

LIFE INSURANCE (A) COMMITTEE

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Dwight K. Bartlett III, Chair—Md.
Kerry Barnett, Vice Chair—Ore.

CONTENTS

Life Insurance (A) Committee Sept. 12, 1995, Minutes	673
Life Disclosure Working Group Report (Attachment One).....	676
Life Insurance Illustrations Model Regulation (Attachment One-A).....	679
Memo Regarding Concerns with Current Draft Proposal Life Insurance Illustrations Model Regulation (Attachment One-B).....	688
Genetic Testing Working Group Sept. 10, 1995, Minutes (Attachment Two)	689
Viatical Settlements Working Group Sept. 11, 1995, Minutes (Attachment Three).....	689
Ad Hoc Working Group on Annuities Sept. 11, 1995, Minutes (Attachment Four)	691

MINUTES

The Life Insurance (A) Committee met in Salon D of the Marriott Hotel in Philadelphia, Pa., at 10 a.m. on Sept. 12, 1995. A quorum was present and Dwight K. Bartlett III (Md.) chaired the meeting. The following committee members or their representatives were present: Kerry Barnett, Vice Chair (Ore.); Terri Vaughan (Iowa); James H. Brown (La.); Christopher P. Krahling (N.M.); Jim Long (N.C.); Elton Bomer (Texas); and Robert E. Wilcox (Utah).

1. Report of the Life and Health Actuarial Task Force

Jerry Fickes (N.M.) reported that the Life Nonforfeiture Working Group is developing a plan that is a substantial change from the current nonforfeiture practice. This is a long-term project, requiring a large commitment of time. He said the Task Force would like permission to request a 10-minute time slot at the Commissioners Roundtable at the Winter National Meeting to explain this theory to all of the commissioners.

He said the other action item for the Life Insurance (A) Committee was a question-and-answer document on the Life and Health Reinsurance Agreements Model Regulation. Mr. Fickes said the document had been under development for more than a year and a half and had received considerable exposure. He said that it had been developed in response to many questions about interpretation of the Life and Health Reinsurance Agreements Model Regulation, and the Task Force believed it was most appropriate to attach this to the NAIC's model in the NAIC's *Model Laws, Regulations and Guidelines*, as additional guidance. Mr. Fickes explained that the Life and Health Actuarial Task Force had adopted the document and suggested that the Life Insurance (A) Committee allow a period for further comments and consider whether this document should be attached to the Life and Health Reinsurance Agreements Model Regulation.

Upon motion duly made and seconded, the report of the Life and Health Actuarial Task Force was received, and the Committee concurred with the recommendations made by the Task Force.

Julie Spiezio (American Council of Life Insurance—ACLI) requested that the A Committee consider an ACLI suggestion that it would be more appropriate to include the question-and-answer document as an appendix to Chapter 24 of the *Accounting Practices and Procedures Manual*, which had just been adopted by the Accounting Practices and Procedures Task Force. She said from the perspective of the ACLI, if the question-and-answer document were added to the Life and Health Reinsurance Agreements Model Regulation, it would serve as a modification of the regulation. Commissioner Dwight Bartlett (Md.) asked if the Life and Health Actuarial Task Force had considered this location. Mr. Fickes responded that the Task Force had, but felt that the document would be more readily available if attached to the Life and Health Reinsurance Agreements Model Regulation, but the Task Force would defer to the judgment of the A Committee. Commissioner Bartlett asked that comments for the A Committee regarding this issue be sent to Carolyn Johnson (NAIC/SSO) by Oct. 15, 1995.

2. Report of the Life Disclosure Working Group

Commissioner Robert E. Wilcox (Utah) reported that after more than two years of hard work, the Life Disclosure Working Group was pleased to recommend a proposed model law to the Life Insurance (A) Committee. He explained that the attached Life Insurance Illustrations Model Regulation is to cover non-variable life, with an exclusion for small policies. He said the Working Group now intends to move directly to consideration of variable life insurance policy illustrations so that there would be consistency between variable and non-variable life. Commissioner Wilcox explained that the new model contains provisions to be used in conjunction with the actuarial standard of practice being developed by the Actuarial Standards Board (ASB). He pointed out that the actuarial standard of practice is really a compliance guideline that tells actuaries how to comply with the state laws based on the NAIC's Life Insurance Illustrations Model Regulation. Commissioner Wilcox said the working group had received outstanding cooperation from the ASB.

Commissioner Wilcox said that at the heart of the NAIC's Life Insurance Illustrations Model Regulation was "disciplined current scale" and behind that was the actuarial certification. He said it would empower the actuary to bring discipline to the illustration process and prohibit unrealistic expense assumptions. Commissioner Wilcox said the Working Group had discussed extensively persistency bonuses and how to eliminate illustration of them, but found this very difficult. The Working Group decided that the most egregious practices would be eliminated by the definition of self-support and lapse-support and deleted the prohibition on illustration of persistency bonuses.

Commissioner Wilcox said the treatment of expenses is another difficult area. The Working Group recognized that new companies would have high expenses not covered by the policy premium. Recognizing the need for some flexibility, the Working Group agreed to the ASB suggestion to allow illustrations based on one of three levels of expense: fully allocated expenses, which the Working Group felt most comfortable with; marginal expenses, which include the direct expenses of the product but no overhead, as long as they are not less than a table created from industry averages for fully allocated expenses. The Life Insurance Illustrations Model Regulation includes a requirement that the company disclose the choice of expense allocation to both the regulator and the applicant.

The Life Insurance Illustrations Model Regulation requires the board of directors to designate an illustration actuary, who will certify the scale used in the illustrations. Certification also is required by a company officer that the illustration complies with the format of the regulation. The agent also is required to sign the illustration, saying that he or she has not made any statements that would be inconsistent with the illustration, and the consumer acknowledges that he or she was told that the figures illustrated are not guaranteed. Commissioner Wilcox said the Life Insurance Illustrations Model Regulation provides good flexibility to use supplemental illustrations, such as split-dollar, as long as they were consistent with the basic illustration.

Commissioner Wilcox said that he thought that consumers would find themselves in a better position to understand the policy illustrations than they were before. He cautioned that the Working Group's project is not complete and pointed out concerns raised by two members of the Working Group (Texas and California) that would still need to be addressed. He said some of the concerns raised by these states appealed to the other members of the Working Group, but the regulators recognized that it would be hard to get the Life Insurance Illustrations Model Regulation adopted in some states if their suggestions were included. Ted Becker (Texas) said that his state has concerns about the model and would not vote for its adoption. He said that his concerns had been summarized in a memo to Commissioner Wilcox attached to the Working Group's minutes.

Scott Cipinko (National Alliance of Life Companies—NALC) opined that significant changes had been made to the Life Insurance Illustrations Model Regulation in the last month, and more time is needed for comment before the Life Insurance (A) Committee adopted the model. Tony Spano (ACLI) agreed the model is complex and the disclosure requirement added to Section 6A(8) needs further review. He recommended that the A Committee defer action until the Winter National Meeting.

Mary Griffin (Consumers Union) also expressed concerns. She said her concerns had been voiced again and again, and she was disappointed in some of the changes made to the Life Insurance Illustrations Model Regulation at the August meeting. She said it seemed that her concerns were not responded to, and she asked for further time to review the model.

Commissioner Bartlett asked Commissioner Wilcox to speak to the concerns being voiced about recent changes made in the Life Insurance Illustrations Model Regulation. Commissioner Wilcox said that the timing issue was critical in the development of the model. He said the Working Group had been very open to comment and had reviewed the model in response to the comments received. He said the Working Group had agreed to a delayed effective date of Jan. 1, 1997, because the insurance industry said it needs a significant period of time in which to make programming changes. The postponement of a decision until the Winter National Meeting in December would mean the Life Insurance Illustrations Model Regulation would not be up for adoption by the NAIC until March, and he said there is a crying need to get this model out to the states to protect the public. Commissioner Wilcox pointed out that the changes made in the last month respond to concerns that the industry had raised. He said the most significant change was to drop the persistency bonus prohibition as the Working Group had been requested by the insurance industry. Commissioner Wilcox suggested that if further amendments were needed and brought to the working group's attention, the Life Insurance (A) Committee could have a conference call before the Winter National Meeting to agree on any necessary changes, and the Life Insurance Illustrations Model Regulation could still be brought before the Plenary at the December meeting. Tom Foley (Fla.) pointed out that the changes made in the model most recently were an accommodation to the industry. To remain in sync with the ASB, the Life Insurance Illustrations Model Regulation needs to be moved forward.

