

LIFE INSURANCE (A) COMMITTEE

Reference:

1993 Proc. 4th Qtr. 642
1994 Proc. 1st Qtr. 352

David J. Lyons, Chair—Iowa
Robert M. Willis, Vice Chair—D.C.

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MINUTES

The Life Insurance (A) Committee met in Maryland B of the Stouffer Harborplace Hotel in Baltimore, Md., at 11 a.m. on June 15, 1994. A quorum was present and David J. Lyons (Iowa) chaired the meeting. The following committee members or their representatives were present: Robert M. Willis, Vice Chair (D.C.); James H. Dill (Ala.); Dwight K. Bartlett, III (Md.); Harold T. Duryee (Ohio); Kerry Barnett (Ore.); J. Robert Hunter (Texas); Steven T. Foster (Va.); and Deborah Senn (Wash.).

1. Report of the Life Disclosure Working Group

Bob Wright (Va.) said the working group met twice in Baltimore and circulated drafts of the Life Insurance Illustrations Model Act and the Rules Governing the Use of Illustrations. He said these drafts permit illustrations of guarantees only into the future as well as illustrations of past performance. He said the working group did not intend to expose the drafts until September, and he asked for further comments by July 20. Mr. Wright also said that the working group would request approval from the Life Insurance (A) Committee to look at future projections possibly to develop a second draft.

Commissioner Robert Willis (D.C.) commended the group for its work product, which he said demonstrated substantial progress. He said the framework is now set to take on more thought-provoking issues. He applauded the working group for looking at the issue from the viewpoint of the consumer. He said the sales illustration should not be thought of as a sales tool, but a consumer information tool.

Commissioner David Lyons (Iowa) said the A Committee understands that the concept of providing information for consumers must be balanced with the need to prevent abuses. Upon motion duly made and seconded, the report of the Life Disclosure Working Group was received (Attachment One). The Life Disclosure Working Group was given the additional charge of considering options that would authorize non-guaranteed elements to be projected into the future. Commissioner Lyons said it would be up to Mr. Wright to decide whether an interim meeting is necessary before exposing the drafts in September, but he asked Mr. Wright to seriously consider this option.

2. Industry Response on Accelerated Death Benefits

Julie Spiezio (American Council of Life Insurance—ACLI) presented the response of the insurance industry to a request from the Life Insurance (A) Committee to study availability of accelerated benefits. Ms. Spiezio said the ACLI recommended the following actions by the NAIC: (1) the NAIC can encourage uniform adoption of accelerated benefits regulations in the states. Ms. Spiezio said only 10 states had adopted the NAIC's Accelerated Benefits Model Regulation, and she said this really hampered companies getting into the market; (2) the NAIC can encourage states to develop a streamlined approval process. She said in some states it took 12-24 months to get approval for accelerated benefits provisions; (3) she asked the NAIC to officially support a resolution of federal tax issues. In addition, Ms. Spiezio said that insurers opposed a mandate of accelerated benefits. Because providing accelerated benefits is not a cost-free move, the ACLI believed that it was up to the individual company to decide whether to provide accelerated benefits.

Ms. Spiezio presented to the group the preliminary results of a study done by the ACLI and the Life Insurance Marketing Research Association (LIMRA) (Attachment Two). She said the study showed that companies offering accelerated benefits represent approximately 75% of the life insurance in force in the United States, a 16-fold increase in persons covered since 1991.

Upon motion duly made and seconded, the Life Insurance (A) Committee voted to authorize the chair to contact all members urging adoption of the Accelerated Benefits Model Regulation, to encourage streamlined approval procedures, and to urge the NAIC to speak on behalf of a revised federal law.

Commissioner Lyons said he had recently received information that insurance companies are starting viatical settlement companies or buying viatical companies. He said he found it extremely disconcerting that an insurer would be acting in that fashion. He asked Ms. Spiezio to comment on the question: "Is it a prudent practice for insurers to be in the viatical settlement business?" He asked Ms. Spiezio if she saw any problem with a company selling insurance and then its viatical subsidiary buying insurance back. Ms. Spiezio said she was unaware of companies doing this and was unable to comment on the question. Commissioner Lyons said he would ask her for more formal feedback at the September meeting and offered to send her information to help in the response. He said this issue is technically beyond the charge of the Viatical Settlement Working Group, but at the September meeting the A Committee should consider a charge to pursue this issue.

3. Report of the Viatical Settlement Working Group

Roger Strauss (Iowa) said the NAIC had adopted a model act on viatical settlements in December 1993, and the working group now recommends adoption of the accompanying regulation and requested discharge of the working group because its task was fulfilled. Commissioner Lyons commended the working group members for their quick response and the good results that they had provided. He also noted that he had received some comments that the draft had been prepared by the insurance industry to benefit the insurance industry. He said nothing could be further from the truth. The draft had been prepared by NAIC members with consumers in mind. He said even though the NAIC's project was complete, support would be needed by consumers and the good players in the viatical settlement industry so that this law and regulation could be adopted in the states. He encouraged those who were in favor of this model to put that support in writing and to lend support when states introduced bills. Upon motion duly made and seconded, the report of the Viatical Settlement Working Group, including the Model Viatical Settlement Regulation, was adopted (Attachment Three).

4. Report of the Genetic Testing Working Group

Kip May (Ohio) reported that the working group had discussed the topic of genetic testing and would be working with a group of technical resource advisors. He requested comments in writing and oral presentations at the September National Meeting on the following topics: (1) use of genetic testing pros and cons; (2) parameters of genetic testing; (3) privacy issues; (4) technical advances—cost and quality of genetic testing; and (5) rating factors. He cautioned the group not to consider just life insurance issues or health insurance issues but to consider both. Mr. May said that after the hearing at the September meeting, the working group plans to consider the regulatory issues and formulate a position. Commissioner Lyons asked the working group to maintain close communication with the Accident and Health Insurance (B) Committee. Upon motion duly made and seconded, the report of the working group was received (Attachment Four).

5. Report of the Synthetic GIC Working Group

Reginald Berry (D.C.) said a two-hour meeting had been held with a panel discussion by members of the GIC/Stable Value Association. He said the panel included sellers and buyers of synthetic guaranteed interest contracts (GICs). The working group is continuing its efforts to expose the NAIC to information as to what synthetic GICs are and the regulatory effects. Upon motion duly made and seconded, the report of the Synthetic GIC Working Group was received (Attachment Five).

6. Report of the Life and Health Actuarial Task Force

John Montgomery (Calif.) reported on the two nonforfeiture laws that the Life Insurance (A) Committee had requested the task force to review further. He said progress is being made on the annuity model, and the life disclosure model was beginning to take shape. He said the Actuarial Task Force is not recommending exposure of a new draft of the Life Nonforfeiture Model because it is still working on the problem of fund-based products. Commissioner Dwight Bartlett (Md.) commented that the difficulties in the annuity model have to do with two-tier annuities. He said that most discussion was on the topic of whether there should be a limit on the differential between the two tiers. He saw this as a consumer protection issue.

Mr. Montgomery said the recommendations of the Life and Health Actuarial Task Force were that: (1) the June 6, 1994, draft of the Actuarial Guideline No. GGG, entitled "Determining Minimum CARVM Reserves for Individual Annuity Contracts" be exposed for comments; (2) the June 12, 1994, draft revisions of the NAIC Model Standard Nonforfeiture Law for Deferred Annuities be exposed for comments with the intention that a version of this draft would be recommended for adoption in September 1994; (3) Project No. 2m "Valuation—Need for a New Life Insurance Tables" be placed on hold in June 1994; (4) Project 2r "Valuation—Cost of Collection in Excessive Loading" be placed on hold in June 1994; and (5) potential Project 4dd "Special Plans—Separate Account Annuities" be added to the agenda of the Actuarial Task Force as a No. 2 priority project.

A motion was made and seconded to receive the Life and Health Actuarial (Technical) Task Force report. Mr. Berry said that while the majority of the task force agreed with this action, the minority (D.C.) opposed the motion. He said the A Committee had charged the Actuarial Task Force to test two-tier annuities. When the task force discussed the issue, it had concluded testing was not appropriate and he questioned whether the task force was completing its charge. He asked whether the charge was to decide whether or not to test or whether the charge was to test.

Mr. Berry made a substitute motion to receive the report with the exception of the exposure draft of the Standard Nonforfeiture Law on Deferred Annuities, which he requested be sent back to the Actuarial Task Force for testing. Commissioner Lyons said that as a non-actuary, he would give deference to the task force's recommendation to spend time on other issues before it. Bob Callahan (N.Y.) said the task force had discussed this issue for a number of years. It could not reach satisfaction with one particular company on the issue of two-tier annuities. He said Larry Gorski (Ill.) had done some testing and the task force had given this question a great deal of consideration. Barbara Lautzenheiser (Lautzenheiser & Associates) said she saw this as a form of rate regulation. She

thought it was the task force's responsibility to test the validity of the 10% limit that had been included. Commissioner Bartlett said the task force had agreed that it would meet before the next Life Insurance (A) Committee meeting to review any testing results presented to it.

The motion to receive the report except for the Standard Nonforfeiture Law for Deferred Annuities was defeated. The original motion to receive the report passed. Mr. Montgomery said that the joint A and B actuarial working group is recommending that the June 11, 1994, draft of proposed changes to the Actuarial Opinion and Memorandum Model Regulation be exposed for comments. Upon motion duly made and seconded, this report was received.

Having no further business, the Life Insurance (A) Committee adjourned at 12:30 p.m.

David J. Lyons, Chair, Iowa; Robert M. Willis, Vice Chair, D.C.; James H. Dill, Ala.; Dwight K. Bartlett, Md.; Harold T. Duryee, Ohio; Kerry Barnett, Ore.; J. Robert Hunter, Texas; Steven T. Foster, Va.; Deborah Senn, Wash.

ATTACHMENT ONE

Life Disclosure Working Group of the Life Insurance (A) Committee Baltimore, Maryland June 11 and 13, 1994

The Life Disclosure Working Group of the Life Insurance (A) Committee met in Maryland E of the Stouffer Harborplace Hotel in Baltimore, Md., at 11 a.m. on June 11, 1994. A quorum was present and Bob Wright (Va.) chaired the meeting. The following working group members or their representatives were present: Don Koch (Alaska); John Montgomery (Calif.); Roger Strauss (Iowa); Lester Dunlap (La.); Tony Higgins (N.C.); Noel Morgan (Ohio); Robert E. Wilcox (Utah); and Fred Nepple (Wis.).

1. Adopt Minutes of May 1-3, 1994, Meeting and June 3, 1994, Conference Call

Upon motion duly made and seconded, the minutes of the May 1-3, 1994 (Attachment One-E), meeting and the June 3, 1994 (Attachment One-D), conference call were adopted.

2. General Comments

Bob Wright (Va.) said that since the attendees did not receive copies of the drafts of the Life Insurance Illustrations Model Act and Regulation in time to review them before the meeting, he would ask for comments specifically on the drafts at the June 13 session. He asked if anyone had general comments to make at this meeting. He said it was the intention of the working group not to expose the drafts until September, so there would be time for further comments. He said another reason for postponing exposure until September was because there were some disclosure provisions in the Second Standard Nonforfeiture Law being developed by the Life and Health Actuarial (Technical) Task Force, and the working group wanted to be sure that the two models were consistent. Mr. Wright said the working group might develop two alternative models, one with guarantees only, and one with projections of non-guaranteed elements in an understandable format. Mr. Wright asked those who were interested in making suggestions to work through the technical resource advisors as much as possible, and he introduced George Coleman (Prudential), the chair of that group.

Ted Becker (Texas) distributed to the members of the working group a statement from Commissioner J. Robert Hunter (Texas) (Attachment One-A). Mr. Wright asked if there were any other regulators that wished to comment. Allan B. Roby Jr. (Conn.) said that his commissioner objected to adoption of any model that did not allow projection of non-guaranteed elements into the future. He said Commissioner Robert R. Googins (Conn.) did not consider that to be consumer oriented.

Next, Mr. Wright invited comments from others in attendance at the meeting. John Booth (American Council of Life Insurance—ACLI) said he was commenting on the May 1, 1994, draft of the life insurance illustration regulation, because that was all that was available before the meeting. He expressed concern on several issues:

1. **Use of Guarantees Only and Past Performance:** He said there were difficulties in reconstruction of past data and the numbers were not available at all if the policy had changed.
2. **Variable Life:** He urged the regulators not to make variable life policies subject to the regulation. He said there was already another model dealing with the subject and also variable life was subject to Securities and Exchange Commission (SEC) regulation.

3. **Group Pension Plans:** Mr. Booth asked the group to consider carefully whether the model should apply to group pension plans.
4. **Investment Products:** He said the May 1 draft made insurance look very much like an investment product.
5. **Company Ratings:** He applauded the decision of the working group as reflected in the minutes of the May 1-3, 1994, meeting to remove the concept of insurers' ratings from the draft.
6. **Cost:** Mr. Booth said it would be difficult and expensive to provide annually a statement that would compare actual results with guarantees as required under Section 10 of the draft regulation.
7. **Other NAIC Models:** The proposal being put forward by the Life Disclosure Working Group would be in direct conflict with other NAIC models.

Mr. Wright said that the past performance section was greatly changed from the earlier draft. He asked that Mr. Booth review the new draft and communicate with the committee as to whether the changes ameliorated any of his concerns.

Scott Cipinko (National Association of Life Companies—NALC) asked the working group to keep its focus on consumers. He said the resource group product and other suggestions included changed wording to improve understanding of consumers; for example, "not guaranteed" instead of "projected."

Donald Bertram (Phoenix Home Life) said that in the 1980s, insurers had failed to disclose all of the information consumers needed to know. Improvements in computers now allow that disclosure. He said that some standardization might be needed, but insurers needed flexibility to show a variety of products. Neil Chaffee (Phoenix Home Life) said his company had worked hard at developing an illustration that identified the guaranteed and non-guaranteed elements. His company's illustration also had been purged of "buzz words" that were not understandable to consumers.

