to the members for their review.

Commissioner Weaver then called upon Judy Faucett (Coopers & Lybrand) to report on the efforts being taken by the Society of Actuaries (SOA) and the American Academy of Actuaries (AAA) concerning policy illustrations. Ms. Faucett noted that she had served as the chair of the SOA Task Force on Life Illustrations and that the task force had conducted an extensive survey of life insurance companies and insurance departments on the nature and extent of problems that exist with respect to policy illustrations. As a result of the survey the task force determined that consumers do not understand illustrations or how they should be used. She noted that the task force's findings and recommendations were contained in a report presented to the AAA and that a copy of the report had been distributed to the working group members. Ms. Faucett explained that the SOA is the educational and research arm of the AAA and that final policy recommendations are the responsibility of the AAA. She noted that in conducting the survey, the SOA did not specifically solicit input from consumer advocacy groups but that some consumer input had been received. Ms. Faucett noted that the AAA Task Force on Life Illustrations had reviewed the recommendations of the SOA and had issued a preliminary report (Attachment Two-B), which contained recommendations for required changes which should be implemented for policy illustrations. She noted that some of the recommendations are for immediate changes and that others would require a longer time-frame for implementation. Ms. Faucett felt it was important to coordinate the activities of the various groups that are evaluating concerns regarding policy illustrations and Commissioner Weaver responded by noting that he hoped that the working group could serve that purpose.

Commissioner Weaver then called upon James Hunt (National Insurance Consumer Organization) to give a consumer advocacy perspective. Mr. Hunt stated that he is a funded consumer representative under the NAIC Consumer Participation Program. He provided examples from testimony he had given before Senator Metzenbaum's committee and from an article he had written for publication that illustrated the role that rate of return calculations could and should serve in providing meaningful disclosure to consumers.

Mr. Hunt noted that he had testified to U.S. Senator Howard Metzenbaum that he felt that the zeal with which some companies and agents engage in the replacement of whole life insurance was related to the problems that exist with respect to sales illustrations. He noted that 50% of whole life insurance sales were replacement sales and that most were ill-advised in terms of the financial effect to policyholders. Mr. Hunt felt that rate of return calculations would help consumers make an informed decision with respect to replacing current life insurance coverage.

Mr. Hunt also cited manipulation of mortality assumptions, sales misrepresentations regarding vanishing premium policies, manipulation of surrender charges and bonus abuses as additional areas of concern.

Mr. Hunt recommended that the regulatory practices of the United Kingdom and Australia, as discussed in the SOA's report, are worthy of review and consideration by the working group.

The chair then recognized Bill Albus (National Association of Life Underwriters) who noted that his organization, along with other prominent insurance agent organizations, had formed a committee to address policy illustration concerns and that they would also take part in any activity the NAIC undertakes to address the concerns.

Bart Munson (William M. Mercer Inc.) noted that life insurance disclosure issues have been the subject of ongoing debate for years and that extensive work occurred in the mid-1970s. He noted that while he is in favor of addressing the current problems associated with policy illustrations, he cautioned that it could be an extremely challenging and time-consuming effort.

Commissioner Weaver then asked the group if it was of the opinion that a recommendation should be made to the Executive Committee to continue this working group as part of the 1993 charges of the Life Insurance (A) Committee. The consensus of the group was to make such a recommendation.

Having no further business, the Life Disclosure Working Group of the Life Insurance (A) Committee adjourned at 11:20 a.m.

ATTACHMENT TWO-A

State of California
Department of Insurance
Actuarial Division
3450 Wilshire Blvd.
Los Angeles, CA 90010

September 30, 1992

To: John O. Montgomery
From: W. Harold Phillips, Senior Life Actuary
Subject: Additional Data for Proposed Ledger Illustration Law

This memo provides the information requested by Mark Rakich in his memo of 9/18/92 for legislation proposed by the department.

1. Regulation of the preparation and use of sales ledger illustrations employed in the sale of permanent life insurance and deferred annuities.
2. The problem: misleading sales illustrations structured as inducements to buy rather than helpful tools in understanding the workings of the product or as a comparison between products of competing companies. In addition many purchasers as well as agents do not understand what an illustration is and what it is not.

Most agents, companies and actuaries agree that there is a problem and that something needs to be done. The industry appears to be in gridlock on this matter. The proposed legislation will break the gridlock and force solutions. Regulations seem to take too long and can get bogged down (e.g. OAL). Legislation is preferable. It will permit purchasers to make better purchase decisions in the purchase of life insurance and deferred annuities. It will force companies to avoid gimmicks and concentrate on competing on the basics: better value for your insurance dollar.

Current regulation of illustrations is very weak. Companies and agents can do pretty much as they please.

3. Sales illustrations will have to conform to the principles and rules of the legislation and any regulations flowing therefrom. The new law will impact all life insurance companies and their agents that market permanent life insurance and deferred annuities.
4. To our knowledge, only the actuarial division has been involved in the problem and has given consideration to possible solutions. The contact person is Harold Phillips 213-677-7582 in Los Angeles, or other life actuaries.
5. The draft legislation is attached.
6. Consumer groups and consumerists will applaud the legislation. This is somewhat complex area and we are not aware of other ideas arising from consumer groups to solve the problems. Most consumers are not aware of the problem, until the company pays less than they were expecting. The lack of understanding of what an illustration is and is not comes to the fore.

7. The opposition will be on two grounds:

- (a) The cost of retooling and re-education of agents. Virtually all companies will have to change their illustrations.
- (b) Those companies and agent's whose products will look less competitive will scream the loudest.

The proposal was aired about two years ago. It was met with a deadening silence—no reaction at all. Perhaps there was great fear that it would be seriously be proposed at some time, as it is now.

8. To a large extent the law will be self-regulating. Once companies adjust they likely will continue on the right path. Current staff can handle the minor additional work load. The filing of the illustration with the policy form may indeed help the understanding of the workings of the product and thus facilitate review.

Draft Copy For Discussion Only

Article 9. Requirements For Ledger Illustrations Used In
The Sale Of Life Insurance And Annuity Policies

Section 10509.10 Purpose

The purpose of this article is the following:

- (a) To regulate the preparation and use of ledger illustrations in sale of permanent life insurance and deferred annuities.
- (b) To establish standards to be used in preparation of ledger illustrations used in the sale of permanent life insurance and deferred annuities.
- (c) To help educate the purchaser as to the understanding of and proper use of a ledger illustration.

Section 10509.11 Application of Article

This article is applicable to all life insurance and annuity sales where a ledger illustration is used in the solicitation.

Section 10509.12 Definitions

- (a) "Ledger illustration" means a year by year extension into the future of values and benefits on a guaranteed (G) and nonguaranteed or illustrated basis (NG), the latter (NG) on the assumption that current experience factors such as interest mortality and expense, will continue unchanged into the future. (Note the statute imposes a maximum interest rate after 10 years.)
- (b) "Current scale" means the current dividend scale for participating insurance or the current set of interest, mortality and expense factors used in the illustration of nonguaranteed charges or benefits.

Section 10509.13 Insurance and Annuities Excluded From This Article

Unless otherwise specifically included, this article does not apply to the following:

- (a) Credit life insurance.
- (b) Term insurance.
- (c) Noncontributory group life insurance where a ledger illustration is not used in the solicitation of the business.
- (d) Reinsurance.
- (e) A solicitation where a ledger illustration is not used.

Section 10509.14 Requirements for the Preparation of Ledger Illustrations.

Every ledger illustration prepared for delivery in this state shall meet the following requirements:

- (a) The ledger illustration must be based on factors not more favorable than what the company is currently paying under the insurer's current scale.
- (b) Each ledger illustration must state that it is neither a guarantee nor an estimate of future results, that it is based on current pricing factors which can change and that as these factors change the scale will change and that it is a virtual certainty that actual results will differ from what was illustrated.
- (c) Current dividends shall be illustrated with the use of experience factors consistent with current experience. Nonguaranteed charges and benefit factors shall be illustrated with the use of experience factors consistent with currently anticipated experience.

- (d) Within 120 days from the date it is determined that the currently illustrated scale cannot be supported by current experience or currently anticipated experience, the illustrated scale shall be reduced to that which can be supported.
- (e) The development of current scales and ledger illustrations shall be consistent with the principles and standards of performance as promulgated by the Actuarial Standards Board of the American Academy of Actuaries.
- (f) Ledger illustrations may not assume ongoing changes that would increase the scale (e.g., improving mortality). Ongoing changes that would reduce the scale are permitted (e.g., increasing unit expenses or decreasing interest rates).
- (g) Projection of experience trends is not permitted beyond one year. Consistency between current scales and ledger illustrations is required. Ledger illustrations shall be related to scales actually being paid on in-force plans in an equitable and justifiable manner.
- (h) Ledger illustrations shall appropriately reflect the current financial results of the company.
- (i) Each company shall have a written current policy on file at its home office (available to the commissioner on request) for determination and redetermination of dividends and nonguaranteed charges and benefits currently being paid and illustrated.
- (j) In the redetermination of nonguaranteed charges and benefits for current payment or illustration past losses are not permitted to be used. Past gains may be used for the determination of current payout but not for illustrations.

Draft Copy For Discussion Only
Guide To Understanding Of Ledger Illustrations

- (k) The projected interest rate of return for nonguaranteed benefits for durations beyond 10 years shall not exceed the rate of return on 30-year treasury bills rounded to the lower .25%, or the guaranteed rate, if higher. For the current calendar year the rate on Oct. 1 of the previous calendar year shall be used. Where an interest margin is used to cover expenses, such 30-year treasury rate shall be reduced by such margin.
- (l) Where an interest margin is used to amortize initial expenses, the interest rate credited may increase after the expenses are fully amortized. However, such increase may not be illustrated.
- (m) A ledger illustration based on the current scale shall accompany each form filing.
- (n) The ledger illustration shall show with equal or greater prominence the guaranteed values and benefits along with those not guaranteed. Each column must be designated G-guaranteed, or NG-not guaranteed.

Section 10509.15 Regulations

The commission may issue regulations to support this article. Such regulations shall cover items such as smoothness tests, forward pricing, lapse supported ledger illustrations, supportability, enhancements and other related topics.