Upon motion duly made and seconded, the Committee adopted the Life Disclosure Working Group report, including the Life Insurance Illustrations Model Regulation, with Texas abstaining (Attachment One).

3. Report of the Genetic Testing Working Group.

Dixon Larkin (Utah) reported that the Genetic Testing Working Group had considered language for a letter to Sen. Nancy Kassebaum (R-Kan.), in response to a request for information on whether genetic testing or family history are included within company underwriting. Dr. Larkin also said the Working Group had divided responsibility for a first draft for a white paper on genetic testing and expects to have a draft to present at the Winter National Meeting. Upon motion duly made and seconded, the report of the Genetic Testing Working Group was received (Attachment Two).

4. Report of the Viatical Settlements Working Group

Commissioner Glenn Pomeroy (N.D.) reported that the Viatical Settlement Working Group met in Philadelphia to share information. It discussed a recent Securities and Exchange Commission case, federal tax legislation currently pending, and developments in the various states. He said it appeared likely from the states' comments that, as states used the NAIC's models, it might be necessary to develop amendments to them. He said if that were the case, the Working Group would be asking for an expanded charge for 1996. Upon motion duly made and seconded, the report of the Viatical Settlements Working Group was received (Attachment Three).

5. Report of the Ad Hoc Annuity Working Group

Mr. Fickes reported that the working group had decided to develop a questionnaire to send to the states to gather information on their use of the NAIC's various annuity laws. Questions would be asked to determine whether any of the model laws need to be changed, what problems exist in the states, and what new models might need to be developed. Mr. Fickes said the Working Group plans to deliver a recommendation to the A Committee at the Winter National Meeting. Upon motion duly made and seconded, the Ad Hoc Annuity Working Group report was received (Attachment Four).

Having no further business, the Life Insurance (A) Committee adjourned at 11 a.m.

Dwight K. Bartlett, Chair, Md.; Kerry Barnett, Vice Chair, Ore.; Terri Vaughan, Iowa; James H. Brown, La.; Drew Karpinski, N.J.; Chris P. Krahling, N.M.; Jim Long, N.C.; Elton Bommer, Texas; Robert E. Wilcox, Utah

ATTACHMENT ONE

Life Disclosure Working Group Report

The Life Disclosure Working Group of the Life Insurance (A) Committee met in Snowbird, Utah, on Aug. 21-22 and in Philadelphia, Pa., on Sept. 9, 1995, to consider comments and testing results relative to the draft Life Insurance Illustrations Model Regulation. Commissioner Robert E. Wilcox (Utah) informed the participants in the meeting that the working group intended to make final changes to the draft and recommend it to the Life Insurance (A) Committee at the Fall National Meeting. Also participating in the deliberations were: Tom Foley, Vice Chair (Fla.); Don Koch (Alaska); Sheldon Summers (Calif.); Roger Strauss (Iowa); Lester Dunlap (La.); Martin Carus (N.Y.); Tony Higgins (N.C.); and Ted Becker (Texas).

Commissioner Robert E. Wilcox (Utah) said one suggestion had been to delete the word "sales" from the title, since the model also deals with in-force illustrations. The working group agreed to this change. Then the group reviewed the draft section-by-section to respond to the comments they had received.

Section 1. Purpose

The working group considered whether it was advisable to retain the phrase "as far as possible" in reference to elimination of the use of footnotes, but decided to retain that phrase because it stated as a goal the intent to eliminate the use of footnotes.

Section 2. Authority

It was suggested to the working group that there might be states that do not have authority under their existing statutes to adopt this regulation. Commissioner Wilcox opined that there would, at most, be only a few states that would need enabling legislation so no change was made to this section.

Section 3. Applicability and Scope

Tom Foley (Fla.) suggested that the section as drafted seemed confusing because it said the regulation applied to *all* group and individual policies and then in Subsection B that it did not apply to certain kinds of individual and group life insurance policies. He suggested a rephrasing to itemize the types of coverage that were not included under the regulation, and the working group agreed with his suggestion.

The working group considered but discarded a suggestion to add the word "cumulative" to describe the \$10,000 limit. After examination of other sections it was decided that it was not within the terms of the model to divide a policy into a number of smaller policies not exceeding \$10,000 in order to be exempted from the regulation. To clarify that issue, the phrase "on any individual" was added before the \$10,000 limitation.

Section 4. Definitions

The working group spent a considerable amount of time discussing the definition of "disciplined current scale" and issues related to that definition. Mr. Foley suggested adding a definition of "illustrated scale" and taking out the second sentence of the definition of disciplined current scale as being no longer necessary. At a suggestion from the meeting attendees, the working group decided to include a 95-day window in which the company could change its scale and included that in a definition of "currently payable scale." The working group was requested to add language creating a 95-day window in the "illustrated scale" definition, because of a concern that a scale could not be used by an actuary until after it had been certified. Instead, a change was made to the definition of disciplined current scale to clarify that the scale must be certified annually.

The working group also considered comments that suggested too much authority was being delegated to the Actuarial Standards Board (ASB) and reviewed various sections of the model to determine whether more authority needed to be spelled out in the regulation. Commissioner Wilcox pointed out that the insurance department regularly delegates authority for some of its functions, for example, most state laws require companies to prepare the annual statement in accordance with the NAIC's annual statements instructions. To address antitrust concerns raised by the American Academy of Actuaries (AAA), Subsection D was revised to add the four paragraphs conditioning reliance on the actuarial standards upon compliance with various provisions of the model.

Commissioner Wilcox said it was to the benefit of regulators to delegate the actuarial details of the calculation to the ASB. He also pointed out the importance of states adopting language as close to the model as possible. He said the actuarial standard applied to the extent a state law followed the NAIC model, and he did not think it was productive to spend time deciding if a law was substantially similar to the NAIC model. The working group also discussed what procedures would be necessary if the ASB did not adopt the actuarial standard. After consideration of placing alternative language in the model, the working group decided that if the actuarial standard was not adopted, extensive changes would be necessary to include calculation instructions in the model. In this case a re-visiting of the model regulation would be necessary.

Mr. Foley queried the other members of the working group as to whether a company that only wished to illustrate guaranteed elements would be required to follow the standards of the model. The working group members agreed that the definition of illustration would not apply to an illustration of only guaranteed elements, so such an illustration was not covered by the model regulation.

Technical resource advisors suggested adding a definition of in force illustration to clarify to what extent the requirements of a basic illustration also applied to the in force illustration. The working group agreed this was a good idea and discussed which of the requirements of a basic illustration should apply to an in force illustration.

Mr. Foley suggested removing the definition of persistency bonus and other sections related to persistency bonuses from the model. His reason was that at this point the definition of lapse support and the testing provided in the actuarial standard of practice would eliminate most abuse. He said that the three definitions being considered by the working group all generated a significant number of false results, and suggested that it was not possible to arrive at a good definition to recommend to the Life Insurance (A) Committee at this time. Other members of the working group agreed that the definition was difficult. Roger Strauss (Iowa) said that he preferred not to have any persistency bonus illustrated, but he would vote in favor of elimination of the requirements because most of his concerns had been addressed and he thought it was necessary to move forward. Ted Becker (Texas) had reservations but, some of his concerns were reduced by the addition of a phrase to Section 7E(3).

To deal with the issue of group insurance, a definition of "group universal life" was added. This would coordinate with Section 5D. At the Fall National Meeting in Philadelphia, the working group considered suggestions to expand the definition and Section 5D to include qualifying individual products marketed through association groups and other permitted groups, but did not add other types of coverage because it would expand the model considerably. Tony Higgins (N.C.) reminded those in attendance that at the Utah meeting in August, the working group had intended to refer only to employer groups, but had compromised on a broader definition.