Mr. Coleman spoke as chair of the technical resource advisors. He said he had submitted a comprehensive analysis of the May 1, 1994, draft regulation to the working group members. He said the advisors felt it was still flawed, but they made an honest attempt to address the issues in the draft. On June 1, 1994, he sent a letter to the working group outlining improvements in the resource advisors' proposal. He said there was significant improvement from the earlier presentation. Bill Koenig (Northwestern Mutual) said the second technical resource advisors' document was closer to the current regulators' draft of the regulation showing guarantees only. He said the technical advisors' draft eliminated "flights of fancy" and long strings of numbers. If information was available for that policy form, the draft used recent historical information to project into the future. There was an effort to tie numbers to actual company historical performance if numbers on a particular policy were not available. He said the advisors' draft used real company expense and mortality, with no projections of improvement in mortality, etc.

Andrew Ware (Northwestern Mutual Life) commented that he had reviewed several of the suggestions, including the working group draft, and compared them with the elements of the white paper the Life Disclosure Working Group had prepared last year. He said that there were defects in all of the drafts, including that of the working group. He suggested that it was important that the Actuarial Standards Board (ASB) write standards on such problems as new money versus portfolio income and margins—the spread between actual experience and what was illustrated. He said the ASB could go a long way to preventing abuse. He said lapse-supported products created the largest potential problem and suggested that illustrations of lapse-supported products not be permitted.

Commissioner David Lyons (Iowa) asked how long it would take for the ASB to develop standards to put in place. Gary Corbett (ASB) said that as soon as a draft that was reasonably close to what might be adopted was prepared, it would take approximately nine months to one year to have the standards prepared. He said the problem with portfolio versus new money would definitely be one of the issues that would be considered by the ASB. Commissioner Lyons asked Carolyn Johnson (NAIC/SSO) to research whether the NAIC had ever adopted a model that worked as an alternative. He suggested something that could be put in place if the ASB did not act or until the ASB had completed its product.

Michele Van Leer (John Hancock) said the newest suggestion prepared by the technical resource advisors put credibility in the numbers in an illustration. She said it was an attempt at a disciplined illustration of numbers; a movement from where the advisors' draft was before to understandable terminology and showing guarantees and non-guaranteed elements more clearly. She said she was not in favor of the NAIC developing two alternative models.

Hugh Alexander (Alexander & Associates) said he represented small companies that were worried about being able to show innovative new products. He said there was already financial testing available through the NAIC that could determine whether a company could support what it was illustrating. He said cash flow testing and asset and liability matching would be able to determine whether the company was illustrating something it could accomplish.

Commissioner Lyons said it was not his intention or the intention of the Life Insurance (A) Committee to do anything that interfered with innovation. He said if the Life Insurance (A) Committee could see that consumer-friendly illustrations were being developed, it would not want to stifle this activity. He did emphasize that until the last year, he had not seen much innovation in this area at all.

Mr. Wright said he was encouraged to see that some good proposals were starting to come forward. He said the proposals were not yet where the working group members wanted to be, but they were getting closer.

Having no further business, the Life Disclosure Working Group adjourned at noon.

The Life Disclosure Working Group of the Life Insurance (A) Committee reconvened in Maryland C of the Stouffer Harborplace Hotel in Baltimore, Md., at 11 a.m. on June 13, 1994. A quorum was present and Bob Wright (Va.) chaired the meeting. The following working group members or their representatives were present: Don Koch (Alaska); John Montgomery (Calif.); Roger Strauss (Iowa); Lester Dunlap (La.); Tony Higgins (N.C.); Noel Morgan (Ohio); Robert E. Wilcox (Utah); and Fred Nepple (Wis.).

3. Comments on Model Act

Mr. Wright (Va.) asked for comments on the specifics of the drafts before them rather than philosophical comments about life disclosure in general. First he asked if there were any comments on the model act draft (Attachment One-B). Mary Griffin (Consumers Union) asked about Section 2 and the phrase "misrepresenting the benefits of the life insurance policy." She said the commissioner might already have the authority under current law to deal with misrepresentations. Mr. Wright directed her to the drafting note after Section 3, which discussed commissioners' authority. No further comments were received on the model act, so Mr. Wright next asked for comments on the model regulation (Attachment One-C).

4. Comments on Model Regulation

Richard Minck (ACLI) said the ACLI had a task force meeting scheduled for the following week. He said at that time that group would prepare comments on the draft regulation. Mr. Wright then asked if there were any comments on specific sections of the draft.

a. Section 3—Applicability and Scope

Mr. Coleman said he did not think Section 3 dealt adequately with the issue of the sophisticated purchaser. Mr. Cipinko said he had a concern that the definition was too broadly written and might bring in some policies without real illustrations simply because they contained some kind of numbers. S. Reed Ashwill (National Association of Independent Life Brokerages Agencies—NAILBA) spoke on the variable life insurance exclusion. He said if the product was not variable and had a yield of zero, the insurer would show the guaranteed amount. If it was a variable product, where the guaranteed yield was zero, the illustration would show up to 12%. He wondered why non-variable products were limited to illustrating the guarantees only.

b. Section 4—Definitions

Mr. Coleman commented on the definition of illustration in Subsection C. He said the definition is broader than he would like to see, and said that the technical resource advisors would give this thought and make suggestions for refined language. He said Subsection D, the definition of "net increase," was not used consistently throughout the draft. Mr. Coleman also said that he did not think Subsection E, the definition of "past performance," was clear. He thought this section placed an extremely difficult burden on the insurers, so it was important that it be clear exactly what was required. Mr. Wright asked about a statement made earlier, that most companies did not have records of past performance. He asked how a company got information in case of a court case, complaints, etc. Mr. Koenig said in the examples Mr. Wright had provided, his company would pull up the records for each individual involved. The problem was reconstructing for all of the policies his company sold. Mr. Wright reiterated that the question was not whether the information was available, but rather if it was accessible. Mr. Koenig said that if he understood the current draft correctly, he has a conceptual problem with how to use the information from past years to apply to policies currently being sold. Linda Lanam (Life Insurance Company of Virginia) said she was responding to Mr. Wright's question from the perspective of a stock company. She said her company kept records for individuals, but to average the data for an entire policy form would mean that a number would be created which did not reflect any one individual's policy. William Fisher (Massachusetts Mutual) said most policies are issued smoker/nonsmoker. Fifteen years ago, this concept was not in use, and he wondered how that would be shown using past performance as indicated in the draft. Mr. Minck said there were also many other variables with the same problems. Ms. Griffin said in the definition of "illustration," the word "tabular" was not included in Subsection C, but was included in other parts of the draft and she thought that this might cause confusion. She also suggested that Subsection F, Qualified Actuary, should contain standards for the commissioner where it allowed a qualified actuary to be any other individual acceptable to the commissioner. Martin Carus (N.Y.) said he was interested in whether a product had a good performance or a bad performance. He asked if the companies weren't interested in demonstrating products that had done well. Mr. Koenig responded that agents for his company used information from *Best's Review* to illustrate how products had performed. He said this information was kept for a limited number of ages and plans, but it was not available for every age and every plan.

c. Section 5—Illustration Format Standards

Ms. Griffin commented on Subsection C(3). She asked the working group to consider a method to make sure there were no changes in the illustration that had been shown. She said her organization found in doing research for their life insurance report, that there were many instances where an agent showed an illustration and afterward made changes or deleted parts of it.

Mr. Cipinko said the term "rating classification" in Subsection C(1) was not a defined term. He asked what benefit there was in disclosing the rating classification. Mr. Wright responded that it would help the applicant determine if that was the rate that he would be likely to get. Tony Higgins (N.C.) also said that the terminology used for the rating classification

might give a wrong impression. For example, calling it "super preferred" might make the individual think he was getting a good buy, when in reality this was the classification of 95% of the people. Mr. Cipinko expressed the opinion that providing the rate classification might insult the prospect.

Mr. Coleman said that he thought this section needed some fleshing out to provide more information. He said that the cover page prepared by the technical resource advisors was a good way to provide a greater amount of information. Mr. Wright said he would agree, but the illustration cover sheet, which is Appendix A, was already pretty full.

d. Section 6—Certification by the Company; Disclosure

Mr. Corbett expressed concern about Section 6A(3). He said he was concerned that the actuary was being asked to certify to the entire illustration rather than to the numbers that were on the illustration. He suggested that the language be "prepared in a manner consistent with the standards" rather than "in compliance with the standards." He said the ASB would be developing standards for the numbers in the illustrations, rather than the illustrations themselves. John Montgomery (Calif.) agreed that this was an important distinction.

e. Section 7—Standards for Illustration

Mr. Wright asked if there were any comments on Section 7. The only comment received was that the provision in Section 7B(1)(a), referring to all policy forms was too broad. Mr. Minck suggested deleting (ii) and (iii) at the very end of Section 7. He said that these items did not take into account the insurance protection offered and thus were misleading.

f. Section 11—Actuarial Standards

Mr. Corbett said the illustration standards for past performance would be much different than those for current scale, and cautioned the working group not to assume too great a similarity between them.

Mr. Wright said the drafts which had been prepared by the working group would be circulated, but not exposed formally at this meeting. He asked interested parties to comment to Ms. Johnson by July 20. He said the working group would consider the comments and decide whether it was necessary to have an interim meeting before the fall National Meeting so that the draft would be ready for exposure.

Having no further business, the Life Disclosure Working Group adjourned at 12:10 p.m.

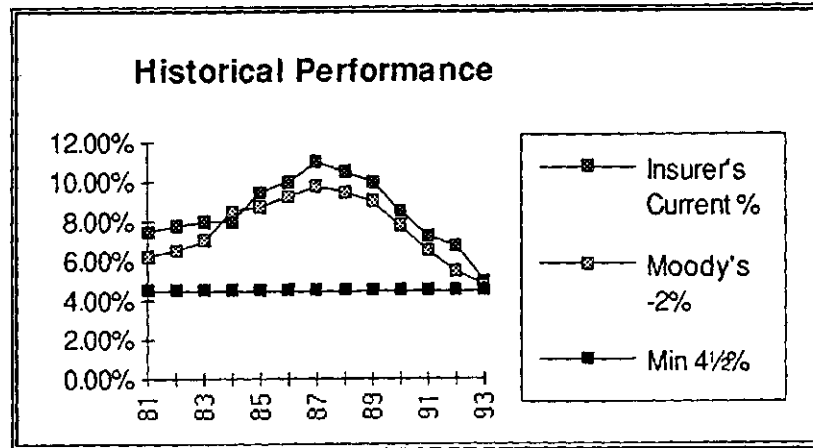
ATTACHMENT ONE-A

From: J. Robert Hunter, Commissioner of Insurance, Texas Department of Insurance
Re: Life Insurance Illustrations of Future Values

With all the discussion about misleading sales practices in the marketing of life insurance, we as regulators must take a position that does justice to the buying public. Ironically, all the columns, figures, pages, disclaimers, and disclosures do not tell consumers what they really want to know—*What does the insurance cost?* Below are my suggestions for what an illustration should tell a consumer. When their policy out-performs the illustration, policyholders will feel they got a good deal instead of feeling ripped-off!!!

- Illustrations of future values must reflect only policy guarantees.
- Any illustration of past performance must include an economic point of reference.*
- All expenses, costs, fees, mortality charges, profits, commissions and the amounts allocated to interest accrual should be itemized by year.
- Annual guaranteed cash values should be illustrated net of all surrender charges.
- An updated illustration should be provided to the policyholder annually.
- Any "enhancement" of figures through the use of persistency, mortality, expense, lapse and other improvements must be prohibited.
- Include a column with net interest realized on premiums paid.
- The total number of pages in a complete illustration should be indicated on each page, e.g., page 2 of 3.
- A standardized format with standardized definitions must be adopted.
- An illustration should include a readable description of the policy.
- An illustration must be printed in at least 10 point type.
- Any policy lapse must be explained and shown in bold print.
- The insurer and/or the agent must be held accountable for any sales illustration.

*A reasonable benchmark must be used as a comparison ("T" bills, S&P). Moody's Corporate Bond Yield Average may be considered. It is used to determine the obligation of the Texas Life, Accident, Health and Hospital Service Insurance Guaranty Association for excess interest payable on policies subject to their coverage, as set out in Article 21.28-D. Sec. 3. Texas Insurance Code.



ATTACHMENT ONE-B

LIFE INSURANCE ILLUSTRATIONS MODEL ACT

Draft: 5/18/94

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Section 3.	Authority to Promulgate Regulations
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Section 1. Applicability and Purpose

This Act shall apply to all life insurance companies and fraternal benefit societies licensed to do business in this state and to all [producers, agents and brokers] licensed to sell life insurance or annuities. The purpose of the Act is to authorize standards which shall be followed in the illustration of life insurance products.

Drafting Note: Insert the appropriate terminology consistent with state licensing laws.

Drafting Note: This section refers to both life insurance policies and annuity contracts. A separate regulation will be required for each.

Section 2. Prohibited Practices

No person engaged in the business of insurance shall misrepresent the benefits, advantages, conditions or terms of any life insurance policy or annuity contract.

Section 3. Authority to Promulgate Regulations

The commissioner shall promulgate regulations that establish standards to assure that illustrations of future benefits use only guaranteed assumptions.

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

Drafting Note: In a state where the commissioner already has this authority, adoption of the model act may not be necessary in order to promulgate the model regulation.

Section 4. Penalties

A violation of this Act by any person shall be subject to the penalties found in Section [insert penalty section of unfair trade practices law].

Section 5. Separability

If any provision of this Act or its application to any person or circumstance is for any reason held to be invalid, the remainder of the Act and the application of the provision to other persons or circumstances shall not be affected.

Section 6. Effective Date

This Act shall be effective [insert date].

ATTACHMENT ONE-C

RULES GOVERNING THE USE OF ILLUSTRATIONS
IN CONNECTION WITH THE SALE OF LIFE INSURANCE
Draft: 6/3/94

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Appendix A.	Cover Page Format
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Section 1. Purpose

The purpose of this regulation is to provide rules for life insurance policy illustrations based upon policy guarantees and past performance. The rules provide illustration formats, prescribe standards to be followed when illustrations are used, and require disclosures to be used in connection with illustrations. The goal of this rule is that illustrations accurately describe policies and be understandable by purchasers of life insurance without explanation by a producer or others possessing specialized insurance knowledge.