Section 10509.16 Additional Requirements

- (a) A ledger illustration shall be provided that is consistent with the policy actually issued (the amount of coverage, premium, mortality class, etc.).
- (b) The applicant shall sign a statement that he or she has reviewed the ledger illustration and that he or she understands its limitations. This acknowledgment along with a copy of the illustration shall be retained with the original application by the insurer.
- (c) The insurer shall notify the policy owner each time there is a decrease in scale below what was originally illustrated. Upon request the insurer shall provide new illustrated values based on the current scale.
- (d) The following Guide to Understanding of Ledger Illustrations shall be presented with each ledger illustration.

This guide is being provided to you so that you can better understand what a ledger illustration is and is not. This is required by law.

What is a ledger illustration?

It is an extension into the indefinite future of current experience factors affecting interest, mortality and expense. These factors reflect current experience. As experience with the factors that affect the performance of a product change, the numbers and results that are nonguaranteed will also change. The ledger illustration also shows with equal prominence values that are guaranteed. The company cannot pay less than these. (Note: the statute imposes a maximum interest rate after 10 years.)

What are the chances that a company will pay exactly what is illustrated?

Nil or zero. If nothing changes in all the experience factors the company will be able to pay exactly what is illustrated. However, we know that these factors will change as experience changes. Interest rates go up and down. Mortality experience changes: it is helped by medical breakthroughs and hurt by things similar to AIDS. Unit expenses change: helped by increased productivity and hurt by inflation.

What are the chances that the company will be able to pay more than illustrated?

It depends on how likely experience factors will be better in the future. For example, as interest rates increase and are greater than those in effect at the time of purchase, chances are very good that the company will pay more.

What are the chances that the company will have to pay less than illustrated?

It depends on how likely experience factors will be poorer in the future. For example, if interest rates decrease and are lower than those in effect at the time of purchase, it is very likely the company will pay less.

Should I rely on the numbers in the illustration?

"Yes" for the guaranteed numbers. For the nonguaranteed numbers—"not at all": these are to show you how the plan would work and help you understand the plan based on an extension into the future of current experience factors which will change as experience unfolds.

What is a ledger illustration not?

The nonguaranteed portion of a ledger illustration is:

- (a) Not a guarantee to pay what is illustrated.
- (b) Not a promise to pay what is illustrated.
- (c) Not a most likely scenario of what will be paid. It might be the least likely.

Remember: The purpose of a ledger illustration is to help you understand how the product works. The better you understand the product the better you'll be able to compare similar products of other companies.

Section 10509.16 Administrative penalties

Same as Section 10509.9

Section 10509.17 Effective date

This article shall become effective Jan. 1, 1994.

ATTACHMENT TWO-B

Preliminary Report American Academy of Actuaries Task Force on Life Illustrations

The AAA Task Force on Life Insurance Illustrations has reviewed the recommendations from the research paper on illustration practices prepared by the SOA. Our primary goal is to focus on changes that will benefit consumers and third-party users of illustrations. A secondary goal is to improve illustration methodology for those involved in developing illustrations and setting the underlying assumptions: actuaries, agents and company management.

Changes to illustrations can be considered in three categories:

- (1) Those that should occur immediately due to perceived problems at the consumer level. Action by the NAIC will be required for these changes to have a widespread and immediate impact.
- (2) Those that require broader exposure within, and input from, the industry. It is expected that these changes can be implemented over the next few years, although work within the industry would begin immediately. Regulatory action may be needed to allow for changes in practice.
- (3) Educational efforts that require broad-based support within the industry. While some of these efforts can be implemented in the short-term, changes in consumer and industry perceptions of illustrations will evolve over time.

The Task Force recognizes that as education efforts have an impact on the use of illustrations, some of the short-term changes may no longer be required. However, such changes are necessary on an interim basis to assist the consumer.

o Immediate Changes

These changes are very specific and deal with product structures and premium financing.

Vanishing Premium Illustrations

- (1) Require adequate disclosure of the vanish concept, either through a footnote, additional columns or illustration of an alternative scenario.
- (2) Require illustrations of guaranteed and non-guaranteed values to be based on consistent premium and death benefit patterns.
- (3) Require an illustration showing the premiums necessary to maintain the original death benefit for all years under guaranteed assumptions.
- (4) Change the name from "guaranteed values" to "policy values based on guaranteed assumptions."

Second-to-Die Policies

- (1) Require a statement regarding whether policy values change at the first death, and how they change.
- (2) If values do change, describe when the first death is illustrated to occur and why this assumption was selected (policyholder request, life expectancy of that insured, etc.). To be complete, the illustration must demonstrate the operation of the contract when both insureds are alive and after the first death.

Modular Policies

These are policies that allow for blends of term riders, PUA riders and dividend options to provide an integrated package of benefits.

- (1) Disclose the modular structure (both initial premiums and initial death benefits) clearly in the illustration. The illustrated values based on guaranteed assumptions should be consistent with the premium pattern.
- (2) Disclose the current and guaranteed premium for any applicable term coverage (whether provided by riders or dividends).
- (3) Require an illustration showing the cost for the total death benefit in all years under guaranteed assumptions.

Two-Tier Policies

- (1) Life insurance and annuity components should be illustrated separately.
- (2) If current annuitization values are shown, guaranteed values must also be shown (both with respect to annuitization fund and monthly income).

Cost Comparisons

- (1) Require the illustration to include a footnote similar to the following:

Sales illustrations should not be used for comparative policy performance purposes. Life insurance policies are complex financial instruments, which generally contain both guaranteed and non-guaranteed elements. A sales illustration may be helpful in understanding how a particular policy performs under specified circumstances. It is generally not feasible, however, to use sales illustrations to determine whether one policy is a better buy than another.

- (2) Delete the interest-adjusted cost indexes from point-of-sale illustrations, recognizing that these indexes are generally used to compare policy costs.

• Short-Term Changes

Factions within the industry have considered or recommended changes. To be effective, rather than offering more and possible conflicting recommendations, our Task Force suggests industry-wide consideration of the following:

- (1) Disclosure of the underlying assumptions which could reasonably be understood and evaluated by the consumer.
- (2) Use of standardized earned rate assumptions, that are linked to short-term and long-term indexes, to illustrate sensitivity to different interest rate environments.
- (3) Consideration of other sensitivity analyses that may be helpful to the consumer.
- (4) Development of standardized definitions of the terms generally displayed in the illustration.

- (5) Consideration of standardized notes as appropriate.
- (6) Optional use of different print (bolder or bigger) to be permitted for specific notes.

The results of this industry-wide review should be a package of recommended changes that can generally be supported by companies, agents, actuaries, regulators and other insurance professionals.

There is one short-term action that could be undertaken by the actuarial profession. The recommended change would be to develop appropriate definitions of such terms as "current experience," "best estimate" and "supportability," that underlie the Actuarial Standards of Practice. This would be a project recommended to the Actuarial Standards Board. This action might help actuaries, but would have limited impact on the perceived problem with illustrations.

o Long-Term Changes

These are strategies that are largely educational. The goal of these efforts is to make the creators and users of illustrations aware of the limitations on, and the appropriate uses of, illustrations. The Task Force believes that most of these strategies will require industry-wide support and cooperation. Among the items to be considered are:

- (1) Development of a consumer brochure that is presented at point-of-sale.
- (2) Education strategies for agents, actuaries and company personnel.
- (3) Research into appropriate methodologies/measures to compare companies and products.

The third item was identified as a research project for the SOA, although a task force has not yet been formed.

ATTACHMENT TWO-C

Life Disclosure Working Group
of the Life Insurance (A) Committee
Boston, Massachusetts
November 8, 1992

The Life Disclosure Working Group of the Life Insurance (A) Committee met in the Simmons Room of the Boston Marriott, Copley Place Hotel in Boston, Mass., at 8:30 a.m. on Nov. 8, 1992. A quorum was present and Mike Weaver (Ala.) chaired the meeting. The following working group members or their representatives were present: Harold Duryee (Ohio); Steven Foster (Va.); John Garamendi (Calif.); and David Lyons (Iowa).

Commissioner Weaver (Ala.) began by noting that the formation of the working group was prompted by U.S. Senator Howard M. Metzenbaum's letter of Sept. 18, 1992, addressed to Director William McCartney (Neb.) and Commissioner Steven Foster (Va.) regarding the adequacy of information disclosed or available to consumers of life insurance. Commissioner Weaver explained that one of the Senator's main concerns dealt with computer generated sales illustrations. Commissioner Weaver began the open forum discussion of this concern by stating that, while he felt there was a place for sales illustrations when used in a reasonable and responsible manner, there was no place in the market for illustrations that are misused. He stated that the purpose of the meeting was to begin to get a feel for the nature and extent of the problems that exist with respect to illustrations, if any, and to begin to identify means of addressing the problems identified. He said that judging from the amount of activity being undertaken regarding policy illustrations by other organizations, such as the Society of Actuaries, the American Academy of Actuaries and the Society of CLUs along with the media attention that policy illustrations have received, it seemed likely that there were some problems in this area that require a regulatory response.

Bob Katz (Ohio) noted that misrepresentations are prohibited by the Unfair Trade Practices Act of practically every state and that Ohio regulates sales illustrations on an exception basis, i.e., while specific guidelines, requirements or parameters have not been established, if a policy illustration is used in a misrepresentative manner, Ohio can and will intervene.

This sentiment was echoed with a number of people of the opinion that while outright fraud and misrepresentations are illegal and violations can be prosecuted, you cannot prevent someone who is determined to use illustrations in an abusive manner from doing so.

The consensus was that the effort of the group should be to address problems with misunderstandings as to what policy illustrations are and how they should be used.

Mr. Katz expressed an interest in obtaining the transcript of the testimony presented before Senator Metzenbaum at his June 23, 1992, subcommittee meeting. He said he felt it was important for this working group to determine whether the Senator's concerns arise from a few egregious anecdotal examples or whether the examples typify a widespread problem. The NAIC staff was directed to obtain a copy of the transcript and circulate it to the members of the working group.

The group then engaged in a general discussion of the differences and similarities between life insurance and securities and the disclosure requirements applicable to both. The group noted that the NAIC Model Rules Governing the Advertising of Life Insurance contained requirements concerning the advertising or illustration of non-guaranteed policy elements but acknowledged that they had not been widely adopted.