Section 5. Policies to be Illustrated

The working group considered changes to Subsection A but decided to leave the section as it was. One of the suggestions was to define policy form but it was decided that the term did not need defining; it was a term of art. Mr. Becker said that he would prefer that anything with a separate number was considered a separate policy form. He was concerned that the company would have the right to decide what a policy form was.

The working group discussed whether Subsection B prohibited a company that had designated a form to be marketed without an illustration from giving out an in-force illustration. To prevent this result, the phrase "prior to the first policy anniversary" was added after the word "form." It was suggested that this might conflict with the replacement regulation, and Commissioner Wilcox asked Carolyn Johnson (NAIC/SSO) to review the replacement regulation and add a drafting note if required.

Mr. Higgins suggested adding to Subsection C that this exemption applied only if it was employer-paid coverage. George Coleman (Prudential) clarified that this provision was meant to exempt corporate-owned life insurance, which is paid by the employer, so the addition was not necessary. Mr. Coleman asked the working group to consider a suggestion from technical resource advisors that granted a broader exemption for group universal life. He explained that generally a generic illustration was provided, and few enrollees paid in more than the cost of insurance. He also pointed out that no agent was involved. The technical resource advisors suggested that delivery of an individualized illustration be optional with the requirement that the applicant request an illustration before one would be delivered. The working group agreed to add a Subsection D that said those who received an illustration for a group policy could receive a generic illustration, and those who purchased the policy would get a personalized illustration if a premium was paid high enough to build up values in the policy. In addition, anyone who wished a personal illustration could ask for it. If the policy was individually marketed, every enrollee would get a basic illustration, and the rules requiring a diligent effort to get a signature would apply.

Section 6. General Rules and Prohibitions

Mr. Foley suggested that Subsection C needed a great deal of work. He said traditional companies have not wanted to separate the components, but in a universal life policy the interest rate was broken out. Commissioner Wilcox reminded those in attendance that Subsection C had been added because of a concern of the working group members that any interest rate shown on the illustration could be manipulated and the requirement to use the interest rate underlying the disciplined current scale was an attempt to reduce that manipulation. Several in attendance pointed out difficulties with complying with this model and the Universal Life Model Regulation and its requirements. Commissioner Wilcox agreed that there was not an easy solution to this because of the requirements in the universal life regulation. The working group agreed on revised language for Subsection C.

Section 7. Standards for Basic Illustrations

During the discussion, the working group members realized there was no requirement in the model for a date on the illustration, and they agreed an illustration should indicate the date it was prepared.

The working group members were questioned by the audience about the mid-point for the numeric summary since the illustrated scale concept has been added. There was confusion as to what mid-point should be used and whether that mid-point would shift each time a different illustrated scale was used. The language of Subsection C was clarified to use the term "illustrated scale" in place of "disciplined current scale" where this created confusion.

Mr. Higgins said he was convinced by the comments to the working group that Subsection E should be changed in regard to term life policies. He suggested adding a phrase that allowed term to be shown for years 1-20, and each five years beyond that and any years in which the premium outlay changed, and the working group adopted the suggestion.

After hearing a comment that Paragraph (1)(a) would allow great deviation if the premium outlay was paid monthly and illustrated on an annual basis, the working group members agreed to eliminate that problem by adding the words "and mode" after the words "premium outlay."

Paragraph 2 of Subsection E was revised by dividing it into two paragraphs and changes suggested by Mr. Becker were added to limit the illustration of non-guaranteed elements to only those described in the contract. Mr. Becker suggested this modification so that persistency bonuses could only be shown if they were described in the contract.

Section 8. Standards for Supplemental Illustrations

Mr. Higgins voiced concern that illustration of an insurance product would be combined with illustration of, for example, a mutual fund. He thought it was important that this not be allowed and questioned whether wording needed to be added in Section 8. After review of the rest of the regulation, the working group members agreed that the illustration contemplated in this model referred only to life insurance and a complying illustration would not include a mutual fund. Judy Faucett (Coopers & Lybrand), an NAIC consultant, asked if it was appropriate to combine term and whole life, for example, in an illustration. Working group members agreed that this was appropriate in a supplemental illustration.

Section 9. Delivery of Illustration and Record Retention

The working group received a considerable number of comments about Subsection C and its signature requirement. Those in attendance expressed discomfort with the vague nature of the diligent effort required. There was also concern that the insurer had no legal recourse if the signed copy was not returned. The working group adopted a suggestion for a revised Subsection C that included instructions for the applicant to sign a duplicate copy of the numeric summary page of the illustration and return it to the insurer. The revised subsection also included a safe harbor provision for diligent effort.

Section 10. Annual Report: Notice to Policy Owners

The working group members accepted a suggestion to add a Paragraph (3) to Subsection A exempting policies without nonforfeiture values from the requirement to send an annual report each year, even if no changes had occurred.

The working group extensively discussed the requirements for an in force illustration. The working group agreed to replace Subsection C with a revised section that described the standards applicable to an in force illustration. At the same time, the working group decided a definition of an in force illustration was appropriate, and it was also added to Section 4.

Section 11. Annual Certifications

Subsections A and B were revised by reversing the order and clarifying that the illustration actuary certified to the scales used in the illustration.

The working group agreed to add a sentence to Subsection C requiring disclosure by the illustration actuary if the currently payable scale had been reduced during the past five years for reasons other than changes in the experience factors underlying the disciplined current scale.

Subsection F was revised to clarify that the officer certified that the format followed the requirements of the regulation and that the scales used were those certified by the actuary.

A suggestion was made that Subsection G be changed to allow the insurer to determine the date for filing its annual certification, rather than having that date prescribed by the commissioner, because this would be more useful for companies that were not on a calendar year. The working group agreed to this change.

Other Issues

In addition to review of the proposed model regulation, the working group held a joint meeting with the ASB in Utah, to resolve issues and answer questions from that group that had arisen during its development of the actuarial standards of practice. Ed Silins (Coopers & Lybrand), chair of the ASB Life Committee, said the committee had several questions on which it desired input from the working group. The most difficult issue being addressed was the expense assumptions included in disciplined current scale. The working group had indicated a desire to allow illustration only of fully allocated expenses, but for new companies and startup lines of business this created a problem. Typically, for this type of business marginal pricing was utilized. To give some control over illustrations based on marginal pricing, the ASB suggested a new category of expense assumptions based on generally recognized expense studies. Mr. Silins said that at least two such studies had been done, one by Milliman & Robertson and the other by Tillinghast. Mr. Silins explained that, when a company fully allocates the expenses, that means that the expenses of that line plus a share of the overhead costs are allocated to that policy form and would be reflected in the illustration. Companies recognize that a new line of business might not be able to fully carry its share of overhead, so often marginal pricing is used, which does not allocate the full share of overhead to the costs being included in the calculations for the illustration. To put a limit on illustrations based on marginal pricing, the ASB suggested using the studies of industry averages of fully allocated expenses as a floor for the pricing.

After considerable discussion, the members of the working group were persuaded that, if the generally recognized expenses were placed into a table that was subject to approval by the NAIC membership or the commissioner, this would be a workable solution. Gary Corbett (ASB) said that he recognized that the ASB would have to look at antitrust issues, but he thought it was the job of ASB to define the criteria used in developing the table. He suggested the Academy of Actuaries or Society of Actuaries develop the table. Commissioner Wilcox asked if it was possible to have the table developed before the regulation became effective, and Mr. Corbett said that he did not find July 1, 1996, to be an unreasonable date because of the studies that had already been done. The working group spent some time discussing whether this was an inappropriate delegation of authority by the insurance commissioner. Larry Gorski (Ill.) said that in his state a regulation that delegated authority was not generally approved, but he thought this might be similar in concept to the risk-based capital formula, which was developed by the NAIC.

Commissioner Wilcox pointed out that, if there are expenses that are not being considered in the illustration, it is important that consumers not be misled. He said disclosure was a crucial part of this proposal. The working group spent a considerable amount of time on drafting a disclosure statement to be included in the illustration, but was unsuccessful. The group voted to require disclosure in the actuarial certification to the commissioner and added a consumer disclosure requirement to Section 6A.