Section 2. Authority

This regulation is issued based upon the authority granted the Commissioner under [cite appropriate enabling legislation].

Section 3. Applicability and Scope

This regulation shall apply to all group and individual life insurance policies and certificates marketed with the aid of an illustration, except individual and group annuity contracts, variable life insurance as defined in [cite Article II, Section 19 of the NAIC Variable Life Insurance Model Regulation] and credit life insurance.

Section 4. Definitions

- A. "Guaranteed benefits" means those benefits which the insurer guarantees as provided in the policy contract.
- B. "Guaranteed cash value" means the minimum values guaranteed by the policy that will be available on surrender of the contract, assuming all required or illustrated premiums have been paid to the date of surrender.
- C. "Illustration" means any numerical or graphic description of the performance over time of policy values or benefits which is:
 - (1) Used by a producer or insurer to sell a policy; or
 - (2) Represented by the producer or insurer as describing the past or future performance of a policy.
- D. "Net increase" means the total amount of all increases in a policy's value (e. g., excess interest or dividend credits).

E. "Past performance" means a demonstration of amounts credited to a policy during each year that a policy form has been issued, including both guaranteed and non-guaranteed values.

F. "Qualified actuary" means a member in good standing of the American Academy of Actuaries or any other individual acceptable to the Commissioner.

Section 5. Illustration Format Standards

Regardless of the medium used in a sales presentation, any illustration must be incorporated into a written document in the following format:

A. Each page of an illustration, including any explanatory notes or pages, shall be numbered, showing its relationship to the total number of pages in the illustration (e.g., the fourth page of a seven-page illustration shall be labeled "page 4 of 7 pages").

B. The illustration shall be clearly labeled "Life Insurance Illustration," identify the insurer, the generic type of life insurance, the company product name, if different, and the policy form number.

C. The illustration shall have a cover page, numbered as page one, and containing the following:

(1) The rating classification upon which the illustration is based, a narrative explanation of this classification, and the percentage of insureds who are covered by this form and are included in this as well as a better rating classification. In calculating the percentage of insureds covered, the insurer should use actual experience or, in the absence of meaningful actual experience during the first year after issue of a new policy, reasonably anticipated experience.

(2) A statement to be signed and dated by the applicant as follows: "I have received a copy of this illustration of the life insurance policy for which I have applied."

(3) A statement to be signed and dated by the insurance producer as follows: "I certify that this illustration is appropriate for the life insurance policy applied for and that no representations have been made that are inconsistent with the illustration."

Section 6. Certification by the Company; Disclosure

A. At or prior to delivery of a life insurance policy, an insurer shall provide the applicant with a second copy of the illustration provided under Section 5, which is certified by the company as:

- (1) Appropriate for the rating classification of the applicant and the policy issued;
- (2) Accurately describing the guaranteed values and past performance of the policy; and
- (3) Prepared in compliance with the standards of the Actuarial Standards Board.

B. An officer of the insurer shall sign and date the certification required under Subsection A. The officer of the insurer may authorize the use of his facsimile signature.

C. An insurer may comply with Subsection A by substituting a different illustration than the illustration signed by the applicant under Section 5, but only if:

- (1) The substitution is necessary because the policy issued is other than that illustrated at the time of sale;
- (2) The substituted illustration complies with Section 5 and is signed and dated by the producer and the applicant as required by Section 5C; and
- (3) The substituted illustration includes on the cover page a clear and prominent disclosure that it is a revised illustration and that it should be carefully reviewed prior to acceptance of the policy.

Section 7. Standards for Illustrations

A. An illustration shall show guaranteed values, in a manner consistent with Appendix B, as follows:

- (1) Producer's name and address;
- (2) Insured's name;
- (3) Age and sex of insured;
- (4) Underwriting class;

(5) Columns as follows:

- (a) Policy years listed annually for years one to twenty (20) and five-year intervals beginning at age sixty (60) and ending at age 100, if applicable;
- (b) Premium for each year sufficient to produce an endowment at age 100 with totals at year ten (10) and year twenty (20) and age sixty-five (65);
- (c) Net cash surrender value for each year; and
- (d) Death benefit for each year.

B. Illustrations of past performance shall be utilized in connection with the sale of a policy subject to the requirements of this section.

(1) Illustrations of past performance shall be the results of the application of the individual assumptions actually used by the company to derive the nonguaranteed policy benefits for the prior periods being illustrated.

- (a) If the company used consistent assumptions for all policy forms, those assumptions may be applied to prepare an illustration of past performance to be used in connection with the sale of any current policy form. If the company is the result of a corporate merger and one predecessor company predominates, the merger alone will not be sufficient reason to construe that assumptions are not consistent.
- (b) If the company did not use assumptions that were consistent for all policy forms, an illustration of past performance must be based only on the assumptions used for the policy form being sold. The term policy form shall include all forms issued by the company that are identical with regard to all provisions that affect the illustration of past performance.
- (c) Application of these assumptions is limited to illustrating the actual periods when the assumptions were used.

(2) Illustrations of past performance are not to be utilized to illustrate future performance of the policy form being sold. Each illustration must contain the following in prominent form:

"This illustration of past performance shows the actual results achieved by the company for the periods shown. Future results may be better or worse than the results shown."

(3) Illustrations of past performance may be in tabular, graphic or narrative form or any combination of those forms.

(4) Each illustration of past performance shall contain the following information:

(a) Individual characteristics of the insured that affect results such as:

- (i) Gender;
- (ii) Smoker or non-smoker status;
- (iii) Issue age;
- (iv) Underwriting rating; or
- (v) Issue date;

(b) Policy definition characteristics such as:

- (i) Policy form description;
- (ii) Face amount;
- (iii) Premium amounts;
- (iv) Premium mode;
- (v) Ancillary benefits;
- (vi) Dividend option; or
- (vii) Other options exercised such as policy loans;

- (c) Policy Year
- (d) Premium paid;
- (e) Death benefits;
- (f) Net cash value;
- (g) Net increase;
- (h) Rate of increase;
- (i) The following explanations of the information disclosed:
 - (i) *"Net cash value is the total cash value of a policy less any policy loans."*
 - (ii) *"Net increase is the net cash value minus the net cash value at the end of the prior year and minus the premium paid."*
 - (iii) *"Rate of increase is the ratio of the net increase to the sum of the net cash value at the end of the prior year and the premium paid."*

Section 8. Record Retention

An insurer shall maintain a copy of the signed illustration delivered with the policy until three (3) years after the policy is no longer in force.

Section 9. Prohibitions

The following actions by companies or their producers are prohibited:

- A. Representing the policy as anything other than life insurance;
- B. Making any representation about the future performance of the policy, including but not limited to potential dividends, rate of return or cash value other than those which are guaranteed by the company and described in the illustration.

Drafting Note: The working group recognizes that it may be desirable to allow some demonstration of the mechanics of the policy. The working group has asked the technical resources advisors to suggest precisely circumscribed exceptions to Subsection B which would permit such a demonstration.

- C. Making any representation regarding the past performance of the policy other than the representations contained in the illustration;
- D. Using a policy illustration which does not comply with the requirements of Section 5 of this rule;
- E. Providing an applicant with an incomplete policy illustration;
- F. Representing in any way that contractual premium payments will not be required for each year of the policy in order to maintain the illustrated death benefit; or
- G. Illustrating any product not identified pursuant to Section 5B.

Section 10. Annual Report

The insurer shall provide annually a notice to the insured that he or she may request a report which compares the illustrations made at the time of sale with the actual results attained since the last report was prepared. The notice shall be given no later than thirty (30) days after each anniversary date. Any report requested shall contain information similar in format to the original illustration and any changes which affect policy values or premium outlay requirements must be explained.

Section 11. Actuarial Standards

Illustrations shall meet standards with regard to measurement of past performance established by the Actuarial Standards Board. Each insurer shall require a qualified actuary to certify that illustrations used by the company meet these standards. In the event that the Actuarial Standards Board does not develop standards that are acceptable to the Commissioner, the Commissioner may prescribe alternative standards to be met in connection with illustrations.

Section 12. Separability

If any provision of this regulation or the application thereof to any person or circumstance is for any reason held to be invalid by any court of law, the remainder of the regulation and its application to other persons or circumstances shall not be affected thereby.

Section 13. Effective Date

This regulation shall become effective one year after the date of adoption, and shall apply to contracts sold on or after the effective date.

Appendix A

Company Name

LIFE INSURANCE POLICY ILLUSTRATION

Proposed Insured: _____ Age/Sex: _____
 Rating Class: _____ Amount of Insurance: _____
 Plan Type/Name: _____
 Dividend Option: _____

This is an illustration for a [Twenty-Pay Whole] life insurance policy. Payment of premiums is required as follows: [Annually for twenty (20) years].

The purpose of this illustration is to help you understand how the policy works. In comparing different policies, you should not rely solely upon illustrations. You should also consider the financial stability of the company, past performance, the service you expect to receive and the specific policy features you want.

If this illustration demonstrates the policy's past performance, you should understand that future results may be better or worse than the past. Because the values and benefits shown in the illustration will change over time, you should keep this illustration with the policy. The company will annually provide a report that shows account value. You should compare the actual results with the information presented in the illustration. Also, you should periodically contact the company or your agent to check on the status of your policy.

Explanation of Rating Classification. Health history, occupation and recreational activities are used to determine the proposed insured's Rating Class. This illustration is based upon [an average likelihood of claim] designated as [STANDARD]. [Ninety percent] of insureds covered by this type of policy are rated [Standard or better].

I (we) have received a copy of this illustration of the life insurance policy for which I (we) have applied.

 Applicant Date

 Co-Applicant Date

I certify that this is the illustration which is appropriate for the life insurance policy applied for and that no representations have been made that are inconsistent with the illustration.

 Agent Date

Appendix B

**ABC LIFE INSURANCE COMPANY
ILLUSTRATION OF GUARANTEED BENEFITS**

This table shows guaranteed benefits under a policy issued by the company on the date shown. Future results may be better than shown but the company promises they will not be worse.

Participating Whole Life Insurance Policy
Policy Form xyz1234

Producer's Name:
Insured's Name:

Underwriting Class:

	Individual Rating Characteristics		Policy Definition	
Gender:	Male	Annual Premium:	\$1,000.00	
	Nonsmoker	Death Benefit:	\$100,000.00	
Rating:	Preferred			
Age:	35			
Issue Date:	01/01/95			

End of Policy Year	Premium Paid	Death Benefit	Net Cash Value	Net Increase	Rate of Increase
1	\$1,000	\$100,000	\$325	\$(675)	-67.50%
2	1,000	100,000	1,350	25	1.89%
3	1,000	100,000	2,425	75	3.19%
4	1,000	100,000	3,550	125	3.65%
5	1,000	100,000	4,725	175	3.85%

The Net Cash Value is the total guaranteed cash value of the policy minus any policy loans. This is the amount that is guaranteed to be available upon surrender of the policy.

The Net Increase is the Net Cash Value minus the Net Cash Value at the end of the prior year and minus the premium paid.

The Rate of Increase is the ratio of the Net Increase to the sum of the Net Cash Value at the end of the prior year and the Premium Paid.

Appendix C

**ABC LIFE INSURANCE COMPANY
ILLUSTRATION OF PAST PERFORMANCE**

This table shows what actually happened under a policy issued by the company on the date shown. Future results may be better or worse.

Participating Whole Life Insurance Policy
Policy Form xyz1234

	Individual Rating Characteristics		Policy Definition	
Gender:	Male	Annual Premium:	\$1,000.00	
	Nonsmoker	Death Benefit:	\$100,000.00	
Rating:	Preferred	Dividend Option:	Paid-up Additions	
Age:	35			
Issue Date:	01/01/90			

End of Policy Year	Premium Paid	Death Benefit	Net Cash Value	Net Increase	Rate of Increase
1	\$1,000	\$105,000	\$350	\$(650)	-65.00%
2	1,000	112,000	1,450	100	7.41%
3	1,000	121,000	2,650	200	8.16%
4	1,000	131,000	3,950	300	8.22%
5	1,000	142,000	5,250	300	6.06%

The Net Cash Value is the total cash value of the policy minus any policy loans. This is the amount that is available upon surrender of the policy.

The Net Increase is the Net Cash Value minus the Net Cash Value at the end of the prior year and minus the premium paid.

The Rate of Increase is the ratio of the Net Increase to the sum of the Net Cash Value at the end of the prior year and the Premium Paid.

ATTACHMENT ONE-D

Life Disclosure Working Group of the Life Insurance (A) Committee June 3, 1994

The Life Disclosure Working Group met by conference call at 2 p.m. on June 3, 1994. Bob Wright (Va.) chaired the meeting and the following working group members or their representatives participated: Don Koch (Alaska); John Montgomery (Calif.); Roger Strauss (Iowa); Lester Dunlap (La.); Tony Higgins (N.C.); Noel Morgan (Ohio); and Commissioner Robert Wilcox (Utah). Carolyn Johnson (NAIC/SSO) also participated.

Bob Wright (Va.) asked the working group members to consider first the Life Insurance Illustrations Model Act. He asked if there were any changes that the working group members recommended. He also asked if the members were comfortable with the revision to Section 4—Penalties, and the reference to the Unfair Trade Practices Act. Members of the working group agreed that the provision was written in an appropriate manner. Mr. Wright next asked whether Section 3—Authority to Promulgate Regulation should be changed. He suggested changing the provision to read “the commissioner may promulgate regulations...” After some discussion the working group members decided to leave “the commissioner shall promulgate regulations...”

Mr. Wright asked the working group members to review with him the Rules Governing the Use of Illustrations in Connection With the Sale of Life Insurance. Mr. Wright asked Carolyn Johnson (NAIC/SSO) to interject comments throughout the document that had been received from the working group members in response to the draft they had received the prior week.