The group identified a number of potential responses such as: (1) establishing standardized definitions of terms or assumptions used in preparing illustrations; (2) adopting a range approach which would allow for standard variations of a set percentage above and below the current scale; (3) requiring illustrations to include a projection based on past performance with a caveat that historical performance is no guarantee of future performance; and (4) enhancing the disclosures used with illustrations so the consumers would have a better opportunity to understand which elements of the sales illustrations are guaranteed and which elements are not.

The group recognized that it needed more information in order to fully understand the nature and extent of the problems that exist with respect to policy illustrations. It was noted that a number of other groups had recently spent a considerable amount of time and effort in studying illustrations and that the working group could benefit from their knowledge.

George Coleman (Prudential) volunteered to chair the advisory committee and the NAIC staff was directed to work with him to distribute copies of the Society of Actuaries' Report on Policy Illustrations to members of the working group and to facilitate the participation of the society and other interested and knowledgeable parties in the next meeting of the working group at the NAIC Winter National Meeting in Atlanta on Dec. 6, 1992. It was noted that the scheduled one-hour format would probably be insufficient and staff was directed to attempt to get an extension of the time allotted to two hours.

Having no further business, the Life Disclosure Working Group of the Life Insurance (A) Committee adjourned at 10:50 a.m.

ATTACHMENT THREE

Life Insurance (A) Committee Conference Call November 24, 1992

The Life Insurance (A) Committee held a telephone conference call on Nov. 24, 1992, at 1:30 p.m. Central time. A quorum participated in the call and Commissioner Mike Weaver (Ala.) chaired the meeting. The following committee members or their representatives participated: David J. Lyons (Iowa); John Garamendi (Calif.); James H. Brown (La.); Harold T. Duryee (Ohio); Georgia D. Flint (Texas); Harold C. Yancey (Utah); and Steven T. Foster (Va.).

Commissioner Mike Weaver (Ala.) noted that the purpose of the call was to consider adoption of a Guide to Buying Life Insurance After Age 60 (Attachment Three-A) along with a proposed amendment to Section 8(I) of the NAIC Model Life Insurance Disclosure Regulation (Attachment Three-B).

Commissioner Weaver called on Roger Strauss (Iowa) to give a brief overview of the guide and the proposed amendment to the model. Mr. Strauss noted that the guide was the result of considerable time and effort on the part of the drafting group and represented a consensus of industry and consumer representatives as well as regulators. He noted that the purpose of the guide was to help consumers use and understand the Financial Review of This Policy disclosure form. He explained that there were differences of opinion as to the appropriate time for delivery of the guide with some in favor of requiring delivery at point-of-sale and others of the opinion that the only practical time for delivery of the guide is with the Financial Review of This Policy disclosure form and the policy. He noted that while states would have the capability of modifying the rule to fit their particular circumstances, the proposed amendment had the effect of requiring the guide to be delivered with the policy any time the policy triggers the delivery of the Financial Review of This Policy disclosure form.

Upon completing his explanation of the guide and proposed amendment, Mr. Strauss moved that both recommendations be adopted.

Bob Katz (Ohio) suggested that the recommendations be considered separately. This suggestion was concurred to by Mr. Strauss and the committee proceeded to discuss the recommendation relating to the adoption of the guide.

Mr. Katz indicated that consumer advocacy representatives from his department felt that certain changes should be made to the guide. He acknowledged that the guide could be revised to fit the particular needs of Ohio citizens but noted that Ohio would have difficulty voting in favor of the guide in its current form.

Upon further discussion of the guide and upon motion duly made and seconded the committee adopted the guide with Ohio the only member opposed.

The discussion then turned to adoption of the proposed amendment. Sheldon Summers (Calif.) noted that he had submitted comments regarding the appropriate time for delivery of the guide which he had assumed would be discussed at the Atlanta meeting. Mr. Strauss indicated that the issue of the appropriate time of delivery is subject to further debate if the Executive Committee gives such a charge to the A Committee or if Commissioner Weaver takes it up as part of his ongoing analysis of life insurance disclosure in general but that it was his opinion that the proposed amendment should be adopted as proposed. Mr. Katz concurred and felt that the proposal was the most reasonable and practical approach to take.

After further discussion and upon motion duly made and seconded, the proposed amendment was adopted with no opposition and California abstaining.

Having no further business the Life Insurance (A) Committee adjourned at 2 p.m.

ATTACHMENT THREE-A

Guide To Buying Life Insurance After Age 60 Appendix F to Life Insurance Disclosure Model Regulation Draft: 10/19/92

This guide is designed to help you review your life insurance policy. Like many financial products, life insurance is regulated to protect buyers. It's not possible to discuss all of the consumer protections in this guide. Also, they vary from state to state. This guide discusses two items of particular importance to older buyers, the "free look" period and the Financial Review of This Policy form.

You will also receive a *Life Insurance Buyer's Guide*. It has additional information you may wish to review. Both guides were prepared by the National Association of Insurance Commissioners, an association of state insurance officials. Neither guide endorses any company or policy.

"Free Look" Period

With every new policy, your state requires insurance companies to provide policyholders with a "free look" period. During that period you can reconsider your decision to purchase the policy. Your policy has a 30-day "free look" period. If you choose to cancel during the "free look" period, the company must refund the premium paid (premiums are the amount you pay for coverage). The clock starts ticking when you receive the policy.

The "free look" period is the time for you to decide if the life insurance policy meets your needs.

Financial Review

To help you make a financial evaluation of your policy, before you make your final decision to keep it, insurance regulations in your state require life insurance companies to furnish some buyers over age 60 with a financial review of their policy. This review displays your policy's premiums, death benefits (the amount your beneficiary, the person you designate, receives after death) and cash values (the amount available if you cancel). Not every buyer over 60 will receive this form. Persons receiving the form purchased a policy where:

- Premiums for the policy, plus 5% interest, compounded annually, exceed death benefits at some time during the first 10 years; or
- Death benefits are limited for some period after the policy is issued (for example, a policy that limits death benefits for the first two years).

Drafting Note: State law may require full death benefits for accidental death.

The review form is an individual analysis of your policy. It's displayed on a form called a "Financial Review of This Policy." The review is designed to help you decide if this policy makes financial sense for you and your family.

This guide uses two examples to let you see how the review form works with two different policies. These are real policies purchased by people over age 60. The policy you buy will almost surely be different from these two. Nevertheless, these illustrations should help you evaluate your policy.

Marvin Policyholder

Marvin Policyholder is 77 years old and bought an increasing benefit life policy. Even though he pays premiums over a 10-year period, his death benefits begin on day one. The policy returns an increasing death benefit as long as Marvin pays his annual premium of \$507.38 (\$5,073.80 over 10 years). The death benefit starts at \$1,500.00 and increases by \$75.00 each year. Marvin received a copy of his policy and the review form at the same time.

Forms may vary from state to state, but Marvin's looked like this:

FINANCIAL REVIEW OF THIS POLICY

Notice: You have thirty (30) days to review your policy and, if not entirely satisfied, to return it for a full refund of any premiums paid.

[] This is a guaranteed issue policy offered without an attempt to classify risks by determining your state of health. Premiums may have been lower if health information had been obtained.

[x] This is a policy issued on the basis of the answers to the health questions set forth in the application. Premiums may have been lower if further health information had been obtained.

[x] This is a policy where the accumulated premium exceeds the death benefit in 10 years or less.

Applicant information:

Name: Marvin Policyholder Age: 77 Sex: M

List other personal information used in determining the premium for this policy:

End of Policy Year	1 Premiums	2 Premiums Accumulating Interest at 5%*	3 Death Benefits	4 Cash Surrender Value	5 Column 3 minus Column 2 Net Gain (Net Loss)
1	\$507.38	\$532.74	\$1500.00	\$45.66	\$967.26
2	\$507.38	\$1092.12	\$1575.00	\$206.79	\$482.88
3	\$507.38	\$1679.47	\$1650.00	\$374.59	\$(29.47)
4	\$507.38	\$2296.19	\$1725.00	\$550.79	\$(571.19)
5	\$507.38	\$2943.75	\$1800.00	\$737.55	\$(1143.75)
6	\$507.38	\$3623.68	\$1875.00	\$938.06	\$(1748.68)
7	\$507.38	\$4337.60	\$1950.00	\$1157.15	\$(2387.60)
8	\$507.38	\$5087.23	\$2025.00	\$1402.34	\$(3062.23)
9	\$507.38	\$5874.33	\$2100.00	\$1684.77	\$(3774.33)
10	\$507.38	\$6700.79	\$2175.00	\$2020.76	\$(4525.79)

Definitions: The following terms used in the above chart are defined as:

1. Premiums – Amount you must pay each year to keep this policy in force.
2. Premiums Accumulating Interest at 5% – The amount which could be earned if, instead of purchasing insurance, the dollars were left to accumulate at 5% interest.
3. Death Benefits – The amount that will be paid upon your death exclusive of any supplementary benefits.
4. Cash Surrender Value – The amount the insurance company will pay you if you surrender your policy to the company for cash.
5. Net Gain or Loss – This column shows whether your money would have earned more or less at 5% interest than your life insurance benefit.

*Note: This figure does not take into account the cost of insurance, any dividends or additional benefits which are not guaranteed under the policy, nor potential preferential tax implications.

If death benefits have been explained in any manner other than shown on the above chart (through use of CPI index, dividends, or other non-guaranteed increase or a reduction in premium), a copy of the illustration signed by the applicant and agent must be attached.

At the top of the form (below the line discussing the 30-day "free look" period) are three boxes. The insurance company checked the second box because Marvin's policy was underwritten. He was required to answer several health questions on his application.

The third box was checked because Marvin's premiums at 5% compound interest, exceed death benefits before the end of 10 years. This occurs in the third year. Whenever premiums accumulated at 5% interest exceed benefits within the first 10 years of a policy, the insurance company is required to check this box.

Next comes Marvin's name, age, and so on. Below that are six columns of information about his policy. Columns 1, 2, 3, and 5 explain in more detail the relationship between the actual premiums Marvin paid, and what would have been the result if he had put money in a 5% compound interest account instead. It also displays how the death benefits increase.