The second issue Mr. Silins brought before the working group was the provision in the actuarial standard of practice that referred to incidental subsidies in expense aggregation. He said that it was difficult to define "incidental" and suggested removing this reference. Mr. Gorski agreed that defining incidental would be a never-ending task and said that the weighting requirements in the aggregation formula would serve the same purpose.

The ASB committee drafting the standard of practice recommended that policies without nonforfeiture values not be included in the lapse support test. Mr. Corbett said that their inclusion produced false results and Commissioner Wilcox pointed out that since terminating policyholders take nothing with them, this would have no effect on the policyholders regulators were trying to protect. The working group agreed with this suggestion from the ASB.

Mr. Silins said that for multiple life policies the 15-year test of self-support was too short. He said that for multiple life policies, such as second-to-die, a 20-year test period would be more appropriate. Reluctantly the working group agreed with the recommendation when the multiple life policy paid at the later death.

After making several technical amendments, the working group voted to adopt the model (Attachment One-A) by a vote of six in favor, with Texas and New York abstaining, and California voting no. Commissioner Wilcox offered California and Texas an opportunity to attach an explanation of how the model should be changed in order for them to support it (Attachment One-B). (New York declined to participate in the vote because it was new to the working group.)

Variable Life Insurance Illustrations

The working group decided to proceed with consideration of variable life insurance and the illustrations appropriate to that product. One question to be decided was whether to add to the current model for variable life or to start over with a new document. Martin Carus and Bill Carmello (N.Y.) reported on the regulation under development in New York, which includes variable life. Mr. Carmello said that New York's draft regulation sets an arbitrary illustration of 0%, 4% and 8% for variable life, and requires compliance with state and federal law, to the extent possible. The working group and members of the audience spent some time in discussing the information available on federal requirements for variable life insurance illustrations. Mr. Foley asked Frank Irish (ASB) if the Actuarial Standards Board would be able to develop a standard of practice for variable life insurance. Mr. Irish responded that it would be possible to do so, however, it would have to go through a full exposure process which would probably take a year. Mr. Higgins suggested that perhaps it would be appropriate to reconstitute the working group with members who were more knowledgeable about variable life insurance. Mr. Foley responded that it was important to maintain uniformity between the treatment of variable life and non-variable life insurance, and he thought it was important that the current members of the working group continue their participation. It was the consensus of the working group to start the drafting process using the current model and adapting it for variable life insurance illustrations.

ATTACHMENT ONE-A

LIFE INSURANCE ILLUSTRATIONS MODEL REGULATION Draft: 9/9/95

Table of Contents

Section 1.	Purpose
Section 2.	Authority
Section 3.	Applicability and Scope
Section 4.	Definitions
Section 5.	Policies to Be Illustrated
Section 6.	General Rules and Prohibitions
Section 7.	Standards for Basic Illustrations
Section 8.	Standards for Supplemental Illustrations

Section 9.	Delivery of Illustrations and Record Retention
Section 10.	Annual Report; Notice to Policy Owners
Section 11.	Annual Certifications
Section 12.	Penalties
Section 13.	Separability
Section 14.	Effective Date

Section 1. Purpose

The purpose of this regulation is to provide rules for life insurance policy illustrations that will protect consumers and foster consumer education. The regulation provides illustration formats, prescribes standards to be followed when illustrations are used, and specifies the disclosures that are required in connection with illustrations. The goals of this regulation are to ensure that illustrations do not mislead purchasers of life insurance and to make illustrations more understandable. Insurers will, as far as possible, eliminate the use of footnotes and caveats and define terms used in the illustration in language that would be understood by a typical person within the segment of the public to which the illustration is directed.

Section 2. Authority

This regulation is issued based upon the authority granted the commissioner under Section [cite any enabling legislation and state law corresponding to Section 4 of the NAIC Unfair Trade Practices Act].

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

Section 3. Applicability and Scope

This regulation applies to all group and individual life insurance policies and certificates except:

- A. Variable life insurance;
- B. Individual and group annuity contracts;
- C. Credit life insurance; or
- D. Life insurance policies with no illustrated death benefits on any individual exceeding \$10,000.

Section 4. Definitions

For the purposes of this regulation:

- A. "Actuarial Standards Board" means the board established by the American Academy of Actuaries to develop and promulgate standards of actuarial practice.
- B. "Contract premium" means the gross premium that is required to be paid under a fixed premium policy, including the premium for a rider for which benefits are shown in the illustration.
- C. "Currently payable scale" means a scale of non-guaranteed elements in effect for a policy form as of the preparation date of the illustration or declared to become effective within the next ninety-five (95) days.
- D. "Disciplined current scale" means a scale of non-guaranteed elements constituting a limit on illustrations currently being illustrated by an insurer that is reasonably based on actual recent historical experience, as certified annually by an illustration actuary designated by the insurer. Further guidance in determining the disciplined current scale as contained in standards established by the Actuarial Standards Board may be relied upon if the standards:
 - (1) Are consistent with all provisions of this regulation;
 - (2) Limit a disciplined current scale to reflect only actions that have already been taken or events that have already occurred;
 - (3) Do not permit a disciplined current scale to include any projected trends of improvements in experience or any assumed improvements in experience beyond the illustration date; and
 - (4) Do not permit assumed expenses to be less than minimum assumed expenses.
- E. "Generic name" means a short title descriptive of the policy being illustrated such as "whole life," "term life" or "flexible premium adjustable life."
- F. "Group universal life" means a group policy or individual policies of universal life insurance issued to members of an employer group or other permitted group where:
 - (1) Every plan of coverage was selected by the employer or other group representative;

- (2) Some portion of the premium is paid by the group or through payroll deduction; and
- (3) Group underwriting or simplified underwriting is used.

G. "Guaranteed elements" and "non-guaranteed elements"

- (1) "Guaranteed elements" means the premiums, benefits, values, credits or charges under a policy of life insurance that are guaranteed and determined at issue.
- (2) "Non-guaranteed elements" means the premiums, benefits, values, credits or charges under a policy of life insurance that are not guaranteed or not determined at issue.

H. "Illustrated scale" means a scale of non-guaranteed elements currently being illustrated that is not more favorable to the policy owner than the lesser of:

- (1) The disciplined current scale; or
- (2) The currently payable scale.

I. "Illustration" means a presentation or depiction that includes non-guaranteed elements of a policy of life insurance over a period of years and that is one of the three (3) types defined below:

- (1) "Basic illustration" means a ledger or proposal used in the sale of a life insurance policy that shows both guaranteed and non-guaranteed elements.
- (2) "Supplemental illustration" means an illustration furnished in addition to a basic illustration that meets the applicable requirements of this regulation, and that may be presented in a format differing from the basic illustration, but may only depict a scale of non-guaranteed elements that is not permitted in a basic illustration.
- (3) "In force illustration" means an illustration furnished at any time after the policy that it depicts has been in force for one year or more.

J. "Illustration actuary" means an actuary meeting the requirements of Section 11 who certifies to illustrations based on the standard of practice promulgated by the Actuarial Standards Board.

K. "Lapse-supported illustration" means an illustration of a policy form failing the test of self-supporting as defined in this regulation, under a modified persistency rate assumption using persistency rates underlying the disciplined current scale for the first five (5) years and 100 percent policy persistency thereafter.

L. (1) "Minimum assumed expenses" means the minimum expenses that may be used in the calculation of the disciplined current scale for a policy form. The insurer may choose to designate each year the method of determining assumed expenses for all policy forms from the following:

- (a) Fully allocated expenses;
- (b) Marginal expenses; and
- (c) A generally recognized expense table based on fully allocated expenses representing a significant portion of insurance companies and approved by the [National Association of Insurance Commissioners or by the commissioner].

- (2) Marginal expenses may be used only if greater than a generally recognized expense table. If no generally recognized expense table is approved, fully allocated expenses must be used.

M. "Policy owner" means the owner named in the policy or the certificate holder in the case of a group policy.

N. "Premium outlay" means the amount of premium assumed to be paid by the policy owner or other premium payer out-of-pocket.