Section 1. Purpose

Noel Morgan (Ohio) suggested changing the sentence that read “the objective of this rule is that illustrations adequately describe policies...” to “the goal of this rule is that illustrations accurately describe policies...” Mr. Morgan was responding to comments received which suggested that using the term “objective” would create a legal standard which could be challenged more easily. The working group agreed to this change.

Ms. Johnson said one member had commented that the objective of the last sentence saying that there should be understanding without any explanation by a producer was a laudable goal but probably not attainable. Mr. Wright said he had received a comment that the sentence denigrated producers. After some discussion the working group members decided that there was no intention to downgrade the services provided by a producer and they did not think this sentence did that, so they decided to leave the sentence in the draft.

Section 4. Definitions

Ms. Johnson said a comment had been received on Section 4 suggesting that the definition of “guaranteed values” actually referred to “guaranteed surrender values.” Commissioner Robert Wilcox (Utah) agreed the working group was defining guaranteed surrender values, but said this was only one guaranteed benefit of a policy. He said a death benefit was also a guaranteed benefit. Mr. Wright asked if it would be appropriate to add another definition of guaranteed benefits. Commissioner Wilcox suggested adding the definition of “guaranteed cash value” from the set of definitions provided by the American Academy of Actuaries, as well as a broader definition. The working group decided to add a definition that was broader and to use the American Academy of Actuaries definition for guaranteed cash values.

The working group next looked at the definition of illustration and the suggestions for alternatives that had been received. The working group decided that the American Academy of Actuaries definition and the resource group definition were both inappropriate because the definitions included non-guaranteed elements. It was decided the provision should apply to the producer and the insurer, to cover direct sales of life policies. The working group also considered whether it was best to use the word “sell” in the first paragraph, and the decision was made to leave the definition as written with the addition of the words “or insurer” after each instance where the word producer appears. Ms. Johnson said she had received a telephone comment the prior day suggesting that this regulation should not apply to term insurance where illustrations were designed to compare the prices of different companies. She asked whether this definition included that type of illustration. Mr. Wright said the dividing line was in the term “performance over time.” If the term insurance showed only straight premiums that were not dependent on the performance of the policy, the illustration would not be included in this definition.

Section 5. Illustration Format Standards

Mr. Wright asked if there were any comments on Section 5, and Hal Phillips (Calif.) asked about the purpose of Subsection C(1) on the rating classification. Mr. Wright said it would give the consumer some idea of what his classification meant. Otherwise he had no way to know whether he was being shown the best classification or the worst. Mr. Morgan said it served as a protection against low-balling. The consumer could get an idea of whether he would get the rate being illustrated. Mr. Phillips asked how past performance would be demonstrated as defined in Subsection E when the policy was a new one. John Montgomery (Calif.) recommended inclusion of the resource advisors' suggested language allowing for this situation and suggested limiting the time when this would apply to one year.

Mr. Wright asked if Subsection C(2), which said only that the applicant had received the illustration, was appropriate. He asked if a greater burden should be placed on the applicant. Tony Higgins (N.C.) said he thought the language was appropriate as written. He thought it was important that the consumer not say he had understood the illustration. Mr. Wright asked if Paragraph (3) was too broad. He read to the group the resource advisors' comments that this was not good language. Since no alternatives have been suggested by the technical resource advisors, the working group decided to leave the language as written.

Section 6. Certification by the Company; Disclosure

Mr. Wright summarized the comments that he had received from the technical resource advisors and the working group decided to leave the provisions of Section 6 as they were written.

Section 9. Prohibitions

A comment was received that Subsection F should have a phrase added to cover the situation where premium payments were not required, such as a single-pay policy. Mr. Morgan suggested adding the word "contractual" before the words "premium payments" to cover that situation. The working group agreed this would address the problem.

Section 10. Annual Report

The working group considered the comments from the resource advisors and others saying that the annual report was difficult to produce and expensive. Mr. Phillips asked what the purpose of this report was. Roger Strauss (Iowa) said that, since only the guarantees had been illustrated, this would give the company an opportunity to show how the non-guaranteed elements had actually performed during the past year. Sheldon Summers (Calif.) asked whether this should be mandatory. He suggested that the company would want to show how it had performed so he did not think it was necessary for that provision to be mandatory. If there were illustrations of other than guarantees, then it would be important to require showing how the policy had actually performed. The members of the working group agreed with Mr. Summers' analysis and decided to change the requirement to providing information that an annual report would be available.

Mr. Wright next reviewed some procedural issues with the members of the working group. He said the working group had agreed not to expose the draft until the fall National Meeting because it wanted to incorporate some of the language from the Second Standard Nonforfeiture Law draft. He said the working group would continue to refine the draft prior to exposure. Mr. Morgan asked if there was a way to focus the comments of the interested parties. He said that it seemed the comments were the same thing over and over again, and he asked if there was a way to give some kind of structure about what topics the working group wanted to hear comments on. Mr. Wright said he would send a letter to George Coleman, chair of the technical advisors, outlining the expectations of the working group. Mr. Wright said that, at the Baltimore meeting in June, comments would be solicited of a technical nature, rather than a philosophical nature. Since time was limited the industry would run the risk of the draft containing technical glitches if comments were not focused on that aspect of the draft. Mr. Wright said another important step was to develop a good working relationship with the actuarial standards board. He said the board's meaningful help would be critical to the efforts of the working group. Mr. Higgins and Lester Dunlap (La.) said they had received many interesting responses supporting guarantees and "honest illustrations."

Having no further business, the Life Disclosure Working Group adjourned at 4 p.m.

ATTACHMENT ONE-E

Life Disclosure Working Group
of the Life Insurance (A) Committee
Washington, D.C.
May 1 - 3, 1994

The Life Disclosure Working Group met at the Embassy Suites Hotel in Washington, D.C., at 1 p.m. on May 1, 1994. The meeting was called to order by Bob Wright (Va.), chair, and the following working group members were in attendance: Don Koch (Alaska); Roger Strauss (Iowa); Lester Dunlap (La.); Noel Morgan (Ohio); Tony Higgins (N.C.); and Fred Nepple (Wis.).

Bob Wright (Va.) stated the purpose of the meeting was to work on a draft of a model illustrations regulation to implement the vote taken at the March meeting of the working group to allow projections into the future only of guarantees, and to show past performance in conjunction with an index such as the Consumer Price Index. Roger Strauss (Iowa) distributed a memo

(Attachment One-E1) from Commissioner David Lyons (Iowa), chair of the Life Insurance (A) Committee, for discussion. He said there had been some misunderstanding on the part of the life insurance industry, which the memo was designed to address. Mr. Strauss said that some individuals had the impression that the working group would not consider illustrations of current scale and planned to adopt the guarantees-only model in June. The working group agreed that it would continue to follow the instructions of the A Committee, which was to work on the guarantees-only provisions, but to keep the door open for suggestions for understandable illustrations based on projections of current scale.

Mr. Wright listed the core elements to be included in the draft: (1) a cover sheet; (2) financial rating of the insurer; (3) signature requirements; (4) illustration of guarantees and past performance; and (5) a yearly update requirement. Noel Morgan (Ohio) asked if the illustration would be made part of the policy. The working group decided to table that issue until later in the process and then discuss it further. Tony Higgins (N.C.) asked if the regulation should apply to pension and welfare plans. After some discussion, the working group decided to leave the exemption in Section 2 of the draft. Mr. Wright also noted that a separability provision would be needed, and asked Carolyn Johnson (NAIC/SSO) to add language such as usually found in the NAIC models. Mr. Wright listed other issues on the table for discussion: whether to include a consumer signature requirement, whether to prescribe the format, and what prohibitions to include.

The working group discussed extensively the provision contained in Section 5C(1) that provided for disclosure of the rating classification on which the illustration was based. Mr. Wright said it was important to deal with the issue of the company that illustrated the best classification when only 2% of the people were actually written in that class. If an individual actually was underwritten in a different classification from that illustrated, a requirement should be included to show the appropriate illustration and to get that one signed also. Mr. Morgan suggested a requirement that the producer illustrate the rating classification that the individual would be most likely to get. Mr. Higgins responded that the producer might not be able to make that determination, but he felt that there would be an incentive to get the closest one possible because the agent would not want to go back and have to show a different illustration and explain new numbers. Don Koch (Alaska) pointed out that if it is a new offering the company would not know what percentage of people were going to fit into each class.

The working group next discussed the appropriateness of including a requirement for a consumer signature on the document. The group decided it was important not to imply consumer understanding of what was in the illustration but just an acknowledgment of receipt of the illustration.

The working group adjourned at 5:30 p.m.

The Life Disclosure Working Group reconvened on May 2, 1994, at 9 a.m. The following working group members were in attendance: Bob Wright (Va.), chair; Don Koch (Alaska); Roger Strauss (Iowa); Lester Dunlap (La.); Noel Morgan (Ohio); Tony Higgins (N.C.); Commissioner Robert Wilcox (Utah); and Fred Nepple (Wis.). Mr. Wright called the meeting to order and announced the format of this open meeting to those in attendance. He summarized what had been accomplished by the working group and said the task for this day would be to consider comments section by section on the model draft regulation. He said the working group was interested in listening to comments on concepts and also suggestions on wording, and said the working group would meet on the next day to rewrite the draft in response to the comments received. He promised that a revised draft would be circulated so that comments could be made on that draft. He asked those who wished to have comments considered before the NAIC summer National Meeting to return comments to Ms. Johnson within the next week to 10 days. He said there would also be a time for comments at the June meeting in Baltimore.

Mr. Wright asked if there were any comments on Section 1, Purpose. Barbara Lautzenheiser (Lautzenheiser & Associates) said the issue goes beyond understandability to understandability for what purpose. She said an individual looking at a policy that shows guarantees only cannot tell how the policy works. She said in the last 20 years there has been a great deal more emphasis on insurance as an investment, and this illustration regulation would make that trend even worse. She said the purpose of an illustration was to show how a particular policy would fit a policyholder's needs.

S. Reed Ashwill (National Association of Life Insurance Brokerage Agencies—NALIBA) said that if an agent was funding for a target amount at age 65, guarantees only would not allow that to be shown. He said this also encourages the concept that life insurance policies are like securities, so that they should be taxed like those investments. He emphasized the importance of not giving the impression of life insurance as an investment.

Mr. Morgan expressed surprise at the last two comments. He said his impression was that showing guarantees only into the future moved the industry closer to talking about insurance rather than investments because it did not show larger and larger numbers marching off into the future. Mr. Wright asked why it would not be possible to demonstrate how the policy worked using past performance—the concrete data showing what had really happened. Mr. Ashwill responded that if it was a new policy there would not be any numbers to use. He also questioned the use of numbers from a period when interest rates were so much higher than is currently the case. Mr. Higgins reminded the group that the charge was to develop a regulation using guarantees and past performance, and he suggested looking at these other issues at a later time.

Michael DiPiazza (Metropolitan Life) said that an appropriate use for past performance was to compare policies from different companies. He said it was like a consumer purchasing a mutual fund and comparing the performance of the various funds to determine which one to purchase. George Coleman (Prudential) asked how to fill in the gap when it was possible to show 40 years of guarantees, but a company might only have past performance for two or four or six years. Mr. Wright acknowledged the difficulty and asked those in attendance to think of ways to fill this gap and to demonstrate the performance of the policies.

Linda Lanam (Life of Virginia) asked about policies containing a benefit that was not available until the policy had been in effect for 10 years. If there was not 10 years of past performance, there would be no way to show this benefit. She also pointed out that dividend histories were only available for mutual companies; stock companies did not usually have that information.

Bill Koenig (Northwestern Mutual) shared a chart which he had prepared showing recent historical experience for his company. He presented a way of looking at company experience and putting this into a formula which he suggested could be projected into the future. Mr. Morgan asked how this would differ from projections as currently being done. Mr. Koenig acknowledged that there might not be much difference in some cases, but there would be in the instance where illustrations showed improving mortality. He said he understood the purpose of the working group's project was to eliminate imagination and to show actual demonstrable numbers. Ms. Lautzenheiser asked what a consumer would do with all these numbers. She said too many numbers were as bad as too few. Ms. Koenig said he was giving the chart to the working group as a way to demonstrate that there was more than one way to show past performance. Mr. Coleman urged the group to consider projection of the numbers on this type of chart beyond the eight years shown here. He said it was a disadvantage to show the policy potential without using some projections. He said this could be described as future projections with discipline. Mr. Higgins reminded the group that its charge was to move forward with guaranteed elements. He said this effort by the technical resource advisors made giant steps forward from the earlier efforts, but it was not the charge of the group today. John Dinius (Aetna) said that in some sense using past performance was a projection into the future. Mr. Morgan said the current proposal of the working group left it to the buyer to draw inferences; using the illustrations currently in practice, the agent or insurer has drawn the inferences for the consumer.

Scott Cipinko (National Alliance of Life Companies—NALC) said that the information presented so far ignored the death benefit. He said using a consumer price index focuses on the wrong thing because the illustration does not show the death benefit. He said it was not appropriate for the insurance industry or the regulators to encourage consumers to look at insurance as an investment rather than a death benefit.

Frank Irish (John Hancock) spoke as a member of the Actuarial Standards Board. He said the board stood ready to write standards as soon as the NAIC could give it an idea of where this project was headed. He pledged to put the project on a fast track as soon as it was clear what would be needed for an illustration actuary to certify.

Hearing no comment on Section 2, Mr. Wright moved on to Section 3. Commissioner Robert Wilcox (Utah) asked if it was appropriate to exclude variable life policies from the regulation. Mr. Wright asked if it was possible to include variable life since they did not have guarantees. Mr. Koenig asked if this type of illustration was generally used for a variable life policy. Mr. Ashwill pointed out that if variable life policies were not included, they could project into the future and other policies could not, so that parity between the different types of policies would be lost. Carolyn Cobb (American Council of Life Insurance—ACLI) said that variable life policies were subject to regulation by the Securities Exchange Commission (SEC). She said the disclosure required by the SEC was formidable. Mary Griffin (Consumers Union) pointed out that the SEC has stated that it feels the disclosure it requires is insufficient and it is considering requiring standardized assumptions. William Fisher (Massachusetts Mutual) said that many variable life policies have a fixed portion and he wondered if this regulation would apply to the fixed portion.