End of Policy Year—This column gives the time frame on which columns 1 through 5 are based. That is, how do premiums and benefits, and cash surrender values, all of which change, compare at the end of each year for 10 years?

Premiums—This column (Number 1) shows that Marvin pays \$507.38 a year for each of the 10 years shown in the chart. At the end of the 10-year period, Marvin has paid \$5073.89.

Premiums Accumulating at 5%—Here the form (column Number 2) provides Marvin with another way of looking at his life insurance policy. If his premium dollars were deposited every year in a savings instrument, an annuity or other financial product, earning 5% compound interest instead of buying this policy, how would they perform?

Life insurance really isn't a savings investment. For example, Marvin's eligible for \$1500 in death benefits on day one even though he paid only \$507.38. In addition, these benefits aren't taxed. Both of these could be to his advantage. On the other hand he also needs to look at how much it costs for these death benefits over time.

Death Benefits—Column Number 3 indicates the amount of the death benefits his policy provides as long as Marvin pays his premiums. Benefits with Marvin's policy increase every year during the first 10 years by an amount of \$75. This amount increases over the life of the policy.

Cash Surrender Value—This column (Number 4) tells Marvin how much he would receive if he cancels his policy. This amount increases over the life of the policy. Not all policies, however, provide a cash surrender value*.

* Term insurance, for example, does not. See Life Insurance Buyer's Guide for more information.

Net Gain, Net Loss—The last column (Number 5) provides Marvin with cost-benefit information. It is a comparison of columns 2 and 3. Notice the column changes every year. Column 5 tells Marvin:

- For the first two years, his policy has a net gain (\$967.26 in year one, and \$482.88 in year two);
- In the third year, however, there is a net loss. His policy reports a net loss every year after that. Whenever there is a loss, it is reported inside parenthesis such as (\$29.47).

This is important information. Marvin needs to weigh this comparison with his reasons for buying life insurance and then decide if this policy best meets his needs.

Marla Policyholder

Now let's look at a policy purchased by Marla Policyholder. She is a 65 year old woman who purchased a guaranteed issue policy. This means no health questions are asked. Her policy's death benefits are reduced for the first two years. Death benefits are \$470 at the end of the first year, and \$940 at the end of the second. After the third year, however, they rise to \$3880.

Her financial review looked like this:

FINANCIAL REVIEW OF THIS POLICY

Notice: You have thirty (30) days to review your policy and, if not entirely satisfied, to return it for a full refund of any premiums paid.

☒ This is a guaranteed issue policy offered without an attempt to classify risks by determining your state of health. Premiums may have been lower if health information had been obtained.

☐ This is a policy issued on the basis of the answers to the health questions set forth in the application. Premiums may have been lower if further health information had been obtained.

☐ This is a policy where the accumulated premium exceeds the death benefit in 10 years or less.

Application Information:

Name: Marla Policyholder Age: 65 Sex: F

List other personal information used in determining the premium for this policy:

End of Policy Year	1 Premiums	2 Premiums Accumulating Interest at 5%*	3 Death Benefits	4 Cash Surrender Value	5 Column 3 minus Column 2 Net Gain (Net Loss)
1	\$235.20	\$241.52	\$470.40	\$0.00	\$228.88
2	\$235.20	\$495.12	\$940.80	\$72.00	\$445.68
3	\$235.20	\$761.40	\$3880.00	\$96.00	\$3118.60
4	\$235.20	\$1041.00	\$3880.00	\$120.00	\$2839.00
5	\$235.20	\$1334.56	\$3880.00	\$140.00	\$2545.44
6	\$235.20	\$1642.80	\$3880.00	\$160.00	\$2237.20
7	\$235.20	\$1966.48	\$3880.00	\$176.00	\$1913.52
8	\$235.20	\$2066.32	\$3880.00	\$184.00	\$1813.68
9	\$235.20	\$2663.16	\$3880.00	\$188.00	\$1216.84
10	\$235.20	\$3037.84	\$3880.00	\$184.00	\$842.16

Definitions: The following terms used in the above chart are defined as:

1. **Premiums** – Amount you must pay each year to keep this policy in force.
2. **Premiums Accumulating Interest at 5%** – The amount which could be earned if, instead of purchasing insurance, the dollars were left to accumulate at 5% interest.
3. **Death Benefits** – The amount that will be paid upon your death exclusive of any supplementary benefits.
4. **Cash Surrender Value** – The amount the insurance company will pay you if you surrender your policy to the company for cash.
5. **Net Gain or Loss** – This column shows whether your money would have earned more or less at 5% interest than your life insurance benefit.

*Note: This figure does not take into account the cost of insurance, any dividends or additional benefits which are not guaranteed under the policy, nor potential preferential tax implications.

If death benefits have been explained in any manner other than shown on the above chart (through use of CPI index, dividends, or other non-guaranteed increase or a reduction in premium), a copy of the illustration signed by the applicant and agent must be attached.

As you can see, Marla's policy is very different. The major differences are: (1) death benefits exceed premiums accumulating at 5% for all 10 years, and (2) death benefits are limited for the first two years.

Box number one is checked because this is a guaranteed issue policy. No health questions were asked of Marla. Therefore, the second box wasn't checked. This third box wasn't checked because benefits exceed premiums accumulating at 5% for all 10 years. Let's now look at how the policy compares in the five columns of information.

Premiums—Marla pays \$235.20 a year for 10 years for a total of \$2,352.00.

Premiums Accumulating at 5%—The amount in this column is less than the amount if death benefits are payable in each of the first 10 policy years.

Death Benefits—Marla's death benefits are reduced for the first two years and then are \$3,880.00 for the next eight years.

Cash Surrender Value—Cash surrender values are low with Marla's policy.

Net Gain, Net Loss—Marla's policy consistently reports a net gain for the first 10 years. This means her life insurance death benefits are greater than premiums accumulating at 5% interest for the first 10 years.

Part of the difference between Marvin's and Marla's policies is tied to the fact that Marla is younger and she's a woman. Life insurance premiums are usually based on age and sex.

The difference between these policies is also related to the fact that different companies offer different policies. It's up to you to choose what's best for you. You should review your reasons for buying life insurance, your age, and health. In addition, a careful financial review of your policy is needed. This guide is designed to help you review your life insurance policy.

You should also read your policy carefully before deciding to keep it. If you have any questions or if anything is unclear, contact your agent, the insurance company, or your state insurance commissioner.

ATTACHMENT THREE-B

Life Insurance Disclosure Model Regulation Amendment

Section 8. General Rules

I. Whenever a policy is issued for delivery in this state to an applicant at age sixty (60) or over, which limits death benefits during a period following the inception date of the policy or where the accumulated premiums exceed the death benefit at any point during the first ten (10) years, then the form and guide labeled Appendix E to this regulation or a form and guide containing substantially similar information and approved by the commissioner of insurance shall be completed by the insurer and delivered simultaneously with the policy and the free-look period shall be extended to thirty (30) days.

ATTACHMENT FOUR

Life Insurance (A) Committee
Cincinnati, Ohio
September 21, 1992

The Life Insurance (A) Committee met in the Hall of Mirrors at the Omni Hotel in Cincinnati, Ohio, at 3 p.m. on Sept. 21, 1992. A quorum was present and Mike Weaver (Ala.) chaired the meeting. The following committee members or their representatives were present: David J. Lyons, Vice Chair (Iowa); John Garamendi (Calif.); Robert M. Willis (D.C.); James H. Brown (La.); Harold T. Duryee (Ohio); Georgia D. Flint (Texas); Harold C. Yancey (Utah); and Steven T. Foster (Va.).

1. Report of Buyer's Guide to Life Insurance for Seniors Drafting Group

Commissioner Mike Weaver (Ala.) began the meeting by calling on Commissioner David J. Lyons (Iowa) to give the report of the Buyer's Guide to Life Insurance For Seniors Drafting Group. Commissioner Lyons said that the working group had met on Sept. 20, 1992, to continue its work on the guide. Commissioner Lyons said that the working group had worked hard to prepare a draft of the buyer's guide which, while not perfect, was ready to be exposed at this meeting. He stated that it was his hope that the draft could be finalized before the December meeting in Atlanta.

Commissioner Lyons stated that there were three individuals who wanted to comment on the guide: Lee Norrgard (American Association of Retired Persons); Mary Griffin (Consumers Union); and Ed Zimmerman (American Council of Life Insurance).

Mr. Norrgard stated that the current version of the guide was an improvement over previous drafts in that it was shortened and targeted to explaining the Financial Review of This Policy disclosure form. He said that the guide used two examples; one with positive values and one with negative values, to explain how to use the disclosure form. He felt that the draft was a product of compromise and he concurred with Commissioner Lyons' recommendation to expose the draft. He noted that there were several minor technical errors which would need to be corrected during the exposure period.

Mr. Norrgard indicated that the group was of the opinion that the guide would be most useful if it was used on a stand-alone basis and not made a part of the current buyer's guide.

Mr. Norrgard said that one outstanding important issue was the appropriate time for delivery of the guide. He felt that to be of value to the consumer, the guide should be required to be provided at the point of solicitation. He stated that both the amount of coverage being sold and the senior population are increasing. He was of the opinion that seniors are a vulnerable population of consumers; that they are often more trusting and less knowledgeable than other consumers. Mr. Norrgard felt that if the guide was not provided at the time of solicitation, it may not be considered at all.

Commissioner Steven T. Foster (Va.) said that the committee had previously considered the timing issue in connection with the delivery of the disclosure form. He said that even though the committee had decided to require delivery of the disclosure form with the policy, he concurred with Mr. Norrgard and felt that delivery of the guide with the policy was too late. Commissioner Lyons noted that the guide was drafted in a manner that would allow a state to require an earlier point of delivery if it so desired.

Mary Griffin (Consumers Union) stated her support for Mr. Norrgard's position with respect to the timing issue. She noted that delivery of the guide at point of solicitation was one of the recommendations she and Bonnie Burns (California HICAP Association) had made in their June 5, 1992, letter to Commissioner Bill McCartney (Neb.) as president of the NAIC (Attachment Four-A). Ms. Griffin also recommended encouraging states to adopt the Financial Review of This Policy disclosure form contained in the Life Insurance Disclosure Model Regulation and she also recommended that minimum standards for these types of policies be developed. Commissioner Lyons noted that development of parameters was not a current charge of the committee.