O. "Self-supporting illustration" means an illustration of a policy form for which it can be demonstrated that, when using experience assumptions underlying the disciplined current scale, for all illustrated points in time on or after the fifteenth policy anniversary or the twentieth policy anniversary for second-or-later-to-die policies (or upon policy expiration if sooner), the accumulated value of all policy cash flows equals or exceeds the total policy owner value available. For this purpose, policy owner value will include cash surrender values and any other illustrated benefit amounts available at the policy owner's election.

Section 5. Policies to Be Illustrated

A. Each insurer marketing policies to which this regulation is applicable shall notify the commissioner whether a policy form is to be marketed with or without an illustration. For all policy forms being actively marketed on the effective date

of this regulation, the insurer shall identify in writing those forms and whether an illustration will be used with them. For policy forms filed after the effective date of this regulation, the identification shall be made at the time of filing. Any previous identification may be changed by notice to the commissioner.

B. If the insurer identifies a policy form as one to be marketed without an illustration, any use of an illustration for any policy using that form prior to the first policy anniversary is prohibited.

Drafting Note: The prohibition in Section 5B may need to be modified if required by the state's replacement regulation.

C. If a policy form is identified by the insurer as one to be marketed with an illustration, a basic illustration prepared and delivered in accordance with this regulation is required, except that a basic illustration need not be provided to individual members of a group or to individuals insured under multiple lives coverage issued to a single applicant unless the coverage is marketed to these individuals. The illustration furnished an applicant for a group life insurance policy or policies issued to a single applicant on multiple lives may be either an individual or composite illustration representative of the coverage on the lives of members of the group or the multiple lives covered.

D. Potential enrollees of group universal life subject to this regulation shall be furnished a quotation with the enrollment materials. The quotation shall show potential policy values for sample ages and policy years on a guaranteed and non-guaranteed basis appropriate to the group and the coverage. This quotation shall not be considered an illustration for purposes of this regulation, but all information provided shall be consistent with the illustrated scale. A basic illustration shall be provided at delivery of the certificate to enrollees for group universal life who enroll for more than the minimum premium necessary to provide pure death benefit protection. In addition, the insurer shall make a basic illustration available to any group universal life enrollee who requests it.

Section 6. General Rules and Prohibitions

A. An illustration used in the sale of a life insurance policy shall satisfy the applicable requirements of this regulation, be clearly labeled "life insurance illustration" and contain the following basic information:

- (1) Name of insurer;
- (2) Name and business address of producer or insurer's authorized representative, if any;
- (3) Name, age and sex of proposed insured, except where a composite illustration is permitted under this regulation;
- (4) Underwriting or rating classification upon which the illustration is based;
- (5) Generic name of policy, the company product name, if different, and form number;
- (6) Initial death benefit;
- (7) Dividend option election or application of non-guaranteed elements, if applicable; and
- (8) Clear disclosure of the method used by the company to allocate expenses, as disclosed to the commissioner in the actuarial certification as required in Section 11C.

B. When using an illustration in the sale of a life insurance policy, an insurer or its producers or other authorized representatives shall not:

- (1) Represent the policy as anything other than a life insurance policy;
- (2) Use or describe non-guaranteed elements in a manner that is misleading or has the capacity or tendency to mislead;
- (3) State or imply that the payment or amount of non-guaranteed elements is guaranteed;
- (4) Use an illustration that does not comply with the requirements of this regulation;
- (5) Use an illustration that at any policy duration depicts policy performance more favorable to the policy owner than that produced by the illustrated scale of the insurer whose policy is being illustrated;
- (6) Provide an applicant with an incomplete illustration;
- (7) Represent in any way that premium payments will not be required for each year of the policy in order to maintain the illustrated death benefits, unless that is the fact;
- (8) Use the term "vanish" or "vanishing premium," or a similar term that implies the policy becomes paid up, to describe a plan for using non-guaranteed elements to pay a portion of future premiums;

- (9) Except for policies that can never develop nonforfeiture values, use an illustration that is "lapse-supported"; or
- (10) Use an illustration that is not "self-supporting."

C. If an interest rate used to determine the illustrated non-guaranteed elements is shown, it shall not be greater than the earned interest rate underlying the disciplined current scale.

Drafting Note: States may wish to replace disclosure requirements under the state's version of the Universal Life Insurance Model Regulation with the basic illustration as contained in this regulation.

Section 7. Standards for Basic Illustrations

A. **Format.** A basic illustration shall conform with the following requirements:

- (1) The illustration shall be labeled with the date on which it was prepared.
- (2) Each page, including any explanatory notes or pages, shall be numbered and show 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").
- (3) The assumed dates of payment receipt and benefit pay-out within a policy year shall be clearly identified.
- (4) If the age of the proposed insured is shown as a component of the tabular detail, it shall be issue age plus the numbers of years the policy is assumed to have been in force.
- (5) The assumed payments on which the illustrated benefits and values are based shall be identified as premium outlay or contract premium, as applicable. For policies that do not require a specific contract premium, the illustrated payments shall be identified as premium outlay.
- (6) Guaranteed death benefits and values available upon surrender, if any, for the illustrated premium outlay or contract premium shall be shown and clearly labeled guaranteed.
- (7) If the illustration shows any non-guaranteed elements, they cannot be based on a scale more favorable to the policy owner than the insurer's illustrated scale at any duration. These elements shall be clearly labeled non-guaranteed.
- (8) The guaranteed elements, if any, shall be shown before corresponding non-guaranteed elements and shall be specifically referred to on any page of an illustration that shows or describes only the non-guaranteed elements (e.g., "see page one for guaranteed elements.")
- (9) The account or accumulation value of a policy, if shown, shall be identified by the name this value is given in the policy being illustrated and shown in close proximity to the corresponding value available upon surrender.
- (10) The value available upon surrender shall be identified by the name this value is given in the policy being illustrated and shall be the amount available to the policy owner in a lump sum after deduction of surrender charges, policy loans and policy loan interest, as applicable.
- (11) Illustrations may show policy benefits and values in graphic or chart form in addition to the tabular form.
- (12) Any illustration of non-guaranteed elements shall be accompanied by a statement indicating that:
 - (a) The benefits and values are not guaranteed;
 - (b) The assumptions on which they are based are subject to change by the insurer; and
 - (c) Actual results may be more or less favorable.
- (13) If the illustration shows that the premium payer may have the option to allow policy charges to be paid using non-guaranteed values, the illustration must clearly disclose that a charge continues to be required and that, depending on actual results, the premium payer may need to continue or resume premium outlays. Similar disclosure shall be made for premium outlay of lesser amounts or shorter durations than the contract premium. If a contract premium is due, the premium outlay display shall not be left blank or show zero unless accompanied by an asterisk or similar mark to draw attention to the fact that the policy is not paid up.
- (14) If the applicant plans to use dividends or policy values, guaranteed or non-guaranteed, to pay all or a portion of the contract premium or policy charges, or for any other purpose, the illustration may reflect those plans and the impact on future policy benefits and values.

B. **Narrative Summary.** A basic illustration shall include the following:

- (1) A brief description of the policy being illustrated, including a statement that it is a life insurance policy;
- (2) A brief description of the premium outlay or contract premium, as applicable, for the policy. For a policy that does not require payment of a specific contract premium, the illustration shall show the premium outlay that must be paid to guarantee coverage for the term of the contract, subject to maximum premiums allowable to qualify as a life insurance policy under the applicable provisions of the Internal Revenue Code;
- (3) A brief description of any policy features, riders or options, guaranteed or non-guaranteed, shown in the basic illustration and the impact they may have on the benefits and values of the policy; and
- (4) Identification and a brief definition of column headings and key terms used in the illustration.

C. Numeric Summary.

(1) Following the narrative summary, a basic illustration shall include a numeric summary of the death benefits and values and the premium outlay and contract premium, as applicable. For a policy that provides for a contract premium, the guaranteed death benefits and values shall be based on the contract premium. This summary shall be shown for at least policy years five (5), ten (10) and twenty (20) and at age 70, if applicable, on the three bases shown below. For multiple life policies the summary shall show policy years five (5), ten (10), twenty (20) and thirty (30).