Mr. Wright next turned the attention of the group to the exemption for pension and other retirement plans. He asked if it was the intent of the working group that this should only apply to ERISA plans. Commissioner Wilcox asked if he bought a policy to fund his retirement, did that become a pension plan? Mr. Wright responded that it was not his intent that the provision should be utilized that broadly. Commissioner Wilcox said that tying it to an employer selection might be a useful way to narrow the provision, but he questioned the need to exclude them at all. Mr. Higgins said that pension plan administrators were not always sophisticated purchasers, and might also need the benefit of the protections provided in the model regulation. Mr. Coleman suggested that it was not possible to decide this issue in a vacuum. He said it was important to discover whether there were provisions in ERISA that would address these issues. Commissioner Wilcox responded that under ERISA there was almost no protection.

Mr. Ashwill asked if using guarantees only might result in overfunding for pension plans. He pointed out there were serious penalties for overfunding and suggested that consideration might be a good reason to exclude pension plans from the purview of the model.

Mr. Wright then asked for any comments on Section 4, Definitions. Mr. Fisher asked that the working group be careful that the definition of illustration (4B) not be so broad that a letter from an agent to a customer was considered to be an illustration requiring columns of guaranteed numbers. Ms. Lanam said that in some parts of the draft the illustration is referred to as a numeric, tabular or graphic demonstration and at other times it is just referred to as a tabular illustration, and she wondered what impact that had on an illustration in the form of a graph or a chart. Ms. Griffin spoke in favor of a standardized format, with a standard also for a chart or graph. Mr. Koenig asked whether this illustration would apply to in-force business, for example if a consumer asked how his policy was doing. Mr. Morgan replied that the model applies to "the sale of life insurance policies."

Next attention was turned to Section 4C, "interest credited." Commissioner Wilcox pointed out that the draft throughout used the term "interest" for anything that increased value. Ms. Lautzenheiser said this terminology also reinforced the idea that insurance was more like an investment. Mr. Dinius said the terminology was not accurate; rather than saying "increase" it should say "net increase" because there would be some pluses and some minuses. In the definition of "past performance" in Section 4D Commissioner Wilcox questioned whether it was appropriate to limit the demonstration to amounts credited to a policy during the calendar year. He said if a company could produce information from policy anniversary to policy anniversary, that method of demonstration should not be precluded. Mr. Wright asked if it would be appropriate to take out the adjective.

Commissioner Wilcox asked if a policy form changed in some minor way, did that mean it was a new policy form? He asked if a new mortality table was a requirement to start all over for every policy form?

Consideration next turned to Section 4E, Qualified Actuary. Commissioner Wilcox suggested crossing out everything after the word "actuary." He said if someone is an actuary, he has agreed in the profession's code of conduct not to give an opinion where he does not have understanding so putting in the requirements for the actuary to have certified an understanding of illustrations was unnecessary.

Mr. Wright asked for comments on Section 5, Illustration Format Standards. Ms. Lanam pointed out that throughout the draft the terms "premium classification," "underwriting classification" and "rating classification" are used interchangeably and she suggested using one of these terms instead of all three. Mr. Ashwill said the term "underwriting class" is the appropriate, more accurate term to use. Mr. Ashwill also asked why it was important to include the percentage of insureds covered by a particular form as required in Section 5C(1). Mr. Strauss responded that if only 1% of the insureds get that rate, that is useful information to have. Mr. Dinius suggested changing this to "this class or better" because if a person were to see that 30% got that class it might be misleading because 70% got a better class.

Discussion next turned to Section 5C(2) which required a reporting of the current financial rating of the insurer by all rating agencies that had rated the insurer. Arnold Bergman (Aetna) asked who was going to regulate the rating agencies. He said insurance regulators should not encourage the use of unregulated rating agencies' numbers. Mr. Cipinko said this requirement was weighted against small companies, who generally did not get as good a rating. Mr. DiPiazza agreed that this requirement created an uneven playing field in favor of the big companies. Mr. Wright said he thought it was valuable for the consumer to know something about the company to which he was entrusting his money. Jeff Tate (Great American Life) suggested as an alternative a provision that said if a company wanted to use its rating, then it should explain what that meant. Ms. Lanam said it would also be important to disclose that some rating agencies require payment of a fee to get the best ratings. Ms. Griffin said that the explanation for the rating agency requirement was not as cumbersome as the industry was implying.

Discussion next turned to Section 6, Certificate of the Company; Disclosure. Fred Nepple (Wis.) summarized the intent of the section which required a second copy of the illustration if the policy issued was not the same as that illustrated at the first contact. Mr. Irish asked if Subsection B, which presently says an officer of the insurer shall sign and date the certification, should be changed to have an actuary sign. Mr. Nepple said that it was the intent of the working group that an officer of the company be the one to sign the policy. Mr. Fisher registered concern about having an officer signing policies. He asked that the drafting note, saying that it could be a facsimile signature, be made a part of the section rather than a drafting note.

Discussion next turned to Section 7, Standards for Illustrations. Michelle VanLeer (John Hancock) expressed confusion about the requirements of Section 7. She asked if there was to be one illustration for both future guarantees and past performance. Mr. Wright responded that it was intended that there be one illustration with two parts. Mr. Koenig said that it would be a tremendous expense for companies to get all of the information required to show past performance. Mr. Nepple asked if the working group could expect companies to keep this data from this time forward. Mr. Morgan asked what would be available if not all of this information. Mr. Koenig responded that information was available for a few ages and a few plans. Mr. Coleman expressed concern about comparing past performance to the Consumer Price Index. Mr. Wright said the group had asked for information on an appropriate index and suggested that Mr. Coleman provide information to Ms. Johnson. Ms. Cobb said that the Section 7 provisions requiring guaranteed performance were not understandable. She suggested an appendix to demonstrate what the working group was looking for.

Mr. Wright then asked for comments on Section 8, Prohibitions. Ms. Griffin pointed out there was no penalty in the regulation. Mr. Wright said the penalty provision was generally found in a statute. Mr. Fisher said the provisions of this section were much too sweeping, and it would be impossible to talk about the policy without using some of these prohibited elements. Ms. Lautzenheiser said the provisions of this section would have a major impact on policy design. She said if regulators wanted to limit product design they should do so directly.

Discussion next turned to Section 9, Annual Report. Mr. Koenig asked if this report was a new illustration. Mr. Wright responded that it was intended to be a report of what had actually occurred during the prior year. Mr. Coleman questioned the purpose of this report. Mr. Wright responded that it would allow the policyowner to compare the actual performance with the guarantees that he had been shown.

Mr. Wright said the working group would be meeting on the following day to consider the issues raised. He expressed appreciation for the constructive comments the group had received on how to make the draft clearer. He said the working group would make an effort to incorporate the comments that it had heard. Commissioner Wilcox said it was not the intent of the working group to make regulation obtrusive, but at the same time, he was being a realist about what was being shown now. He said if it was possible to get control of the situation without stepping on the toes of those who were not damaging consumers, he would be in favor of it. He said at the current time something very close to fraud is being committed with the assistance of illustrations. He said it would be necessary for all to put up with some things that they did not want, to get a healthy insurance industry. He hoped it was the goal of everyone present to help consumers truly understand what they were purchasing.

Having no further business, the Life Disclosure Working Group of the Life Insurance (A) Committee adjourned at 5 p.m.

The Life Disclosure Working Group reconvened on May 3, 1994, at 9 a.m. at the offices of the NAIC in Washington, D.C. In attendance were: Bob Wright (Va.), chair; Don Koch (Alaska); Roger Strauss (Iowa); Lester Dunlap (La.); Noel Morgan (Ohio); Commissioner Robert Wilcox (Utah); and Fred Nepple (Wis.).

The first issue discussed was the illustration of past performance. Mr. Morgan suggested making the illustration of past performance optional. Mr. Nepple pointed out that if the illustration of past performance is not required, the objective of using it to compare between companies would not work because only the good companies would show past performance. Commissioner Wilcox said he thought it would be easier to use past performance if a company was not limited only to that particular policy form. He said it would be possible to project actuarially how past performance would have varied due to the features of each policy. Commissioner Wilcox volunteered to prepare an appendix on past performance using that concept. He said he had expected that small companies would not be able to produce the required information, but he was surprised to hear large companies say they could not easily access this information.

The working group next looked at the illustration of guarantees. Commissioner Wilcox said this part was already done because it could be copied from the Second Standard Nonforfeiture Law, which is being considered by the Life and Health Actuarial Task Force. Since the Second Standard Nonforfeiture Law has not yet been adopted, the working group decided it would not be appropriate to reference that model, but instead should copy the standards into the illustrations model regulation.

The next item for discussion was whether it was appropriate to include variable life insurance under the purview of the model. Commissioner Wilcox pointed out that the Second Standard Nonforfeiture Law does include variable annuities. He thought there was more abuse on variable products than others and asked if companies were being allowed to do whatever they wanted by removing variable life from the model. He also pointed out that model did not include a definition of variable life insurance. The working group decided to include a reference to variable life in the exceptions, and to be more specific by referring to the NAIC's model on variable life insurance.

The group next discussed the issue of disclosure of financial ratings. The group decided there were several alternative approaches: 1) require disclosure of financial ratings; 2) allow them and require an explanation of the ratings if they are used; 3) do not allow the use of financial ratings; 4) disclose that there are agencies that do a rating of the companies and suggest where to get further information; 5) allow reference to one financial rating; or 6) allow disclosure of the highest, the lowest, and one of the insurer's choice. Mr. Wright said he thought a point had been made in the prior day's meeting that the rating agencies were an unregulated industry. He recognized that the system of rating was imperfect but he wondered if it was better than nothing. Commissioner Wilcox said he thought the regulators were giving the rating industry more credibility by including them in the model. Upon motion duly made and seconded, the working group voted not to include ratings in the model law.

The working group next considered Subsection B under Section 8—Prohibitions and the comment that the subsection was too broad. Mr. Morgan suggested adding a drafting note saying that the working group was waiting for input from the technical advisors on how to revise this section.

Commissioner Wilcox presented to the working group a suggestion for standards for past performance. Included was an assumption that an index, such as the consumer price index, would not be included. The group agreed that this was appropriate.

The next issue discussed by the working group was the actuarial certification. It was agreed that when an officer signs the policy illustration, that it is assumed that he has the backing of an actuarial certification.

The working group went through the rest of the model regulation section by section considering comments made at the prior day's meeting and making changes as necessary. Several assignments were made to working group members to prepare other portions for addition to the model regulation. Mr. Wright asked Ms. Johnson to mail out the revised draft regulation to the interested parties and to the working group members as soon as it was ready.

Having no further business, the working group adjourned at 3:30 p.m.

ATTACHMENT ONE-E1

TO: Members of the Life Disclosure Working Group
FROM: Commissioner Dave Lyons (Iowa), Life Insurance (A) Committee Chair
DATE: April 29, 1994
RE: Work on Illustrations Model

First of all, let me apologize for being unable to attend your May 1-3 meetings. My schedule has made this impossible.

Second, on behalf of myself, Vice Chair Willis and all the members of the Committee, I would like to take this opportunity to thank you for all of your efforts to date. This has been a huge undertaking with short time frames.

Third, I have recently received questions regarding the position and intentions of the Life Insurance (A) Committee. I have discussed these questions with Vice Chair Willis and several other committee members. As these questions may arise during your meetings next week, I wanted you to be aware of what appears to be the general position of the Committee on these questions:

Question: Has the Committee taken the position that the illustration of non-guaranteed values for life insurance policies is inherently improper, and as such must be banned?

Answer: No, as long as the illustrations are clear and understandable and the benefit they represent to the consumer outweighs their potential for abuse. However, it has not appeared to the Committee that a system has been devised which could assure this outcome, and therefore restrictions appear in order.

Question: It is rumored that the Life Insurance (A) Committee will only consider, and will in fact adopt for exposure, a Model Act prohibiting "non-guaranteed illustrations," whether it has been adequately completed or not. Is this what the industry can expect in June?

Answer: No. If the "guaranteed only" Model is not adequately developed or the members of the committee believe that there has been insufficient time for review and comment on that Model, I would not expect adoption. Additionally, as several members noted during the March meeting of the Committee, there will be interest in reviewing materials and options which go beyond "guaranteed only."

Question: Given the present focus of the working group on "guaranteed only," and the limited time before the June meeting, should industry experts cease work on materials and options relating to "non-guaranteed" illustrations prior to the June meeting?

Answer: No, to the extent possible, the industry should both respond to the "guaranteed only" draft and continue its work on "non-guaranteed" illustration options.

Question: Will the June meetings of the Life Insurance (A) Committee be limited to consideration and discussion of "guaranteed only" options?

Answer: No. The full range of issues and options regarding illustrations are anticipated for consideration and debate.

Again, my thanks for all your efforts on this issue to date.

ATTACHMENT TWO

To: Julie Spiezio, ACLI
 From: Mary Eileen Dixon, ACLI
 Date: June 9, 1994
 Re: Preliminary Results of ACLI/LIMRA Accelerated Death Benefit Product Survey

Although results are not yet final, provided below are some of the preliminary results of this effort. Final results should not differ substantially from these numbers.

1. The survey was sent out to 664 companies, representing the combined memberships of American Council of Life Insurance (ACLI) and Life Insurance Marketing and Research Association (LIMRA) as well as some non-member companies which we understood offered accelerated death benefit features. Taken together, the companies on the mailing list represent approximately 95% of the life insurance in force in the United States, according to the latest available numbers.

2. As of June 8, we have identified 216 companies which offer some type of accelerated death benefit product (e.g., terminal illness, dread disease, long-term care, or some combination or variation thereof). Of the 216, 204 have responded to the survey, while 12 have not yet responded but have confirmed offering an accelerated death benefit feature.

The last time a survey of similar scope was conducted was in 1991. At that time, 113 companies were identified as offering an accelerated death benefit product. The 216 companies identified this year represent an increase of more than 90% since 1991.

3. The 216 companies currently identified as offering accelerated death benefit products represent approximately 70% of the life insurance in force in the United States.