Ed Zimmerman (American Council of Life Insurance) stated that these issues had been before the A Committee for about three years and that the model disclosure regulation had been amended to: (1) provide for the Financial Review of This Policy form; (2) extend the free-look period for policies subject to the disclosure form to 30 days; and (3) provide for an advance notice regarding the disclosure form. Mr. Zimmerman felt that with the development of the guide, substantial protections had been

afforded senior consumers and that the charge had been completed. He reiterated that from the industry's perspective, providing the guide at any time other than at the time the policy is issued was neither possible nor practical.

Commissioner Foster indicated that the regulators have a responsibility to react to concerns and complaints that are received and that there is an obligation to ensure the consumers have the right information at the right time.

Mr. Zimmerman responded by noting that the industry is supportive of disclosure and that if the committee re-examined the timing issue that industry representatives would be interested in participating in such a discussion to further explain their support for requiring the guide to be delivered with the policy and disclosure form.

Upon motion duly made and seconded, the minutes of the Buyer's Guide to Life Insurance for Seniors Drafting Group, including the recommendation to expose the Guide to Buying Life Insurance After Age 60, were adopted (Attachment Four-B).

Commissioner Lyons then offered a motion under the terms of which the Life Insurance (A) Committee would go on record, through a letter to the Executive Committee members with a copy to all NAIC members, noting that most members have not acted to adopt the disclosure form and encouraging such adoption. He asked that Ms. Griffin's letter be attached to the letter. This motion was seconded and unanimously adopted.

2. Report of Insurable Interest Working Group

Commissioner Weaver then called upon Commissioner Harold C. Yancey (Utah) to give the report of the Insurable Interest Working Group.

Commissioner Yancey noted that the working group had met on Sept. 20, 1992. Commissioner Yancey noted that the working group (1) adopted Guidelines on Gifts of Life Insurance to Charitable Institutions, (2) exposed Guidelines on Corporate Owned Life Insurance, and (3) reviewed a working draft of a model law for the regulation of living benefits.

Commissioner Foster asked what the intent was behind the development of guidelines. Commissioner Yancey indicated that they were intended to be educational in nature and could be used by insurance departments in responding to inquiries and in developing laws or regulations on the matters in question. Commissioner Foster noted that there were legislative proposals pending in a number of states relating to the issues addressed in the guidelines.

Upon motion duly made and seconded, the minutes from the Insurable Interest Working Group of Sept. 20, 1992, including final adoption of Guidelines on Gifts of Life Insurance to Charitable Institutions, were adopted (Attachment Four-C).

3. Report of Life and Health (Technical) Actuarial Task Force

Commissioner Weaver then called upon Sheldon Summers (Calif.) to present the report of the task force. Mr. Summers stated that the report contained the following recommendations.

1. Recommend adoption of proposed changes to the Actuarial Opinion and Memorandum Regulation to accommodate the change to the Asset Valuation Reserve (AVR) and Interest Maintenance Reserve (IMR) and to clarify other areas.
2. Recommend adoption in principle of changes to the Actuarial Opinion and Memorandum Regulation to facilitate reconciliation with standards established by the Actuarial Standards Board.
3. Recommend adoption of proposed actuarial guideline "Guideline Concerning Reserves of Companies in Rehabilitation" as amended Sept. 7, 1992, to define reserves for life insurance contracts and annuity contracts which have been modified by a court having jurisdiction.
4. Recommend adoption of proposed actuarial guideline "Guideline AAA - Guideline for the Application of Plan Type to Guaranteed Interest Contracts (GICs) with Benefit Responsive Payment Provisions used to fund Employee Benefit Plans" to clarify the method for determining the proper plan type for certain guaranteed interest contracts.
5. Recommend adoption of proposed "Actuarial Guideline DDD - Valuation Issues vs. Policy Form Approval" to clarify that establishment and/or acceptance of a method for computing minimum reserves for a type of benefit should not be construed to mean that a state is required to approve a form containing that kind of benefit.

Upon motion duly made and seconded, the recommendations were adopted.

4. Any Other Matters Brought Before the Committee

Commissioner Foster stated that he received a letter from U.S. Senator Howard M. Metzenbaum, Chairman, Subcommittee on Antitrust, Monopolies and Business Rights Committee, Committee on the Judiciary, United States Senate on the adequacy of information disclosed or available to consumers of life insurance (Attachment Four-D). Commissioner Foster recommended the establishment of a working group to fully review the concerns expressed in the letter and to recommend appropriate regulatory responses. Commissioner Weaver indicated that he would chair such a group and that the group's first meeting would be at the interim meeting scheduled to be in November in Boston. He encouraged those interested in participating to contact him or the NAIC staff.

Robert Corn (NAIC) noted that the Life Insurance (A) Committee had received a request from the NAIC Long-Term Care Insurance Task Force to review a proposed amendment to the Long-Term Care Insurance Model Regulation (Attachment Four-E). Prior to adopting the life insurance component of the disclosure amendment, the Long-Term Care Insurance Task Force wanted to give the Life Insurance (A) Committee an opportunity to review and comment on the proposal.

The chair took the request under advisement and asked the NAIC staff to coordinate the committee's response.

Having no further business, the Life Insurance (A) Committee adjourned at 3:55 p.m.

ATTACHMENT FOUR-A

Consumers Letter Regarding Limited Benefit Life Insurance Policies

June 5, 1992

Commissioner William McCartney, President
National Association of Insurance Commissioners
Department of Insurance
State of Nebraska
Terminal Building
941 O Street, Suite 400
Lincoln, NE 68508

Dear Commissioner McCartney:

We are writing this letter as representatives of consumers of insurance. We request that NAIC's Executive Committee address an important issue—the regulation of limited benefit life insurance policies.

While there may be reasons to buy life insurance after age 65, generally it is not a good value. Nonetheless, the sale of life insurance to persons over 55 has doubled in the last 10 years.¹ While hard data is scarce, it is safe to say most of these policies are low value life with face amounts of \$25,000 or less. Many are used to prepay funerals.

The older population is daily bombarded with television ads, door-to-door sales, telemarketing and direct mail solicitations for these low value policies. To be sure, consumers can find life products that have value even after age 65. Many if not the majority of low value life products, however, "go negative" after the second or third year. That is, the premium(s) exceed the benefits.

As you may know, Commissioner Marquardt of Washington implemented a regulation prohibiting the sale of life policies to people over the age of 62 when premiums exceed benefits in the first ten policy years. This regulation was challenged but the state supreme court upheld it in a unanimous decision.

NAIC Response

The NAIC Life Insurance Committee began almost three years ago to formulate a response to this important issue. A Senior Marketing Working Group and an advisory committee were created. For almost a year, the debate focused on whether or not the NAIC model regulation should contain language similar to the Washington state regulation.

Even though it never fully rejected the concept of minimum value, the working group recommended a disclosure regulation. Specifically, a disclosure form, entitled "Financial Review of This Policy," was added to the Life Insurance Model Regulation. This form charts how a low value policy sold to someone age 60 or older performs over time.

In 1991 the Senior Marketing Working Group addressed the issue of the timing of this disclosure. Should it be a point-of-sale or point-of-issue? Industry members of the advisory committee opposed disclosure at point-of-sale, arguing that providing accurate information at that point would be virtually impossible. Instead, the industry proposed, the purchaser would be notified that the "Financial Review of This Policy" form was coming with the policy. Further, the free-look period would be extended to 30 days.

The consumer members of the advisory committee argued that the point-of-sale is the time when the information is most needed.

The regulators voted to adopt the industry position with the understanding that further study of parameters would take place. An informal group of regulators was formed to address the issue and at least one regulator wrote a letter discussing the issue, providing suggestions for reform. It was the understanding of the consumer members that the working group was going to ask the life committee to determine if it was in the realm of the NAIC's authority to study the issue of parameters with the goal of developing a set of minimum values for these products.

¹American Council of Life Insurance, *1991 Life Insurance Fact Book*. In 1980, life insurance sales to people 55 and older were 5% of the market. In 1990, they were 10%.

Further, Commissioner David Lyons suggested that it would be valuable to provide consumers with a "buyer's guide" to life products. This would be similar to the NAIC's long-term care and medigap guides.

This year, a Senior Marketing Working Group was not reestablished. Instead, a Buyer's Guide to Life Insurance for Seniors Drafting Group was established to review a draft written by an American Association of Retired Persons (AARP) staff person.

Consumer Protection in the Marketplace

We are currently at a juncture where it is important for the Executive Committee to review this issue. This is for a number of reasons:

- The growth of these products is on an upward curve. It tracks the aging of our population, but marketing is pervasive.
- The only state that has taken any steps to improve these policies is Washington state. It is our understanding that, to date, not one state has adopted the disclosure form recommended by the NAIC.
- The reason for drafting a buyer's guide is to discuss the Financial Review Form as well as general issues about life insurance. Without anyone using the disclosure form the guide is hollow.
- Finally, the issue of parameters has apparently disappeared from the agenda.

Actions Requested of the NAIC

We request that the Executive Committee consider taking the following actions to address this issue:

- Encourage states to adopt, at a minimum, the disclosure form provided in the Life Insurance Disclosure Model Regulation.
- Encourage states to adopt a requirement that the buyer's guide be provided at time of sale.
- Direct the development of minimum standards to ensure that insurance departments approve only those products that are of value through a parameter or formula approach.

Thank you for your time and consideration of this request.

Sincerely,

Mary Griffin, Insurance Counsel
Consumers Union, Washington Office

Bonnie Burns, California Consumer Advocate

ATTACHMENT FOUR-B

Life Insurance (A) Committee
Buyer's Guide for Life Insurance for Seniors Drafting Group
Cincinnati, Ohio
September 20, 1992

Commissioner David Lyons (Iowa) began the meeting by noting that the purpose of the meeting was to receive and finalize the most recent version of The Senior's Guide to Buying Life Insurance After Age 60. He noted that the members had been provided with the draft dated Sept. 17, 1992, which Lee Norrgard (American Association of Retired Persons), chair of the drafting group, had prepared with the other drafting group members. He indicated that it was his hope that the drafting group could finalize the draft which would then be recommended for exposure by the Life Insurance (A) Committee. He said his intent was for the A Committee to expose the draft at this meeting with a view toward adoption prior to the Atlanta meeting in December. The A Committee's adoption prior to Atlanta would facilitate final adoption of the guide at the Plenary Session in Atlanta.