- (a) Policy guarantees;
- (b) Insurer's illustrated scale;
- (c) Insurer's illustrated scale used but with the non-guaranteed elements reduced as follows:
 - (i) Dividends at fifty percent (50%) of the dividends contained in the illustrated scale used;
 - (ii) Non-guaranteed credited interest at rates that are the average of the guaranteed rates and the rates contained in the illustrated scale used; and
 - (iii) All non-guaranteed charges, including but not limited to, term insurance charges, mortality and expense charges, at rates that are the average of the guaranteed rates and the rates contained in the illustrated scale used.

(2) In addition, if coverage would cease prior to policy maturity or age 100, the year in which coverage ceases shall be identified for each of the three (3) bases.

D. Statements. Statements substantially similar to the following shall be included on the same page as the numeric summary and signed by the applicant, or the policy owner in the case of an illustration provided at time of delivery, as required in this regulation.

- (1) A statement to be signed and dated by the applicant or policy owner reading as follows: "I have received a copy of this illustration and understand that any non-guaranteed elements illustrated are subject to change and could be either higher or lower. The agent has told me they are not guaranteed."
- (2) A statement to be signed and dated by the insurance producer or other authorized representative of the insurer reading as follows: "I certify that this illustration has been presented to the applicant and that I have explained that any non-guaranteed elements illustrated are subject to change. I have made no statements that are inconsistent with the illustration."

E. Tabular Detail.

(1) A basic illustration shall include the following for at least each policy year from one (1) to ten (10) and for every fifth policy year thereafter ending at age 100, policy maturity or final expiration; and except for term insurance beyond the 20th year, for any year in which the premium outlay and contract premium, if applicable, is to change:

- (a) The premium outlay and mode the applicant plans to pay and the contract premium, as applicable;
- (b) The corresponding guaranteed death benefit, as provided in the policy; and
- (c) The corresponding guaranteed value available upon surrender, as provided in the policy.

(2) For a policy that provides for a contract premium, the guaranteed death benefit and value available upon surrender shall correspond to the contract premium.

(3) Non-guaranteed elements may be shown if described in the contract. In the case of an illustration for a policy on which the insurer intends to credit terminal dividends, they may be shown if the insurer's current practice is to pay terminal dividends. If any non-guaranteed elements are shown they must be shown at the same durations as the

corresponding guaranteed elements, if any. If no guaranteed benefit or value is available at any duration for which a non-guaranteed benefit or value is shown, a zero shall be displayed in the guaranteed column.

Section 8. Standards for Supplemental Illustrations

A. A supplemental illustration may be provided so long as:

- (1) It is appended to, accompanied by or preceded by a basic illustration that complies with this regulation;
- (2) The non-guaranteed elements shown are not more favorable to the policy owner than the corresponding elements based on the scale used in the basic illustration;
- (3) It contains the same statement required of a basic illustration that non-guaranteed elements are not guaranteed; and
- (4) For a policy that has a contract premium, the contract premium underlying the supplemental illustration is equal to the contract premium shown in the basic illustration. For policies that do not require a contract premium, the premium outlay underlying the supplemental illustration shall be equal to the premium outlay shown in the basic illustration.

B. The supplemental illustration shall include a notice referring to the basic illustration for guaranteed elements and other important information.

Section 9. Delivery of Illustration and Record Retention

A. (1) If a basic illustration is used by an insurance producer or other authorized representative of the insurer in the sale of a life insurance policy and the policy is applied for as illustrated, a copy of that illustration, signed in accordance with this regulation, shall be submitted to the insurer at the time of policy application. A copy also shall be provided to the applicant.

(2) If the policy is issued other than as applied for, a revised basic illustration conforming to the policy as issued shall be sent with the policy. The revised illustration shall conform to the requirements of this regulation, shall be labeled "Revised Illustration" and shall be signed and dated by the applicant or policy owner and producer or other authorized representative of the insurer no later than the time the policy is delivered. A copy shall be provided to the insurer and the policy owner.

B. (1) If no illustration is used by an insurance producer or other authorized representative in the sale of a life insurance policy or if the policy is applied for other than as illustrated, the producer or representative shall certify to that effect in writing on a form provided by the insurer. On the same form the applicant shall acknowledge that no illustration conforming to the policy applied for was provided and shall further acknowledge an understanding that an illustration conforming to the policy as issued will be provided no later than at the time of policy delivery. This form shall be submitted to the insurer at the time of policy application.

(2) If the policy is issued, a basic illustration conforming to the policy as issued shall be sent with the policy and signed no later than the time the policy is delivered. A copy shall be provided to the insurer and the policy owner.

C. If the basic illustration or revised illustration is sent to the applicant or policy owner by mail from the insurer, it shall include instructions for the applicant or policy owner to sign the duplicate copy of the numeric summary page of the illustration for the policy issued and return the signed copy to the insurer. The insurer's obligation under this subsection shall be satisfied if it can demonstrate that it has made a diligent effort to secure a signed copy of the numeric summary page. The requirement to make a diligent effort shall be deemed satisfied if the insurer includes in the mailing a self-addressed postage prepaid envelope with instructions for the return of the signed numeric summary page.

D. A copy of the basic illustration and a revised basic illustration, if any, signed as applicable, along with any certification that either no illustration was used or that the policy was applied for other than as illustrated, shall be retained by the insurer until three (3) years after the policy is no longer in force. A copy need not be retained if no policy is issued.

Section 10. Annual Report; Notice to Policy Owners

A. In the case of a policy designated as one for which illustrations will be used, the insurer shall provide each policy owner with an annual report on the status of the policy that shall contain at least the following information:

(1) For universal life policies, the report shall include the following:

- (a) The beginning and end date of the current report period;
- (b) The policy value at the end of the previous report period and at the end of the current report period;

(c) The total amounts that have been credited or debited to the policy value during the current report period, identifying each by type (e.g., interest, mortality, expense and riders);

(d) The current death benefit at the end of the current report period on each life covered by the policy;

(e) The net cash surrender value of the policy as of the end of the current report period;

(f) The amount of outstanding loans, if any, as of the end of the current report period; and

(g) For fixed premium policies:

If, assuming guaranteed interest, mortality and expense loads and continued scheduled premium payments, the policy's net cash surrender value is such that it would not maintain insurance in force until the end of the next reporting period, a notice to this effect shall be included in the report; or

(h) For flexible premium policies:

If, assuming guaranteed interest, mortality and expense loads, the policy's net cash surrender value will not maintain insurance in force until the end of the next reporting period unless further premium payments are made, a notice to this effect shall be included in the report.

Drafting Note: For states that have adopted the NAIC Universal Life Model Regulation, this paragraph could be replaced with a reference to the equivalent of Section 9 of the model regulation.

(2) For all other policies, where applicable:

(a) Current death benefit;

(b) Annual contract premium;

(c) Current cash surrender value;

(d) Current dividend;

(e) Application of current dividend; and

(f) Amount of outstanding loan.

(3) Insurers writing life insurance policies that do not build nonforfeiture values shall only be required to provide an annual report with respect to these policies for those years when a change has been made to nonguaranteed policy elements by the insurer.

B. If the annual report does not include an in force illustration, it shall contain the following notice displayed prominently: "IMPORTANT POLICY OWNER NOTICE: You should consider requesting more detailed information about your policy to understand how it may perform in the future. You should not consider replacement of your policy or make changes in your coverage without requesting an in force illustration. You may annually request, without charge, such an illustration by calling [insurer's phone number], writing to [insurer's name] at [insurer's address] or contacting your agent. If you do not receive an in force illustration within 30 days from your request, you should contact your state insurance department." The insurer may vary the sequential order of the methods for obtaining an in force illustration.

C. Upon the request of the policy owner, the insurer shall furnish an in force illustration of current and future benefits and values based on the insurer's present illustrated scale. This illustration shall comply with the requirements of Section 6A, 6B, 7A and 7E. No signature or other acknowledgment of receipt of this illustration shall be required.

D. If an adverse change in non-guaranteed elements that could affect the policy has been made by the insurer since the last annual report, the annual report shall contain a notice of that fact and the nature of the change prominently displayed.