4. In addition to the companies currently in the market, 12 other companies indicated that they were planning to introduce such a product by June 30, 1994. An additional 65 are currently considering introducing such a product. Two hundred three (203) companies have not responded at all. Sixteen have indicated that they were inappropriate for inclusion in the study (e.g., they do no business in the United States, sell only annuities, etc.).

In survey-related calls to a number of companies not currently offering an accelerated death benefit product, several volunteered that they were reluctant to offer such a product until regulatory problems and tax clarification issues have been resolved.

5. The 204 companies responding to the survey reported a total of 270 separate accelerated death benefit products. One hundred eighty (180) companies reported offering at least one individual product, while 56 reported offering a group product. Thirty-two (32) companies reported offering both types of products.

6. The diagnosis of a terminal illness is by far the most common triggering event for the products on the market. Of the 180 companies offering an individual accelerated death benefit feature, 158 offer products which accelerate for terminal illness. Of the 56 companies with a group accelerated death benefit product, 55 provide a terminal illness product. The numbers of companies offering products which accelerate for catastrophic illness, permanent confinement to a nursing home, need for long-term care, or other conditions are much smaller.

7. Of the 56 companies offering a group accelerated death benefit product, only 23 were able to provide figures concerning the number of individuals covered by such provisions. Together, the 23 companies report a total of approximately 5,033,000 certificate holders covered by an accelerated death benefit provision.

Of the 180 companies offering an individual product, 103 provided comparable information. They report approximately 13,058,000 policyholders covered by an accelerated death benefit provision.

Despite the fact that these numbers taken together represent a 16-fold increase over the 1,130,000 policyholders reported as being protected by an accelerated death benefit provision in 1991, it must be recognized that they probably represent substantial undercounts of the numbers of individuals actually covered by an accelerated death benefit provision at the present time. In addition to the responding companies which were unable to provide coverage figures for their products, the companies which have not responded to the survey may well include a substantial number which offer some type of accelerated death benefit feature.

FIGURE 1

Life Insurance Companies Offering Accelerated Death Benefit Products

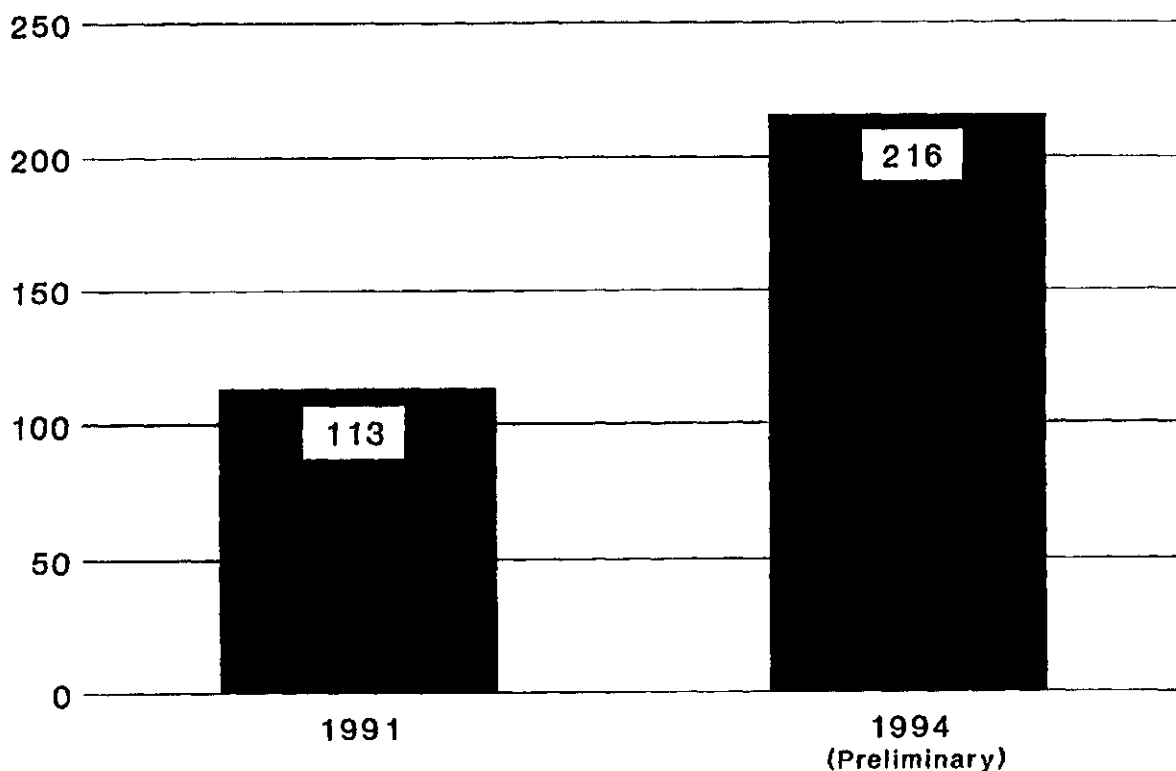
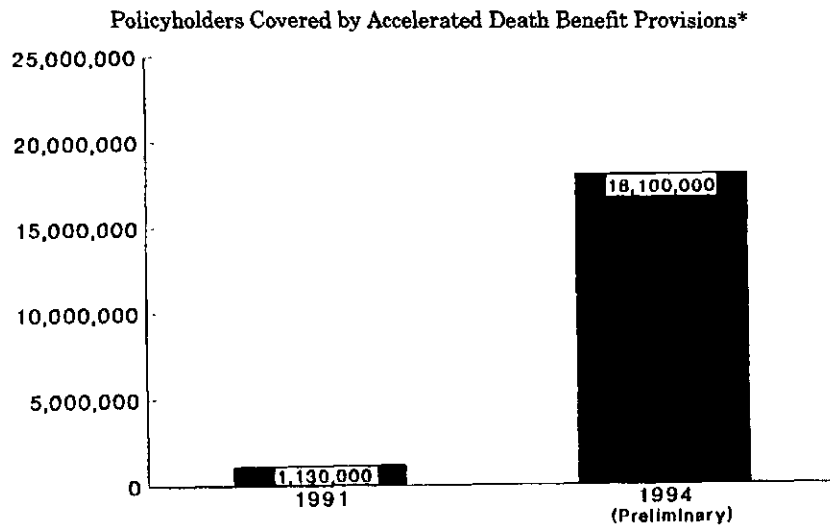


FIGURE 2



*The figures provided for both years represent substantial undercounts since many of the companies offering these features were unable to provide this information in both 1991 and 1994.

ATTACHMENT THREE

Viatical Settlement Working Group
of the Life Insurance (A) Committee
Baltimore, Maryland
June 13, 1994

The Viatical Settlement Working Group of the Life Insurance (A) Committee met in Maryland A of the Stouffer Harborplace Hotel in Baltimore, Md., at 3 p.m. on June 13, 1994. A quorum was present and Roger Strauss (Iowa) chaired the meeting. The following working group members or their representatives were present: Don Koch (Alaska); Reginald Berry (D.C.); Mary Alice Bjork (Ore.); Rhonda Myron (Texas); and Bob Wright (Va.).

1. Adopt Minutes of April 29, 1994, Conference Call

Upon motion duly made and seconded, the minutes of the April 29, 1994, conference call were adopted (Attachment Three-B).

2. Receive Comments on Revised Draft of Model Regulation

Roger Strauss (Iowa) highlighted the changes made to the Viatical Settlements Model Regulation draft released in March 1994. He said a drafting note had been added to Section 1, incorporating a delayed effective date so that companies could continue to do business while going through the application process in their state. A comment had been received that a surety bond was not appropriate for the broker, so the requirement for a surety bond was moved to Section 1 and made to apply to providers. An errors and omissions policy was required of the viatical settlement broker in Section 2. Subsection 2F(3) was added to provide that the license of a broker could be revoked if he placed business with a viatical settlement provider that was not licensed in the state. Mr. Strauss drew the attention of the working group to Section 4 where the amounts for the minimum percentage had been changed to the amount in the original draft. Mr. Strauss said Section 5 was an entirely new section. Section 6, General Rules, had provisions added to provide for wire transfer or certified check and to require that payment of the proceeds be made in a lump sum.

Mr. Strauss asked if there were any comments on any section of the model. Mary Alice Bjork (Ore.) said she thought it would be helpful if Mr. Strauss would explain why Section 5 had been added to the draft. Mr. Strauss responded that the working group members realized that the viatical settlement industry was a relatively new industry. He said there was not a lot of statistical information available, and the working group members thought the information required in this Section 5 would serve as a database of information on the new industry. Roy Olson (Wash.) suggested that the information required in Section 5 should say at the beginning of the introductory paragraph, "For the previous calendar year."

John Banks (Viaticus) asked about Section 6C. He said his company occasionally had an instance where an individual asked if it was possible to have the money paid in installment payments. He asked how his company should respond to this request. Mr. Strauss said the working group had been concerned that paying the proceeds in payments put the viatical settlement company in the position of acting as an insurer. Bob Wright (Va.) said the normal practice for a structured settlement was to purchase an annuity. Mr. Banks asked if there was any provision prohibiting the company from purchasing the annuity from a related company. Mr. Strauss responded that the regulators would be concerned if it was a mandatory provision that the

annuity be purchased from the related company. Commissioner David Lyons (Iowa) suggested that if, after the regulation had been implemented, companies found ways that the model put restrictions on appropriate actions, they should bring the issue to the Life Insurance (A) Committee. He said the Life Insurance Committee had no desire to restrict viatical settlements that were appropriate.

George Coleman (Prudential) asked how the working group had arrived at the percentages contained in Section 4. Mr. Strauss responded that the working group had been uncertain of what the appropriate percentages should be so had reverted to the earlier numbers which had been provided by the industry as average payments. Commissioner Lyons commented that the working group did not intend to limit the availability of viatical settlements and because the data was not available to make clear what the minimum percentages should be, the working group lowered the minimums so as not to artificially interfere with the market. The working group had taken upon itself the burden of providing a method to collect data so that at some later point it would have correct information and could raise the percentages if appropriate.

At that point, Mr. Strauss adjourned the open meeting and in closed session, the working group voted to adopt the model regulation with the change suggested by Mr. Olson (Attachment Three-A).

Having no further business, the Viatical Settlement Working Group adjourned at 4 p.m.

ATTACHMENT THREE-A

VIATICAL SETTLEMENTS MODEL REGULATION 6/13/94

Table of Contents

Section 1.	License Requirements for Viatical Settlement Providers
Section 2.	License Requirements for Viatical Settlement Brokers
Section 3.	Other Requirements for Brokers
Section 4.	Standards for Evaluation of Reasonable Payments
Section 5.	Reporting Requirement
Section 6.	General Rules

Section 1. License Requirements for Viatical Settlement Providers

A viatical settlement provider, as defined in [insert reference to Section 2 of Viatical Settlement Act], shall not enter into or solicit a viatical settlement contract without first obtaining a license from the commissioner.

Drafting Note: States should consider including an effective date three to four months in the future, to allow existing companies to continue operation while licensing requirements are being implemented.

- A. The application shall be on a form required by the commissioner.
- B. Only those individuals named in the application may act as viatical settlement providers.
- C. The commissioner may ask for such additional information as is necessary to determine whether the applicant complies with the requirements of Section [insert reference to Section 3 of Viatical Settlement Act].
- D. Viatical settlement providers shall acquire and maintain a surety in the amount of \$[insert amount]. A copy of the executed bond shall be filed with the commissioner at the time of application for a license.

Section 2. License Requirements for Viatical Settlement Brokers

A viatical settlement broker shall not solicit a viatical settlement contract without first obtaining a license from the commissioner.

- A. A viatical settlement broker shall make application on a form required by the commissioner.
- B. The application shall be accompanied by a fee of \$[insert amount]. The license may be renewed yearly by payment of a fee of \$[insert amount]. Failure to pay the renewal fee within the time prescribed shall result in automatic revocation of the license.
- C. The license shall be a limited license which allows solicitation only of viatical settlements.
- D. Prelicensing education and continuing education required of other agents and brokers in Section [insert section] shall not apply to viatical settlement brokers.

Drafting Note: Delete Subsection D if the state does not require prelicensing and continuing education.

E. A viatical settlement broker shall acquire and maintain an errors and omissions policy in an amount commensurate with the broker's exposure, satisfactory to the insurance commissioner.

F. The commissioner shall have the right to suspend, revoke or refuse to renew the license of any viatical settlement broker if the commissioner finds that:

- (1) There was any misrepresentation in the application for a license;
- (2) The broker has been found guilty of fraudulent or dishonest practices, has been found guilty of a felony or any misdemeanor of which criminal fraud is an element, or is otherwise shown to be untrustworthy or incompetent;
- (3) The licensee has placed or attempted to place a viatical settlement with a viatical settlement provider not licensed in this state; or
- (4) The licensee has violated any of the provisions of [insert citation to the Viatical Settlement Act] or this regulation.

G. Before the commissioner shall deny a license application or suspend, revoke or fail to renew the license of a viatical settlement broker, the commissioner shall conduct a hearing in accordance with [cite the state's administrative procedure act].

Section 3. Other Requirements for Brokers

- A. In the absence of a written agreement making the broker the viator's agent, viatical settlement brokers shall be presumed to be agents of viatical settlement providers.
- B. Viatical settlement brokers shall not, without the written agreement of the viator obtained prior to performing any services in connection with a viatical settlement, seek or obtain any compensation from the viator.

Section 4. Standards for Evaluation of Reasonable Payments

In order to assure that viators receive a reasonable return for viaticating an insurance policy, the following shall be minimum discounts:

Insured's Life Expectancy	Minimum Percentage of Face Value Less Outstanding Loans Received by Viator
Less than 6 months	[80%]
At least 6 but less than 12 months	[70%]
At least 12 but less than 18 months	[65%]
At least 18 but less than 24 months	[60%]
Twenty-four months or more	[50%]

The percentage may be reduced by [5%] for viaticating a policy written by an insurer rated less than the highest [4] categories by A.M. Best, or a comparable rating by another rating agency.