Commissioner Lyons indicated that the current draft was the result of considerable effort on the part of the drafting group and that to the extent possible, the work today should be to clean up the draft for an exposure recommendation. He noted that there would be an opportunity to make additional modifications during the exposure period.

Bonnie Burns (California HICAP Association) expressed her opinion that the policies subject to the guide and disclosure form were of questionable value. Noel Morgan (Consumer Advocate, Ohio Department of Insurance) expressed his interest in having the guide be as clear and concise as possible.

The group then proceeded to review the draft on a page by page basis. The first change was to change the title to Guide to Life Insurance After Age 60 to differentiate this guide from the current buyer's guide. The group also decided to change the third person references on the first page to a first person basis.

Language was added to the second page to further emphasize that the decision making process of determining whether to buy or keep a policy is not complete upon receipt of the policy. Rather, as the guide explains, the revisions made to the model last year allow purchasers a 30-day period to review the policy to decide if the policy meets their needs.

A footnote was added to the second page under the second bullet to indicate that state law in some states does not allow limited benefits to be paid for accidental death.

Revisions were made to both examples of the Financial Review of this Policy disclosure form to: 1) highlight the check-off boxes at the top of the page, and 2) to show the premiums in column one on an annual, rather than, accumulated basis.

The reference to "look/see" period was changed to "free-look." A question was raised as to whether the guide could be used for younger ages. Commissioner Lyons said that the guide tracked the model disclosure regulation which applies only to certain policies issued to those 60 and above.

The group concurred with Mr. Morgan's suggestion to simplify and emphasize the Net Gain, Net Loss provision and to explain that the parenthesis, used in the chart, signifies a negative number. A question was raised as to whether the reference to numbers not being the only item to consider, should be included in a guide directed at explaining the significance of numbers contained in the disclosure form. Glenn Joppa (Union Fidelity Life) indicated that this language reflected the consensus of the drafting group and was included to indicate that there are other factors buyers take into consideration in purchasing life insurance, such as their age, state of health and desired method of obtaining coverage. He felt it provided needed balance to the guide and should be retained. Commissioner Lyons indicated that he was inclined to recommend removal of the provision but that further consideration of the provision could be made during the exposure period.

The second example was modified to remove the comparisons between the policy values of the second example and the policy values of the first example. It was felt that this would be more confusing than helpful since purchasers would not be using the guide to make such comparisons.

Mr. Norrgard indicated that it had been his intent to draft a guide which could be used at the time of solicitation. Mr. Joppa reiterated his feeling that such a requirement would be impossible and impractical. Commissioner Lyons indicated that the question of the appropriate point of delivery would be further considered by the full A Committee.

Having no further business, the Life Insurance (A) Committee adjourned at 9:30 a.m.

ATTACHMENT FOUR-C

Insurable Interest Working Group of the Life Insurance (A) Committee Cincinnati, Ohio September 20, 1992

The Insurable Interest Working Group of the Life Insurance (A) Committee met in Salon BC of the Omni Hotel in Cincinnati, Ohio, at 10 a.m. on Sept. 20, 1992. A quorum was present and Harold C. Yancey (Utah) chaired the meeting. The following working group members were present: Mike Weaver (Ala.); John Garamendi (Calif.); and Steven T. Foster (Va.).

Commissioner Harold Yancey (Utah) stated that the minutes from the July 7, 1992, conference call had been distributed. Upon motion duly made and seconded, the minutes were adopted (Attachment Four-C3).

Commissioner Yancey stated that the next item of business was to consider adoption of the Guidelines of Gifts of Life Insurance to Charitable Institutions. It was noted that there had been a comment received from Diana Marchesi (Transamerica Life Companies) suggesting additional language relative to the need for donors to consider the long-term viability of the intended recipients of their gifts. Upon motion duly made and seconded, Ms. Marchesi's suggested language was included as a second paragraph in the guideline under the section entitled "What other considerations are involved?"

Upon motion duly made and seconded, the Guidelines were approved as amended (Attachment Four-C1).

The discussion then turned to the proposed Guidelines on Corporate Owned Life Insurance. Commissioner Yancey asked for an explanation as to the rights of terminating employees under corporate owned life insurance. George Coleman (Prudential) explained that a terminating employee would have conversion rights with respect to any group life insurance maintained by an employer, but that he would not have any such rights with respect to the type of corporate owned life insurance (COLI) contemplated by the Guidelines. He explained that this type of coverage is owned by the employer and stays with the employer for the benefit of other current and retired employees. He noted that COLI was used primarily as a means of financing the costs of providing retiree health benefits and was largely tax driven. He stated that the coverage is typically provided through an Internal Revenue Code Section 501(C)(9) (VEBA) Trust and that there are contractual and fiduciary responsibilities associated with administering the plan.

It was noted that the advisory committee had recommended certain changes with respect to the staff draft dated 6/4/92. Upon motion duly made and seconded and unanimously approved, both the NAIC staff draft dated June 4, 1992, and the advisory committee draft dated Sept. 7, 1992, were exposed.

Commissioner Yancey asked the NAIC staff to arrange a conference call prior to Atlanta to further discuss the two exposure drafts.

He then noted that a draft of a model law for the regulation of living benefit companies had been distributed (Attachment Four-C2). Mr. Coleman noted that he had reviewed the draft briefly and had noted several items that he felt needed further consideration. He indicated that he would submit his comments in writing. Susan Rodetis, an independent journalist, indicated that due consideration needs to be given to the time value of money and the discount rate used in these transactions. She cautioned, however, not to establish a regulatory framework that could be construed as a restraint of trade and unduly hinder a policyowner's property rights in his policies. Commissioner Yancey directed NAIC staff to route all comments received regarding the discussion draft to the members of the working group. He also asked that a conference call be arranged for further discussion prior to the Atlanta meeting.

Having no further business, the Insurable Interest Working Group of the Life Insurance (A) Committee adjourned at 11:30 a.m.

ATTACHMENT FOUR-C1

GUIDELINES ON GIFTS OF LIFE INSURANCE TO CHARITABLE INSTITUTIONS

Adopted by the Life Insurance (A) Committee
Draft: 9/20/92

These Guidelines have been prepared for use by state insurance department personnel who may be presented with questions or concerns regarding charitable gifts of life insurance. Of course, each state's laws on the issues discussed may differ, and the following discussion should be read with that in mind.

Q. What is meant by a gift of life insurance?

A. As a general principle, the gift of a life insurance policy to any recipient, whether such recipient is a charity or other third party, involves the same considerations and characteristics as a gift of any other property owned by the donor. Once the transaction is made, the ownership of the policy and all ownership rights under the policy, including the ability to change the beneficiary, are forever transferred from the donor to the recipient.

Q. What is meant by "charitable institutions?"

A. Charitable institutions are typically non-profit, tax-exempt organizations such as corporations or foundations organized and operated exclusively for religious, charitable, scientific, literary or educational purposes or to foster amateur sports or for the prevention of cruelty to children or animals.

Q. How is a gift of life insurance to a charity accomplished?

A. A gift of life insurance to a charity is generally accomplished in one of two ways, although there are varying alternatives within these two categories. The gift may be either of an existing policy, in the form of an irrevocable assignment to the charity, or it may be the purchase of a new policy by the insured, or with the consent of the insured, by the charity on the life of the insured, to the benefit of the charity.

Q. Why has there been increased interest and attention focused on gifts of life insurance to charitable institutions?

A. This stems primarily from a private letter ruling issued by the Internal Revenue Service dated Dec. 6, 1990, which indicated that federal income, gift and estate tax charitable deductions may not be allowed for gifts of life insurance to charities if the law in the donor's state did not recognize that charities have an insurable interest in the life of their donors. The ruling was based on the IRS's interpretation of New York law. Following an amendment made to New York law which specifically authorized insureds to transfer life insurance policies to charities, the IRS issued another letter ruling on Nov. 27, 1991, revoking its earlier ruling. As a result of the revocation, much of the concern over charitable giving of life insurance has subsided.

Q. What is insurable interest?

A. Insurable interest can generally be described as an interest on the part of the applicant or owner of the policy in the continuance of the life of the insured. Everyone has an insurable interest in his or her own life and where the applicant is the insured, he or she can generally make the proceeds payable to whomever he or she wants, including a favorite charity. Where someone other than the insured is the applicant, insurable interest is typically based on a family relationship or a reasonable expectation of deriving financial or economic benefits from the continuance of the insured's life. Some states require

beneficiaries to have an insurable interest in the insured. For life insurance to be enforceable, an insurable interest must exist at the time the policy is being applied for.

Q. How is the insurable interest requirement met in the context of gifts of life insurance to charitable institutions?

A. The statutory definition of insurable interest in many states specifically includes charities. In other states, charities who have an ongoing relationship with a donor may qualify under the general definition of insurable interest by demonstrating an expectation of benefit or advantage from the continuance of the life of the insured as a result of the insured's previous donation patterns, whether they be of money, other gifts or volunteer time. Other state statutes simply authorize charities to own or purchase life insurance on an insured who consents to the ownership or purchase of the insurance. The primary protection against abuse in the charitable ownership of life insurance is the requirement that the insured consent to the ownership. Many state laws require that consent to be in writing.

Q. What other considerations are involved?

A. There are various considerations which may help the donor determine the method he or she should use to make a gift of life insurance to a charity. Among these is whether the assignment of an existing policy would exclude from the donor's estate insurance coverage needed for more immediate family or business needs. The donor's state of health and ability to obtain other coverage should also be considered. The type of coverage in force and/or being considered for purchase may also be of significance. In that the donation may be made as part of a donor's estate or tax plan or have varying tax ramifications depending on how the transaction is structured, the donor should seek the advice of a tax expert in connection with any transaction of this nature.

The prospective donor may well find it entirely appropriate to ascertain the longevity of the charitable institution to which he or she is considering making a donation. The length of time which the charity has been in existence and its avowed goals regarding its own future activities could be significant in determining whether or not the charity will still be a viable institution when the life insurance benefit is paid.