Section 11. Annual Certifications

A. The board of directors of each insurer shall appoint one or more illustration actuaries.

B. The illustration actuary shall certify that the disciplined current scale used in illustrations is in conformity with the Actuarial Standard of Practice for Compliance with the NAIC Model Regulation on Life Insurance Illustrations promulgated by the Actuarial Standards Board, and that the illustrated scales used in insurer-authorized illustrations meet the requirements of this regulation.

C. The illustration actuary shall:

(1) Be a member in good standing of the American Academy of Actuaries;

- (2) Be familiar with the standard of practice regarding life insurance policy illustrations;
 - (3) Not have been found by the commissioner, following appropriate notice and hearing to have:
 - (a) Violated any provision of, or any obligation imposed by, the insurance law or other law in the course of his or her dealings as an illustration actuary;
 - (b) Been found guilty of fraudulent or dishonest practices;
 - (c) Demonstrated his or her incompetence, lack of cooperation, or untrustworthiness to act as an illustration actuary; or
 - (d) Resigned or been removed as an illustration actuary within the past five (5) years as a result of acts or omissions indicated in any adverse report on examination or as a result of a failure to adhere to generally acceptable actuarial standards;
 - (4) Not fail to notify the commissioner of any action taken by a commissioner of another state similar to that under Paragraph (3) above;
 - (5) Disclose in the annual certification whether, since the last certification, a currently payable scale applicable for business issued within the previous five (5) years and within the scope of the certification has been reduced for reasons other than changes in the experience factors underlying the disciplined current scale. If nonguaranteed elements illustrated for new policies are not consistent with those illustrated for similar in force policies, this must be disclosed in the annual certification. If nonguaranteed elements illustrated for both new and in force policies are not consistent with the nonguaranteed elements actually being paid, charged or credited, this must be disclosed in the annual certification; and
 - (6) Disclose in the annual certification the method used to allocate overhead expenses for all illustrations:
 - (a) Fully allocated expenses;
 - (b) Marginal expenses; or
 - (c) A generally recognized expense table based on fully allocated expenses representing a significant portion of insurance companies and approved by the [National Association of Insurance Commissioners or by the commissioner].
- D. (1) The illustration actuary shall file a certification with the board and with the commissioner:
- (a) Annually for all policy forms for which illustrations are used; and
 - (b) Before a new policy form is illustrated.
- (2) If an error in a previous certification is discovered, the illustration actuary shall notify the board of directors of the insurer and the commissioner promptly.
- E. If an illustration actuary is unable to certify the scale for any policy form illustration the insurer intends to use, the actuary shall notify the board of directors of the insurer and the commissioner promptly of his or her inability to certify.
- F. A responsible officer of the insurer, other than the illustration actuary, shall certify annually that the illustration formats meet the requirements of this regulation and that the scales used in insurer-authorized illustrations are those scales certified by the illustration actuary.
- G. The annual certifications shall be provided to the commissioner each year by a date determined by the insurer.
- H. If an insurer changes the illustration actuary responsible for all or a portion of the company's policy forms, the insurer shall notify the commissioner of that fact promptly and disclose the reason for the change.

Section 12. Penalties

In addition to any other penalties provided by the laws of this state, an insurer or producer that violates a requirement of this regulation shall be guilty of a violation of Section [cite state's unfair trade practices act].

Section 13. Separability

If any provision of this regulation or its application 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.

Section 14. Effective Date

This regulation shall become effective [January 1, 1997, or effective date set in regulation, whichever is later] and shall apply to policies sold on or after the effective date.

ATTACHMENT ONE-B

TO: Robert E. Wilcox, Chair, Life Disclosure Working Group
 FROM: Ted Becker, Chief Life Actuary, Texas Department of Insurance
 DATE: September 11, 1995
 RE: Concerns with Current Draft Proposal Life Insurance Illustrations Model Regulation

At the Sept. 9, 1995, meeting of the Life Disclosure Working Group, the members voted to recommend the current draft proposal of the Life Insurance Model Regulation to the Life Insurance (A) Committee for adoption. That committee meets Sept. 12, 1995.

Texas is a member of the working group but abstained from voting for recommending the current draft proposal for adoption. One other member state abstained, and another member state voted against the recommendation. You invited those states that did not vote for the recommendation to submit written comments, which could then be attached to the minutes for the Sept. 9, 1995, meeting. This memorandum is submitted for that purpose.

The memorandum expresses our position on three important matters. The first two matters are definite concerns about the wording of the current draft proposal. The third matter expresses our feeling that we need more time to review the current draft proposal with respect to two important actuarial aspects.

1. The current draft proposal is not sufficiently comparison-friendly for us to support adoption. By "comparison-friendly," we believe that an individual who is considering the purchase of a new life insurance policy should be able to request illustrations from two or more insurers and should be able to readily compare them. This could be of significant help in deciding which policy to purchase. Here are two specific aspects where we believe the current draft proposal needs change. First, we believe that the arrangement and format of the basic illustration should allow easy comparison. (As specific examples of our concern we note that the current draft proposal does not require the proposed new life insurance policy to be illustrated without any extra premium riders attached and without any loans against the policy.) Second, we also believe that if the proposed new life insurance policy has more than one non-guaranteed element, such as a universal life insurance policy, then the basic illustration should contain separate information illustrating each of the elements.

2. The current draft proposal does not place enough restraint on insurers in developing illustrations for future policy years for us to support adoption. We support the concept that interest rates used by different insurers should converge or approach convergence at some specific future duration. (One suggestion was that 6% interest should be required to be assumed for all durations beyond the fifth year. This may be too rigid a requirement, but it would be a starting point for "leveling out the playing field" for illustrations involving future policy years.) Additionally, we believe that illustrations of non-guaranteed elements beyond a certain later policy duration may be too nebulous to be allowed in illustrations. (The staff of our department has previously suggested 10 years in the future as a possible "dividing line," so that illustrations of non-guaranteed elements beyond the tenth policy year would not be permitted. An exception might be made for indeterminate premium and conditionally renewable term plans, since the effect of the non-guaranteed elements is not compounded from year to year.)

3. The current draft proposal has been changed several times quite recently with respect to actuarial matters. We believe additional time would be helpful in order to review the recent changes and to be comfortable that this draft proposal is adequate. There are two important specific aspects we would like to consider. One specific aspect involves the expense assumptions used in preparing illustrations. At the August 1995 working group meeting, the working group voted to allow companies to develop illustrations based on industry-average fully allocated expenses for large insurance companies, under certain conditions, instead of the expenses of the insurer preparing the illustration. At the Sept. 9, 1995, meeting of the working group, it was agreed that the use of industry-average expenses would need to be disclosed, when it is applicable, to individuals receiving illustrations of proposed new life insurance policies. Additional time to review the effect of these changes would be helpful. The other specific aspect relates to the formulas used in filling in the actual numbers in illustrations. Is the illustration actuary responsible for those formulas, and does he or she certify that they are appropriate? We believe this is the case, but again we feel that additional time to review the recent changes would be helpful. We note that at the August 1995 working group meeting, some of the persons attending were under the impression that the only responsibility of the illustration actuary was with respect to scales, such as the disciplined current scale.

ATTACHMENT TWO

Genetic Testing Working Group of the
Life Insurance (A) Committee
Philadelphia, Pennsylvania
September 10, 1995

The Genetic Testing Working Group of the Life Insurance (A) Committee met in Salon D of the Marriott Hotel in Philadelphia, Pa., at 9 a.m. on Sept. 10, 1995. Dixon Larkin (Utah) chaired the meeting. The following working group members or their representatives were present: Don Koch (Alaska); Kenney Shipley (Fla.); Robert Lange (Neb.); Kip May (Ohio); Mary Alice Bjork (Ore.); Birny Birnbaum (Texas); and Kathleen Connor (Wash.).