Section 5. Reporting Requirement

On March 1 of each calendar year, each viatical settlement provider licensed in this state shall make a report containing the following information for the previous calendar year:

- A. For each policy viaticated:
 - (1) Date viatical settlement entered into;
 - (2) Life expectancy of viator at time of contract;
 - (3) Face amount of policy;
 - (4) Amount paid by the viatical settlement provider to viaticate the policy; and
 - (5) If the viator has died:
 - (a) Date of death; and
 - (b) Total insurance premiums paid by viatical settlement provider to maintain the policy in force;
- B. Breakdown of applications received, accepted and rejected, by disease category;

- C. Breakdown of policies viaticated by issuer and policy type;
- D. Number of secondary market vs. primary market transactions;
- E. Portfolio size; and
- F. Amount of outside borrowings.

Section 6. General Rules

- A. With respect to policies containing a provision for double or additional indemnity for accidental death, the additional payment shall remain payable to the beneficiary last named by the viator prior to entering into the viatical settlement agreement, or to such other beneficiary, other than the viatical settlement provider, as the viator may thereafter designate, or in the absence of a designation, to the estate of the viator.
- B. Payment of the proceeds of a viatical settlement pursuant to [insert citation for Section 9D of Viatical Settlements Model Act] shall be by means of wire transfer to the account of the viator or by certified check.
- C. Payment of the proceeds pursuant to a viatical settlement shall be made in a lump sum. Retention of a portion of the proceeds by the viatical settlement provider or escrow agent is not permissible. Installment payments shall not be made unless the viatical settlement company has purchased an annuity or similar financial instrument issued by a licensed insurance company or bank.
- D. A viatical settlement provider or broker shall not discriminate in the making of viatical settlements on the basis of race, age, sex, national origin, creed, religion, occupation, marital or family status or sexual orientation, or discriminate between viators with dependents and without.
- E. A viatical settlement provider or broker shall not pay or offer to pay any finder's fee, commission or other compensation to any viator's physician, attorney, accountant or other person providing medical, legal or financial planning services to the viator, or to any other person acting as an agent of the viator with respect to the viatical settlement.
- F. Contacts for the purpose of determining the health status of the viator by the viatical settlement provider or broker after the viatical settlement has occurred should be limited to once every three (3) months for viators with a life expectancy of more than one year, and to no more than one per month for viators with a life expectancy of one year or less. The provider or broker shall explain the procedure for these contacts at the time the viatical settlement contract is entered into.
- G. Viatical settlement providers and brokers shall not solicit investors who could influence the treatment of the illness of the viators whose coverage would be the subject of the investment.
- H. Advertising standards:
 - (1) Advertising should be truthful and not misleading by fact or implication.
 - (2) If the advertiser emphasizes the speed with which the viatication will occur, the advertising must disclose the average time frame from completed application to the date of offer and from acceptance of the offer to receipt of the funds by the viator.
 - (3) If the advertising emphasizes the dollar amounts available to viators, the advertising shall disclose the average purchase price as a percent of face value obtained by viators contracting with the advertiser during the past six (6) months.

ATTACHMENT THREE-B

Viatical Settlement Working Group
of the Life Insurance (A) Committee
April 29, 1994

The Viatical Settlement Working Group of the Life Insurance (A) Committee met by conference call at 1:20 p.m. on April 29, 1994. Roger Strauss (Iowa) chaired the meeting. The following working group members participated: Mary Alice Bjork (Ore.); Rhonda Myron (Texas); and Bob Wright (Va.). Carolyn Johnson (NAIC/SSO) also participated in the call.

Roger Strauss (Iowa) suggested that the group discuss the comments that were received on the Viatical Settlement Model Regulation. The first item Mr. Strauss brought up was whether a surety bond should be required for the broker. Comments received said a bond was unnecessary because the broker is not the one handling the money. Bob Wright (Va.) asked if there was any advantage to requiring both the provider and the broker to have a bond. The response was that if the parties failed to

perform, the money would be available to pay the viator. Rhonda Myron (Texas) suggested that perhaps errors and omissions coverage would be more suitable for the broker. The working group agreed to include a requirement for errors and omissions coverage for the broker, and to move the requirement for the surety bond to the section on the viatical settlement provider. Mary Alice Bjork (Ore.) said that if there was misrepresentation the broker's errors and omissions coverage would provide a protection for the viator.

Mr. Strauss said another comment was that the funds be made available by wire transfer directly into the viator's account or by means of a certified check. The working group members agreed this was a good idea and added this requirement to the draft.

Mr. Strauss next drew the attention of the working group to one comment that suggested providing a specific exemption for employees of the viatical settlement company so that each employee was not required to get a license. The working group reviewed the definition of "viatical settlement provider" and decided that the definition already clearly provided that a license was not required for each employee of the company.

Another comment suggested putting in a provision that a viatical settlement company with a pending application could do business. The drafters hesitated to add this provision but did express interest in adding a drafting note that would grandfather in existing companies while their applications were being processed. The working group decided to add a drafting note to Section 1 of the regulation suggesting an effective date several months in the future to allow companies already in business to continue to operate while their applications were pending.

Mr. Strauss reported on a provision of the pending New York regulation that said if the viator died during the free-look period, the contract was deemed rescinded. After some discussion the working group decided implementation of this was too complicated so decided not to include that provision.

Mr. Strauss next turned to the issue that had received the largest volume of comment: Section 4 of the draft regulation, Reasonableness of Payment. He suggested that one alternative is to put in a reporting requirement instead of minimum discounts and after information had been gathered a provision with percentage amounts could be added. He listed several items that he thought are important to include in any kind of reporting requirement: (1) date viatical settlement entered into; (2) life expectancy at the time of the contract; (3) date of death; (4) face amount of policy; (5) amount paid by the viatical settlement company; and (6) premium payments required by the viatical settlement company before death occurred. One of the comments received had included a list of proposed information to be reported and the working group went through that list and decided to add to Mr. Strauss' list several more items: (1) breakdown of applications received, accepted and rejected by disease category; (2) breakdown of policies viaticated by issuer and policy type; (3) number of secondary market versus primary market transactions; (4) portfolio size in face value; and (5) amount of outside borrowings of the company. The working group considered whether it would be advisable to add a provision requiring disclosure of the amount paid in commissions but decided that it was not necessary to know the amount of individual expenses. The working group did not see that it was any more important to know what the commissions paid were than any of the other operating expenses of the viatical settlement provider.

Working group members discussed whether it was appropriate to include the percentages with minimum payouts. Mr. Strauss outlined three possibilities:

- (1) Reporting requirement only;
- (2) Leave standards that were in the March draft; or
- (3) Modify the percentages.

After considerable discussion the group decided to leave a minimum payout provision in the draft, but to go back to the percentages that had been included in the original draft proposed in February.

The next item for discussion was a suggestion to include a requirement for full payment of the amount agreed upon to the viator. The group decided to insert a provision requiring full payment of the agreed-upon amount without deductions of any kind. In addition, one commentator had pointed out that there was no requirement for a broker to serve as a broker only for a licensed company. That provision was added as well.

Mr. Strauss asked Carolyn Johnson (NAIC/SSO) to prepare a revised draft incorporating the decisions made during the conference call and to mail that draft to interested parties by the middle of May, and to invite further comments to be made at the summer National Meeting in Baltimore.

Having no further business the conference call adjourned at 2:20 p.m.

ATTACHMENT FOUR

Genetic Testing Working Group of the
Life Insurance (A) Committee
Baltimore, Maryland
June 12, 1994

The Genetic Testing Working Group of the Life Insurance (A) Committee met in Maryland A of the Stouffer Harborplace Hotel in Baltimore, Md., at 11:30 a.m. on June 12, 1994. A quorum was present and Robert Katz (Ohio) chaired the meeting. The following working group members or their representatives were present: Mary Alice Bjork (Ore.); Dixon Larkin (Utah); and Roy Olson (Wash.).

1. Adopt Minutes of April 15, 1994, and May 12, 1994, Conference Calls

Upon motion duly made and seconded the minutes of the April 15 conference call (Attachment Four-D) and the May 12 conference call (Attachment Four-C) were adopted.

2. Review Chart on State Actions on Genetic Testing

Robert Katz (Ohio) asked the members of the working group to review a chart prepared by the NAIC which illustrated state actions taken on the subject of genetic testing (Attachment Four-A). He said the working group would want to keep this chart up-to-date and asked interested parties to keep the working group informed of actions taken in other states.

3. Appointment of Technical Resource Advisors

Members of the working group agreed that it would be appropriate to appoint a group of technical resource advisors to assist in providing information about what companies are actually doing in the arena of genetic testing. Mr. Katz asked any individuals interested in participating in the group to communicate that information to Carolyn Johnson (NAIC/SSO).

4. Hearing to be Held at the Fall National Meeting

Mr. Katz announced that the format of the Genetic Testing Working Group at the fall National Meeting would be a hearing covering topics of interest in the area of genetic testing. Kip May (Ohio) said that in the hearing the working group would desire testimony on whether to test and what the parameters would be if testing were done. He said written responses and a three to five minute oral presentation would be greatly appreciated. Mr. Katz asked if other regulators had issues they would like to see discussed. Birny Birnbaum (Texas) said the issue of genetic testing was just a part of the greater question of how insurers group risks. He said the regulators need to consider the broader issue of rating factors. He suggested one issue for discussion at the hearing was "shall genetic testing be used as a rating factor in the sale of insurance?" Tom Foley (Fla.) asked if the working group wanted to consider the larger question of risk classification. He said the number of risk classifications may be greater than the number of age classifications. He asked if it was appropriate to move to broader rather than narrower groups. Roy Olson (Wash.) asked if the public was served by having more classes of risk. If there are more classes, the better risks get better rates, and he asked if this was a desirable result. He said that in more refined classes the effect of pooling of insurance was lost. Mr. Katz asked if it was good public policy to narrow or widen the classes, and asked that this issue be addressed in the testimony at the September meeting. He encouraged consumer representatives to testify at the meeting to present their viewpoint.

Next Mr. Katz opened the meeting to comments from the floor. Robbie Meyer (American Council of Life Insurance—ACLI) said she had prepared a packet of information for the members of the working group that illustrated the concerns of ACLI members. She said a definition of the term genetic testing was an important element when studying this issue. She said she looked forward to assisting the working group in its deliberations. Bill Weller (Health Insurance Association of America—HIAA) said that health insurers also were interested in this issue. Mr. May agreed that the health side was a very important part of this issue. Mr. Weller said that deciding what the definition of genetic testing was would also have a heavy bearing on what companies used in paying claims. Mary Alice Bjork (Ore.) said the definition of genetic testing was important to her also. She considered family history questions to be a way of gathering genetic information, and saw this as part of the issue.

Mr. Katz said that Mr. May would assume the day-to-day chairmanship of the working group from this point forward. He directed the attention of the working group members to an informational paper which had been prepared by Mr. May (Attachment Four-B). Mr. May said the paper was written for the State of Ohio's Working Group on Genetic Testing, but he had broadened its application so that it would point out the issues which were being considered by the working group. Mr. Foley asked that the State of Florida be added to the working group, and Mr. Katz agreed.

Having no further business, the Genetic Testing Working Group adjourned at 12:10 p.m.

ATTACHMENT FOUR-A

STATE POSITIONS ON ISSUE
OF GENETIC TESTING FOR INSURANCE COVERAGE

STATE	CITATION	PROVISIONS
California	Ins. § 10143 <i>SB 1146 pending</i>	No insurer shall refuse to issue or sell or renew any policy of life or health insurance solely by reason the person carries a gene which may be associated with disability in that person's offspring but which causes no adverse effects on the carrier. <i>Would prohibit refusal of coverage or discrimination in health insurance on the basis that the person carries a gene which may be associated with a disability in that person or the person's offspring.</i>
Colorado	<i>SB 58 pending</i>	<i>Prohibits health and disability underwriters from seeking genetic information.</i>
Florida	§§ 626.9706, 626.9707	No life or health insurer shall refuse to issue and deliver any policy of insurance solely because the person has sickle-cell trait.
Louisiana	R.S. 22:652.1	No insurer shall refuse to provide a policy of life insurance or health insurance solely because the applicant has sickle-cell trait.
Maryland	48A § 223	Insurer may not refuse to insure or make or permit any differential in ratings for life insurance solely because the applicant has a genetic trait which is harmless within itself unless there is actuarial justification for it.
Michigan	<i>HB 4398 pending</i>	<i>Amends Unfair Trade Practices Act to make it an unfair trade practice for an insurer to refuse to insure individual who refused to submit to genetic testing or to refuse to insure individual because of the results of genetic testing.</i>
Montana	§ 33-18-206	The rejection of an application or determination of rates based on a genetic condition is unfair discrimination unless the applicant's medical condition and history and either claims experience or actuarial projections establish that substantial differences in claims are likely to result from the genetic condition.
New Hampshire	<i>HB 1423 pending (interim study)</i>	<i>Prohibits genetic testing for insurance purposes.</i>
New Jersey	<i>AB 1333 pending</i>	<i>Prohibits discrimination on the basis of genetic testing results.</i>
North Carolina	§ 58-58-25	Insurer shall not refuse to issue or deliver any policy of life insurance solely by reason of the fact that the person possesses sickle cell trait or hemoglobin C trait, nor shall the policy carry a higher premium rate or charge by reason of the fact of the insured possesses the trait.
Ohio	§§ 1742.42 to 1742.43, 3901.49 to 3901.501	Insurers and HMOs shall not consider any information obtained from genetic testing in processing individual or group health insurance applications. Statute effective until the year 2004.
Tennessee	§ 56-7-207	Insurer shall not refuse to issue or deliver any policy of life insurance solely by reason of the fact that the person to be insured possesses sickle cell trait or hemoglobin C trait.
Wisconsin	§ 631.89	Insurer may not require or request any individual or a member of the individual's family to obtain a genetic test. Shall not condition the provision of insurance coverage or health care benefits on whether a genetic test has been performed or on what the test results are. Does not apply to life insurance or income continuation insurance.