Q. If a state contemplates statutory or regulatory language to clarify the existence of an insurable interest in charitable organizations, what are the main items that should be considered for inclusion in the statute or rule?

- A.** 1. Its purpose should be to acknowledge the existence of the insurable interest in the charity and to clarify how the law applies to charitable interest in life insurance and annuities;
2. It should clearly state that it does not abridge or limit the insurable interest currently existing in common law or by statute;
3. It should make clear that any specific requirements for an insurable interest to exist (e.g., written consent of the insured) are to be applicable only to insurance applied for and assignments made subsequent to enactment or promulgation of the law or rule; and
4. It should define "nonprofit organization" to include charitable, religious, scientific, literary, educational or other legitimate institutions or entities, reasonably anticipated to be the genuine object of a donor's charitable intent. (This would include institutions or entities described in the Internal Revenue Code Sections 170, 501, 2055 and 2522).

Q. What are some examples of statutory language states have used to respond to concerns over charitable ownership of life insurance?

A. Two examples of statutory responses to such concerns are Colorado House Bill 1031 enacted in 1992 adding Section 114 to Article 7 of Title 10, Colorado Revised Statutes, and Tennessee Senate Bill No. 2336, also enacted in 1992 adding Section ___ to Title 56, Chapter 7, Part 3 of the Tennessee Code Annotated.

The Colorado Law provides:

Notwithstanding any other provision of law, any organization that meets the requirements of Section 170(c) of the Federal "Internal Revenue Code of 1986," as amended, may own or purchase life insurance of an insured who gives written consent to the ownership or purchase of that insurance. The provisions of this section do not limit or abridge any insurable interest or right to insure now existing at common law or by statute, shall be construed liberally to sustain the existence of an insurable interest, and shall stand as a declaration of existing law applicable to all life insurance policies whenever issued, in existence on or after the effective date of this section.

The Tennessee Law provides:

If an organization described in either Section 501(c)(3) or Section 170(c) of the Internal Revenue Code of 1986, as amended, purchases or receives by assignment, before, on or after the effective date of this section, life insurance on an insured who consents to the purchase or assignment, the organization is deemed to have had an insurable interest in the insured person's life on the date of purchase or assignment. This section does not limit or abridge any insurable interest now existing at common law or by statute.

Citations to statutory provisions of other states dealing with charitable ownership of life insurance may be obtained by contacting the NAIC Legal Department.

ATTACHMENT FOUR-C2

Living Benefits Model Act Discussion Draft: 7/31/92, corrected 9/29/92

Table of Contents

Section 1.	Short Title
Section 2.	Definitions
Section 3.	License Requirements
Section 4.	License Revocation
Section 5.	Approval of Living Benefits Contract
Section 6.	Reporting Requirements
Section 7.	Examination
Section 8.	Disclosure
Section 9.	General Rules
Section 10.	Authority to Promulgate Standards
Section 11.	Effective Date

Section 1. Short Title

This Act may be cited as the Living Benefits Act.

Section 2. Definitions

A. "Living benefits provider" means an individual, partnership, corporation or other entity that enters into an agreement with a person owning a life insurance policy insuring the life of a person who has a catastrophic or life threatening illness or condition, under the terms of which the living benefits provider pays compensation or anything of value, which compensation or value is less than the expected death benefit of the insurance policy, in return for the policyowner's assignment, transfer, sale, devise or bequest of the death benefit or ownership of the insurance policy to the living benefits provider. Living benefits provider does not include:

- (1) Any bank, savings bank, savings and loan association, credit union or other licensed lending institution which takes an assignment of a life insurance policy as collateral for a loan; or
- (2) The issuer of a life insurance policy which makes a policy loan, permits surrender of the policy or pays other policy benefits, including accelerated benefits, in accordance with the terms of the policy.

B. "Living benefits contract" means a written agreement entered into between a living benefits provider and a person owning a life insurance policy insuring the life of a person who has a catastrophic or life threatening illness or condition. The agreement shall establish the terms under which the living benefits provider will pay compensation or anything of value, which compensation or value is less than the expected death benefit of the insurance policy, in return for the policyowner's assignment, transfer, sale, devise or bequest of the death benefit or ownership of the insurance policy to the living benefits provider.

Section 3. License Requirements

A. No individual, partnership, corporation or other entity may act as a living benefits provider or enter into or solicit a living benefits contract without first having obtained a license from the Commissioner.

Drafting Note: Insert the title of the chief insurance regulatory official wherever the term "commissioner" appears.

B. Application for a living benefits provider license shall be made to the Commissioner by the applicant on a form prescribed by the Commissioner, and the application shall be accompanied by a fee of \$[insert amount].

C. Licenses may be renewed from year to year as of May 1 of each year upon payment of the annual renewal fee of \$[insert amount]. This fee shall be due on or before the first day of April for the succeeding year. Failure to pay the fee within the terms prescribed shall result in the automatic revocation of the license.

D. The applicant shall provide such information as the Commissioner may require on forms prepared by the Commissioner. The Commissioner shall have authority, at any time, to require the applicant to fully disclose the identity of all stockholders, partners, officers and employees, and the Commissioner may, in the exercise of discretion, refuse to issue a license in the name of any firm, partnership or corporation if not satisfied that any officer, employee, stockholder or partner thereof who may materially influence the applicant's conduct meets the standards of this Act.

E. A license issued to a partnership, corporation or other entity authorizes all members, officers and designated employees to act as living benefit providers under the license, and all those persons must be named in the application and any supplements to the application.

F. Upon the filing of an application and the payment of the license fee, the Commissioner shall make an investigation of each applicant and shall issue a license if he finds that the applicant:

- (1) Is competent and trustworthy and intends to act in good faith in the capacity involved by the license applied for;
- (2) Has a good business reputation and has had experience, training or education so as to be qualified in the business for which the license is applied for; and
- (3) If a corporation, is a corporation incorporated under the laws of this state or a foreign corporation authorized to transact business in this state.

G. The Commissioner shall not issue any license to any nonresident applicant, unless a written designation of an agent for service of process is filed and maintained with the Commissioner or the applicant has filed with the Commissioner, such applicant's written irrevocable consent that any action against the applicant may be commenced against the applicant by the service of process on the Commissioner of Insurance.

Section 4. License Revocation

A. The Commissioner shall have the right to suspend, revoke or refuse to renew the license of any living benefits provider if the Commissioner finds that:

- (1) There was any misrepresentation in the application for the license;
- (2) The holder of the license is otherwise shown to be untrustworthy or incompetent to act as a living benefits provider;
- (3) The licensee demonstrates a pattern of unreasonable payments to policyowners; or
- (4) The licensee has been convicted of a felony or any misdemeanor of which criminal fraud is an element; or
- (5) The licensee has violated any of the provision of this Act.

B. Before the Commissioner shall deny a license application or suspend, revoke or refuse to renew the license of a living benefits provider, the Commissioner shall conduct a hearing in accordance with [cite the state's administrative procedure act]. In lieu of revoking or suspending the license for any of the causes enumerated in this section, the Commissioner may, after the hearing, subject the licensee to a penalty of not more than \$[insert amount] for each violation, when the Commissioner finds that the public interest would not be harmed by the continued operation of the provider.

Section 5. Approval of Living Benefits Contract

No living benefits provider may use any living benefits contract in this state unless it has been filed with and approved by the Commissioner. Any living benefits contract form filed with the Commissioner shall be deemed approved if it has not been disapproved within sixty (60) days of the filing. The Commissioner shall disapprove a living benefits contract form if, in the Commissioner's discretion, the contract or provisions contained therein are contrary to the interests of the public, or otherwise misleading or unfair to the policyowner.

Section 6. Reporting Requirements

Each licensee shall file with the Commissioner on or before March 1 of each year an annual statement containing such information as the Commissioner by rule may prescribe.

Section 7. Examination

The Commissioner may, when the Commissioner deems it reasonably necessary to protect the interests of the public, examine the business and affairs of any licensee or applicant for a license. The Commissioner shall have the authority to order any licensee or applicant to produce any records, books, files or other information reasonably necessary to ascertain whether or not the licensee or applicant is acting or has acted in violation of the law or otherwise contrary to the interests of the public. The expenses incurred in conducting any examination shall be paid by the licensee or applicant.

Section 8. Disclosure

A living benefits provider shall disclose the following information no later than the date the living benefits contract is entered into:

- A. Possible alternatives to living benefits contracts for persons with catastrophic or life threatening illnesses, including, but not limited to, accelerated benefits offered by the issuer of the life insurance policy;
- B. Tax consequences that may result from entering into a living benefits contract;
- C. Consequences of interruption of assistance as provided by medical or public assistance programs; and
- D. The policyowner's right to rescind a living benefits contract within thirty (30) days of its execution as provided in Section 9C.

Section 9. General Rules

A. A living benefits provider entering into a living benefits contract with any person with a catastrophic or life threatening illness or condition shall first obtain:

- (1) A written statement from a licensed attending physician that the person is of sound mind and under no constraint or undue influence; and
- (2) A duly witnessed and authorized document in which the person consents to the living benefits contract, acknowledges the catastrophic or life threatening illness, represents that he or she has a full and complete understanding of the living benefits contract, that he or she has a full and complete understanding of the benefits of the life insurance policy, releases his or her medical records, and acknowledges that he or she has entered into the living benefits contract freely and voluntarily.

B. All medical information solicited or obtained by any licensee shall be subject to the applicable provision of state law relating to confidentiality of medical information.

C. All living benefit contracts entered into in this state shall contain an unconditional refund provision of at least thirty (30) days.

Section 10. Authority to Promulgate Standards

The Commissioner shall have the authority to:

- A. Promulgate regulations implementing this Act; and
- B. Establish standards for evaluating reasonableness of payments under living benefits contracts. This authority includes, but is not limited to, regulation of discount rates used to determine the amount paid in exchange for assignment, transfer, sale, devise or bequest of a benefit under a life insurance policy.

Section 11. Effective Date

This act shall take effect on [insert date]. No living benefits provider transacting business in this state may continue to do so after [insert date] unless it is in compliance with this Act.