ATTACHMENT FOUR-B

Ohio Department of Insurance
2100 Stella Court
Columbus, Ohio 43266-0566

GENETIC TESTING: ISSUES AND CONSIDERATIONS

Introduction

Amended Substitute House Bill 71 was passed by the Ohio General Assembly in late 1993 and took effect February 8, 1994. Basically, the bill prohibits HMOs, sickness and accident insurers, or governmental entities providing coverage on a self-insured basis from requiring, considering, or inquiring about the results of genetic testing in the process of providing people with health insurance. After 10 years, the statute will be repealed. The bill also establishes the Task Force on Genetic Testing in Health Insurance, comprised of legislators, industry representatives, consumer representatives, geneticists, and others to thoroughly examine the use of genetic tests in the underwriting practices of health insurers. As Ohio navigates a path through the issue of genetic testing there are considerations that must be taken into account, from an insurer's perspective, the consumer's perspective, and from a regulatory/public policy perspective.

I. Insurer Concerns with Genetic Testing

A. Fair Discrimination Perspective - One of the insurers' arguments against a ban on genetic testing is that if you do not allow insurers the use of genetic testing information they might withdraw from that line of business, spread the unanticipated costs to all of their customers, or be driven out of business by unforeseen claims.

B. Adverse Selection - Applicants for insurance are said to "adversely select" against an insurer when, without informing the insurer of any health problem, they acquire coverage based on their knowledge that they are in poor health. There is a general fear that people who have undergone testing and have tested positive for a genetic disorder will buy as much insurance as possible to cover their impending illness. Without access to the test results, an insurer may agree to provide coverage at a premium that does not reflect the actual risk. If an insurer then tries to spread these unanticipated losses to all its customers, they could run into problems with a state's unfair trade practices act. The end result is that what's at risk is the financial solvency of insurers. This is obviously of concern to all parties involved.

II. Consumer Concerns with Genetic Testing

A. Uninsurability - If insurers do require tests or have access to test results, consumers fear that a positive test for a genetic disorder may cause the insurer to charge a higher premium, add a rider to the policy excluding coverage for the disease for which the applicant was tested, or to deny coverage altogether. This could cause a situation where a majority of genetically challenged people will not be offered insurance or will not be able to afford what they are offered.

B. Confidentiality - When a person undergoes a genetic test, the results of the test become a part of their medical record. The insurer has access to insureds' medical records as an agreement in their contract and will thus become a part of the insurer's records. The information can also be passed on to the Medical Information Bureau where many insurers have access to it. There are arguments that one's genetic make-up is beyond control, and that persons should not be punished for involuntary conditions. Also, DNA is very stable and could be used for different purposes years later.

III. State Regulators Concerns with Genetic Testing

A. Health Care Options for High Risk Individuals - It is important from a public policy perspective to provide avenues for people to get health insurance if they are considered high risk. Some options now include Medicare, Medicaid, Blues Open Enrollment, HMOs Open Enrollment, Commercial Insurers Open Enrollment, and Trade Associations or professional groups.

B. Policy Options - There are several ways states can choose to react to the issue of genetic testing:

1. Moratorium on Genetic Testing - Suspension of the use of the results of genetic tests by all insurers to determine the eligibility of applicants for a certain amount of time.
2. Privacy Determinations - Assigns rights of privacy to genetic information and gives rights of ownership to person on whom the tests were performed.
3. Permit Insurers to Use Genetic Information
4. Ban Use of Genetic Information to Determine Insurance Eligibility

In the area of life insurance, there are strong cases to be made against a moratorium on genetic testing. In order to make a reasoned policy decision, it would be necessary to receive input from not only the insurance industry, but also the medical community.

There are also data considerations. Should the NAIC recommend model legislation or is the technology of genetic testing not well enough understood to make such a determination?

A final consideration would be the shape of things to come in health care reform. In terms of rating methodology, a loss-ratio scheme would limit the usefulness of genetic testing information since rates would be based on the amount of anticipated claims for a group divided by the total premium revenue for that group. The information would be even less useful in a modified community rating or pure community rating structure. The difference between what the best risk and the worst risk would pay in premiums would be narrowed, making obsolete any information used to underwrite an individual.

Conclusion

State regulators will have to gather information about existing and possible uses of genetic information by insurance companies and insureds that is unfair. Once a better picture of this issue is painted, states can then develop policy options for preventing unfair use of this information to protect both the solvency of the insurers and the rights of the individual. We welcome comments from any interested party regarding this subject.

ATTACHMENT FOUR-C

Genetic Testing Working Group of the Life Insurance (A) Committee May 12, 1994

The Genetic Testing Working Group of the Life Insurance (A) Committee met by conference call at 2 p.m. on May 12, 1994. Robert Katz (Ohio) chaired the meeting. The following working group members or their representatives participated: Don Koch (Alaska); Richard Rogers (Ill.); Mary Alice Bjork (Ore.); Dixon Larkin (Utah); and Roy Olson (Wash.). Carolyn Johnson (NAIC/SSO) also participated in the conference call.

Robert Katz (Ohio) said the purpose of the conference call was to review information gathered in response to the questionnaire sent to the states after the last conference call. He reminded the working group members that they had agreed to prepare a list and hear comments at the June meeting of the working group. Carolyn Johnson (NAIC/SSO) reported that only three comments had been received in response to the request for input. The working group discussed possible alternatives to preparing a list from state comments. Kip May (Ohio) said he was preparing a report for the State of Ohio and offered to broaden this report to make it useful to the working group and present it at the June meeting of the working group. Ms. Johnson offered to provide information on the genetic testing bills pending and adopted in the states. Don Koch (Alaska) said he was in the process of making a list of issues which he thought were important for discussion, and offered to forward those to Mr. May for inclusion in his document.

Mr. Katz said that the issue of genetic testing is a very broad issue and asked what the working group members thought their focus ought to be. Mary Alice Bjork (Ore.) said that her state's interest was in whether companies intended to use genetic testing to a greater extent and whether there should be standards. She wondered if there was an appropriate place for genetic testing in insurance underwriting, and if so, if there should be limits. Mary Jo Teer (Ill.) said that her state had never regulated companies' underwriting practices. She said her state would be in favor of a wait-and-see approach and, if the department got consumer complaints, it would determine an appropriate level of regulation. Ms. Bjork said she thought that it would be a good idea to gather a group of technical advisors who would be able to determine what genetic testing was being used today by the industry, and what might be expected in the future. Members of the working group agreed that it would be appropriate to have a group of technical advisors provide this information and the working group would use it as part of the discussion at a hearing to be held at the fall National Meeting in Minneapolis. This would assist the NAIC in determining whether it was appropriate to recommend limits on genetic testing.

Having no further business, the Genetic Testing Working Group adjourned at 2:25 p.m.

ATTACHMENT FOUR-D

Genetic Testing Working Group Life Insurance (A) Committee April 15, 1994

The Genetic Testing Working Group of the Life Insurance (A) Committee met by conference call at 2 p.m. on April 15, 1994. Robert Katz (Ohio) chaired the meeting, and the following working group members or their representatives participated: Don Koch (Alaska); Richard Rogers (Ill.); and Mary Alice Bjork (Ore.). Carolyn Johnson (NAIC/SSO) also participated.

Robert Katz (Ohio) introduced William "Kip" May (Ohio), who is chair of the Ohio Task Force on Genetic Testing; Mr. Katz said that Mr. May would serve as Ohio's representative and chair of the working group, and Mr. Katz would assist Mr. May and continue to represent the working group to the Life Insurance (A) Committee. Mr. Katz said the purpose of the conference call was to analyze what the working group should do for the June meeting and beyond.

Mr. Katz referred to a memo he had prepared that listed some possible issues to discuss. Mary Alice Bjork (Ore.) suggested adding another issue, which is to consider the role of the family history application questions. She said it appears that use of the family history could be construed as a form of genetic underwriting. Mr. May pointed out that adding family history would broaden the scope of the issue considerably.

Don Koch (Alaska) suggested making a list with bullets of information; a list of the implications, pro and con, of genetic testing. Mr. Katz asked if the working group thought it appropriate to prepare a "white paper" for the June meeting with the major implications of testing, and a hearing in September to receive comments on the paper. Mr. Koch said that, to him, a "white paper" implied a list of solutions and he did not think the working group would be prepared with that yet by June. He suggested instead the development of a list of questions to which the working group would seek answers.

The working group decided to prepare a survey for inclusion in the electronic E-News that the NAIC sends to all states. The survey questions decided upon were: (1) Do you have a statute on genetic testing? (2) Do you have a bill or regulation pending? (3) If you answered in the affirmative to (1) or (2), what position do you take? (4) What questions do you have, or what implications do you see to genetic testing?

Chuck Budinger (Ill.) asked if the working group was supposed to limit itself only to consideration of life insurance issues. Carolyn Johnson (NAIC/SSO) informed the group that the issue had been part of the Accident and Health Insurance (B) Committee charges, but considering the workload of the B Committee, the charge was moved to the A Committee. She suggested that the chair report on this working group's progress to the Accident and Health Insurance (B) Committee and refer any issues specific to health insurance to the B Committee. Mr. Katz said that a joint committee might be appropriate, once the working group has identified the implications of this topic.

The working group decided to hold another conference call May 13 to consider the responses to the questionnaire and to prepare for the June meeting.

Having no further business, the Genetic Testing Working Group adjourned at 2:40 p.m.

ATTACHMENT FIVE

Synthetic GIC Working Group of the Life Insurance (A) Committee Baltimore, Maryland June 14, 1994

The Synthetic GIC Working Group of the Life Insurance (A) Committee met in Maryland A of the Stouffer Harborplace Hotel in Baltimore, Md., at 10:30 a.m. on June 14, 1994. A quorum was present and Robert M. Willis (D.C.) chaired the meeting. The following working group members or their representatives were present: Larry Gorski (Ill.); and Salvatore R. Curiale (N.Y.).

Commissioner Robert M. Willis (D.C.) said the purpose of the presentation was to learn more about synthetic guaranteed investment contracts (GICs). He said regulators needed to understand the product and its implications for state regulation. He introduced a panel of presenters: Brian Haendigen (Aetna); William Smith (DuPont); Larry Mylnechek (GIC/Stable Value Association); Joel Coleman (Providian); Victor Gallo (PRIMCO); and John Mercier (Turco and Mercier). Commissioner Willis said the format of the meeting would be a presentation by the panel and then time for questions. He introduced Mr. Mylnechek, who explained that the GIC/Stable Value Association was a non-profit association, active in the stable value marketplace. He said the mission of his association was to educate the marketplace. He said the purpose of the panel was to provide current information to NAIC members regarding the synthetic GIC market, to explore issues related to investment risks, legal framework and market demand for various synthetic GIC products, and to establish a dialog and framework for further sharing of information and ideas.

Mr. Gallo gave an overview of the marketplace by describing traditional GIC products and security-backed investment products. He said the term "synthetic GICs" refers only to products where the underlying investments (bonds) are held in a custodial account in the name of the plan. He said the product began in the early 1990s, with an interest in diversification and concern about insolvencies like Executive Life and Mutual Benefit Life.

Mr. Smith spoke as a manager of a large synthetic GIC fund. He explained what was driving the demand for synthetics and explained his viewpoint of the impact of excluding insurance companies from the market. He said large investors needed more synthetic GIC products available to provide for investment diversification.

Mr. Mercier gave a legal analysis of the product. He provided information on the background of synthetic GICs. He said synthetic GICs are issued by banks, insurers and other financial institutions. He said the synthetic GIC contract issued by an insurer is typically in the form of a group annuity contract, an investment management agreement, a securities purchase or repurchase agreement, a swap, or a liquidity of line of credit agreement. He also discussed briefly whether or not there were financial guarantee issues to be considered. Mr. Coleman gave an actuarial viewpoint. He said as structured, most synthetic GICs were not as risky as traditional GICs. He analyzed the various types of risks and how they applied to the synthetic GIC product. Mr. Haendigen summarized the points made by the other members of the panel. He said the need for synthetic GICs is real and likely to endure. He said insurers such as his company were interested in writing that type of market, and he summarized why he thought the risks were manageable.

Commissioner Willis next asked if any regulators had questions. Superintendent Sal Curiale (N.Y.) announced that, within the next few weeks, the state of New York would issue a circular letter saying that synthetic GICs are not an authorized life insurance product in the state of New York. He said this would apply to New York's licensed companies and domestics and meant that they would not be allowed to issue synthetic GICs. He said that New York had not found that the product was substantially similar to existing products due to the non-ownership of the asset. In his opinion, because of the Employee Retirement Income Security Act (ERISA), state regulators are virtually powerless to impose the types of regulation needed. He said contractual protection might evaporate because of the leverage of a large company wanting to purchase the product. Superintendent Curiale also asked why plan sponsors were so anxious to absorb additional risks. Mr. Smith responded that it was actually the participants that absorb the risk. He said his company tried to explain this to investors. Superintendent Curiale asked if the investment could be done with a separate account. Mr. Smith responded that it could, but it was not as safe for the fund as a synthetic GIC product. Superintendent Curiale asked if Mr. Smith would agree that it was difficult for regulators to write a regulation when there was no ownership of the asset. Mr. Smith responded that that question was difficult to answer.

Commissioner Willis asked if it was true that in the case of a loss of book value, the plan participant suffered the first loss, and only to a point defined in the contract when the general fund of the insurer suffered. Mr. Smith responded that this depended on the contract structure. An experience-rated contract meant that if the market value was less than the book value, the interest rate would be reset. In effect, the risk was the participant's because they would get a lower rate of return. A non-experience-rated contract provided for the wrap provider (the insurer or other synthetic GIC provider) to make up the difference.

Larry Gorski (Ill.) stated that Illinois recognized there were risks in these types of contracts. He said he was not comfortable with the investment guidelines section of the contracts he had reviewed. He said Illinois had concerns about the riskiness, but saw this as part of the evolution of the market. He felt that the products can be sold by life insurance companies, but he would like to see a regulatory framework established.

Commissioner Willis thanked the panelists for their information and said the working group was now ready to move to the next level: consideration of the regulatory issues presented by the synthetic GIC product.

Having no further business, the Synthetic GIC Working Group adjourned at 12:45 p.m.