ATTACHMENT FOUR-C3

Insurable Interest Working Group
of the Life Insurance (A) Committee
Teleconference
July 7, 1992

The Insurable Interest Working Group of the Life Insurance (A) Committee held a teleconference at 10:30 a.m. Central time on July 7, 1992. A quorum was present and Harold C. Yancey (Utah) chaired the meeting.

Commissioner Yancey indicated that the purpose of the call was to determine how or whether to proceed with respect to the development of a guideline regarding corporate and trust owned life insurance.

The group was of the opinion that the states could benefit from the work the group had done thus far and that there was merit in proceeding with the development of an educational guideline. There was also consensus that proposing recommended modifications to the group life insurance law would be beyond the scope of the charge given to the group. Therefore, the group decided that the guideline should primarily be concerned with an overview of the insurable interest aspects of corporate owned life insurance (COLI) and trust owned life insurance (TOLI).

It was noted that there was an NAIC staff draft of a guideline that was directed at the insurable interest aspects of COLI and TOLI and it was determined that this draft guideline, dated June 4, 1992, would be the starting point for development of a guideline.

Commissioner Yancey directed NAIC staff to provide each member of the working group and the chair of the advisory committee with a copy of the June 4, 1992, draft guideline and to ask for any comments regarding the draft to be submitted by Aug. 15, 1992. Commissioner Yancey indicated that the group should then be in a position to recommend exposure of a draft guideline at the September meeting in Cincinnati.

Having no further business, the Insurable Interest Working Group of the Life Insurance (A) Committee adjourned at 10:50 a.m.

ATTACHMENT FOUR-D

United States Senate
Committee On The Judiciary
Washington, D.C. 20510-6275

September 18, 1992

Director William McCartney, President
Commissioner Steven T. Foster, President-Elect
National Association of Insurance Commissioners
120 West 12th Street, Suite 1100
Kansas City, Missouri 64105

Re: Consumer Disclosure

Dear Director McCartney and Commissioner Foster:

As you know, the Subcommittee on Antitrust, Monopolies and Business Rights has held a series of oversight hearings on insurance industry practices and policies. On June 23, 1992, the Subcommittee held a hearing to explore the adequacy of information disclosed or available to consumers of life insurance. What we learned deeply concerns me. I am writing to urge the NAIC to take immediate action on these serious matters.

Our oversight work has made clear that life insurance companies do not provide certain fundamental facts that consumers need in order to make informed decisions. It is equally clear that state insurance regulations do not require that the companies provide that information. First, buyers of life insurance are not being provided essential pricing information that would allow them to understand fully the cost of the policy they are considering or to compare similar policies. Second, prospective buyers are being misled about the projected future values of the policies they are considering. Third, without clear, accurate knowledge about their policies' cost or value, policyholders are being easily convinced to cancel policies in which they have accumulated cash value in order to purchase new, less advantageous products. These problems are particularly apparent in whole life and other permanent and blended products, which offer inside build-up on so-called savings or investment portions of premiums.

In our oversight hearings the subcommittee evaluated policies of five major companies. We learned that prospective buyers of these policies are not given a clear and accurate breakdown of policy-related administrative charges and other expenses they are forced to pay. Let me give some examples.

A prospective policyholder cannot calculate what will be left for savings or have a realistic expectation of the growth of the savings or have a realistic expectation of the growth of the savings portion because there is no reliable accounting of how premiums will be allocated for administrative charges and death benefits. One type of expense that goes unmentioned is the size of agent commissions which are between 55% and 105% of the first few years' premiums. Another is that prospective policyholders cannot determine a policy's actual cash value at cancellation because surrender charges are not clearly indicated. Furthermore, excessive administrative charges and mortality expenses are often refunded to the policyholder as dividends or reflected as reductions of premium. But, if a policyholder does not know what those charges or expenses are, he or she has no means to detect misleading information about vanishing, reducing or level premiums.

Our oversight also shows that individual policies are being designed and manipulated by computer-generated sales illustrations to contemplate many scenarios which are not realistic. Prospective buyers do not understand that projections of non-guaranteed elements are unlikely. The subcommittee has received testimony that less than 10% of policies bought in the 1980s will perform as illustrated. One witness testified that 15 of the largest 20 insurance companies operating in his state of Illinois had reported to regulators that they could not sustain, for even two years, the projected interest rate assumptions they were using in their illustration.

Overwhelming numbers of life insurance buyers do not even understand which, if any, elements of their sales illustrations are guaranteed. For instance, as we demonstrated in our hearing, an Alexander Hamilton illustration did not make it clear that there was no guaranteed death benefit after 12 years.

Another witness testified about his family's dilemma which came out of a misleading sales illustration. He said that in 1984, his family purchased a \$3 million joint whole life policy on his parents from Crown Life of Canada, relying on an illustration which said that the policy would be fully paid within six years and would always have a face value of at least \$3 million. They were not advised that the policy performance was conditional on a continued high dividend rate. Although they believed they had complied with the agreement, they were dismayed to learn recently that unless they pay \$92,000 a year for the next four years and \$22,000 a year thereafter, the policy would decline in value and perhaps lapse altogether. Since our hearing, we have received hundreds of calls and letters from similarly affected consumers.

Last, our oversight indicates that many policyholders are being encouraged, often against their best short- and long-term interests, to replace existing policies without sufficient information with which to compare their current policy to the replacing policy. One hearing witness testified that fewer than one in 10 of the replacement policies sold in recent years was marketed with the intent of upgrading benefits to the policyholders. Agents and companies sell replacement policies and collect up-front commissions and administrative costs from the cash value in the original policies. Neither insurance companies nor selling agents demonstrate to buyers how many years a replacing policy must be kept before lost assets can be restored.

I am also concerned that buyers of life insurance have no way to learn how many of their premium dollars, allocated to administrative charges, are being spent on salaries, benefits and retirement packages for the companies' top executives. Forty-nine states do not require companies to file compensation information with the regulators. Mutual company shareholders have nowhere they can seek information from stock companies, who can inquire of the SEC, are only slightly better off in this respect. (sic)

I am alarmed by the paucity of meaningful information available to consumers. I urge you and the appropriate NAIC task forces to create and pass model regulations that would protect consumers by assuring they have the ability to make informed life insurance purchases. The subcommittee will continue to monitor and evaluate the adequacy of information available to consumers of insurance. It is imperative that state insurance commissioners actively regulate and supervise the information given to consumers.

We look forward to working with you in a mutually constructive manner.

Very sincerely yours,

Howard M. Metzenbaum, Chairman
Subcommittee on Antitrust,
Monopolies and Business Rights
Committee on the Judiciary
United States Senate

ATTACHMENT FOUR-E

TO: Hon. Mike Weaver, Chair of the Life Insurance (A) Committee
FROM: Carole Olson Gates, NAIC Director of Health Policy, Market Conduct & Consumer Affairs
DATE: September 14, 1992
RE: Amendment to the Long-Term Care Insurance Model Regulation Regarding Life Insurance Policies with Long-Term Care Riders

Attached is an amendment proposed by the NAIC Long-Term Care Insurance (B) Task Force, which the task force would like to forward to the Life Insurance (A) Committee for review and comment. In particular, the task force is interested in knowing whether the disclosure amendment as drafted is appropriate and workable for life insurance policies that contain long-term care riders.

The Long-Term Care Insurance (B) Task Force plans to adopt disclosures for all other products at this time, but will await the committee's comment on adopting the life insurance component of that disclosure piece. Attached is the amendment for the committee's review.

LONG-TERM CARE INSURANCE MODEL REGULATION

Premium disclosure

Revised Exposure Draft: September 21, 1992

Amend Section 22E, Number 9 of the model regulation by renumbering it Section 3 with the following changes. Renumber remaining sections of the regulation to reflect the insertion of this language.

9- Section 3. Terms Under Which the Policy [Certificate] May Be Continued in Force or Discontinued

~~(a)~~A. For long-term care health insurance policies or certificates describe one of the following permissible policy renewability provisions;

(1) Policies and certificates that are guaranteed renewable shall contain the following statement: RENEWABILITY: THIS POLICY [CERTIFICATE] IS GUARANTEED RENEWABLE. This means you have the right, subject to the terms of your policy, [certificate] to continue this policy as long as you pay your premiums on time. [Company Name] cannot change any of the terms of your policy on its own, except that, in the future, IT MAY INCREASE THE PREMIUM YOU PAY.

(2) Policies and certificates that are noncancelable shall contain the following statement: RENEWABILITY: THIS POLICY IS NONCANCELABLE. This means that you have the right, subject to the terms of your policy, to continue this policy as long as you pay your premiums on time. [Company Name] cannot change any of the terms of your policy on its own and cannot change the premium you currently pay. However, if your policy contains an inflation protection feature where you choose to increase your benefits, [Company Name] may increase your premium at that time for those additional benefits.

~~(b)~~B. For group coverage, specifically describe continuation/conversion provisions applicable to the certificate and group policy;

~~(c)~~C. Describe waiver of premium provisions or state that there are not such provisions;

~~(d)~~D. State whether or not the company has a right to change premium, and if such right exists, describe clearly and concisely each circumstance under which premium may change.}

(1) Life insurance policies or riders containing accelerated long-term care benefits that have flexible premiums shall contain the following statement: THIS POLICY HAS FLEXIBLE PREMIUMS. This means you have the right, subject to the terms of your policy, to continue this policy as long as you pay your premium on time. [Company Name] cannot change any of the terms of the policy on its own, except that, in the future, due to changes in mortality charges or interest rates [Company Name] may INCREASE THE PREMIUM YOU PAY to keep the policy in force.

(2) Life insurance policies or riders containing accelerated long-term care benefits, that have guaranteed level premiums shall contain the following statement: THIS POLICY HAS GUARANTEED LEVEL PREMIUMS. This means that you have the right, subject to the terms of your policy, to continue this policy as long as you pay your premiums on time. [Company Name] cannot change any of the terms of your policy on its own and cannot change the premium you currently pay. However, if your policy contains an inflation protection feature where you choose to increase your benefits, [Company Name] may increase your premium at that time for those additional benefits.

Amend Section 19A of the regulation by adding a new Paragraph (7) to read:

(7) For long-term care health insurance policies and certificates, use the terms "noncancelable" or "level premium" only when the policy or certificate conforms to Section 6A(3) of this regulation.