1. Discussion of Letter to Sen. Nancy Kassebaum

Dixon Larkin (Utah) said that Sen. Nancy Kassebaum (R-Kan.) had asked for information from the NAIC about the term "genetic history" and whether genetic history and genetic testing were encompassed within the terms "medical underwriting" or "evidence of insurability." The working group discussed a draft of a letter responding to the request. Birny Birnbaum (Texas) said that genetic history was clearing encompassed within the term medical underwriting. Don Koch (Alaska) reminded the group that this was one of the very first issues discussed by the working group. Commissioner James Ulland (Minn.) said that the definition of genetic testing was very important. Dr. Larkin agreed that genetic testing had been discussed by the working group all the way from a family history to sophisticated molecular biological testing. Kenney Shipley (Fla.) said she thought the working group needed to be as specific as possible in responding to Congress. She suggested the working group not mince words but add that genetic testing was less clear, and the working group was in the process of drawing up a position on genetic testing. Roberta Meyer (American Council of Life Insurance—ACLI) said that genetic history clearly included the results of genetic testing and agreed that all of this was part of medical underwriting.

Dr. Larkin said the draft letter would be revised to address the comments received from the working group.

2. Discuss Outline of White Paper on Genetic Testing

Dr. Larkin said the next item on the agenda was to divide up responsibility for the outline of the white paper and flesh out that outline. Kathleen Connor (Wash.) suggested that, between the materials the working group had received earlier and the transcripts of the meetings held by the American Academy of Actuaries and the National Institute of Health, the working group had material adequate to address the outline. Ms. Connor suggested the working group could also draft a sample model law. She suggested that a draft that other members of the working group could react to would be very helpful. It was agreed that various viewpoints could be appropriately presented through different models. It was not felt that the working group had achieved consensus on what would be contained in a single model.

The members of the working group divided responsibility for the white paper. Section I, Definition of Genetic Testing: Commissioner Ulland and Kip May (Ohio) agreed to develop this section. Section II, The Current State of Genetic Testing: Mr. Koch and Dr. Larkin agreed to begin development of this section. Section III, Genetic Testing in Life, Health and Disability Income Insurance: Commissioner Robert Lange (Neb.) agreed to take responsibility for this section. Section IV, Concerns About Genetic Testing in Life, Health and Disability Income Insurance: Mr. Birnbaum agreed to be responsible for drafting Subsection A, Mary Alice Bjork (Ore.) agreed to be responsible for Subsection B, and Ms. Connor agreed to be responsible for Subsection C. Section V, Regulatory Options: Mr. Birnbaum and Mr. May agreed to be responsible for Subsection A. Section VI, Genetic Testing Working Group Recommendations: Ms. Bjork, Ms. Connor, Mr. May and Ms. Shipley agreed to work on recommendations, including a sample draft model regulation.

The working group agreed to a conference call in approximately one month so that the group could see where they might be overlapping in their drafting and could react to each other's contributions. Two weeks later a second conference call will be held to further discuss and refine the draft so that it will be ready to distribute to the public at the 1995 Winter National Meeting.

Having no further business, the Genetic Testing Working Group adjourned at 9:50 a.m..

ATTACHMENT THREE

Viatical Settlements Working Group of the
Life Insurance (A) Committee
Philadelphia, Pennsylvania
September 11, 1995

The Viatical Settlements Working Group of the Life Insurance (A) Committee met in Salon I of the Marriott Hotel in Philadelphia, Pa., at 1 p.m. on Sept. 11, 1995. Glenn Pomeroy (N.D.) chaired the meeting. The following working group members or their representatives were present: Michael Bownes (Ala.); Carol Ostapchuk (Fla.); Ron Kotowski (Ill.); Marilyn Burch (Kan.); Lester Dunlap (La.); Frederick P. Schumpe (Mo.); Tom Jacks (N.C.); Mary Alice Bjork (Ore.); Don Switzer (Texas); Dixon Larkin (Utah); and Eleanor Perry (Vt.).

1. Update on SEC vs. Life Partners

Commissioner Glenn Pomeroy (N.D.) provided an update on the recent decision in *Securities and Exchange Commission vs. Life Partners and Brian Pardo*. Commissioner Pomeroy said that as securities commissioner in North Dakota he had issued a cease and desist order against the company in 1992 in North Dakota, finding that the way this company marketed its viatical settlements was in violation of the North Dakota securities law. Commissioner Pomeroy provided the regulators with a sample of the type of marketing that the company did in North Dakota. He indicated that the Securities and Exchange Commission (SEC) action also alleges this form of marketing violates the federal securities provisions, and that the presiding judge recently issued a preliminary injunction in this matter. He pointed out that not all companies market to individual investors, so not all companies are affected by the SEC decision.

2. Update on Federal Tax Legislation

Gary Choades (Viaticus) provided information on the tax legislation contained in H.R. 1215 now pending before the U.S. House. He said that people were beginning to recognize the importance of favorable tax treatment for viatical settlements and accelerated death benefits. In his opinion one of the most critical parts of the legislation was a demonstration that state regulators were on top of the issue of viatical settlements. He said if Congress did not feel that viatical settlements were being properly regulated, it was not inclined to give a tax break. The pending legislation contains a provision allowing the tax break only if the viatical settlement provider is licensed in the state of residence of the viator. If the state has no law in place, the favorable tax treatment would be given if the viatical settlement is in compliance with Sections 8 and 9 of the NAIC Viatical Settlements Model Act. Mr. Choades said that it appeared support for the tax bill was strong. Bill Kelley (Viatical Association of America) said that his association was pledged to support the model and reasonable regulation for viatical settlement companies and said his organization would work with the NAIC to develop good regulations. He said that a Senate bill might put a sunset on the provision allowing favorable tax treatment for companies that would follow Sections 8 and 9 of the model. He said this put pressure on the states to adopt the model within a short period of time. Mr. Kelley also clarified that the favorable tax treatment in the congressional bills was in favor of the seller of the insurance policy. Commissioner Pomeroy expressed appreciation to the viatical settlement industry for the language that they had been influential in putting in the bill that recognized state viatical company regulation.

3. Implementation Update from States

Commissioner Pomeroy asked states that had recent activity in viatical settlement legislation to update the group. Lester Dunlap (La.) reported that the Louisiana bill had passed their legislature and was effective Aug. 15, 1995, and the department was now working on developing a regulation. Mary Alice Bjork (Ore.) reported that the department in Oregon was working on developing a regulation. Eleanor Perry (Vt.) reported that the comment period had ended on the Vermont regulation and the department was now considering comments. Kevin McCarty (Fla.) reported that Florida had been unsuccessful in adopting the model, but intended to try again. Ron Kotowski (Ill.) reported that his state's bill had been tabled but he was hopeful that it would be reintroduced in the fall session. Don Koch (Alaska) reported that Alaska was planning to introduce a bill based on the NAIC's model in the next session. Commissioner Pomeroy reported that North Dakota had adopted the model but it had been narrowed to a large extent and they had very little authority to adopt a regulation. Frederick Schumpe (Mo.) said that a bill had been introduced in Missouri in the last session, but had not been adopted, and the department hoped that it would be reintroduced in 1996. Mr. Schumpe said the state's bill was based on the NAIC model. Don Switzer (Texas) reported that the law passed in Texas was not very strong, was not based on the model, but did contain authority to adopt regulations compelling disclosure. He said that the department was in the process of developing regulations to implement that law with a concentration on cost comparison. Tom Jacks (N.C.) said that North Carolina had adopted the model and was working on a regulation that the department intended to have in place very shortly.

4. Uniform Application Form

Commissioner Pomeroy asked if this was an appropriate time for a subgroup to develop a uniform application form. He said it seemed to him that it would be easier to do this in the infancy of regulation of viatical settlement companies rather than waiting until each state had developed its own form. Mr. Jacks commented that this was already happening informally as states that had adopted the model contacted each other for assistance. Illinois, North Carolina and Vermont volunteered to be on a committee to begin drafting a uniform application form.

Commissioner Pomeroy asked the audience for reaction to this effort. Mr. Choades said that in his experience licensing in the various states had gone well. He said that the early laws on licensing such as that in California were more difficult, but the model approach was based on common sense and made licensing easier. Mr. Kelley said that it would be a great assistance to establish some uniformity. He expressed support for most of the provisions of the model act, but said that he found that the minimum benefit requirement in the regulation difficult. He said that most of the minimum payments required were actually below the industry average except for the payment for 24 months or more. He said the model provision requiring at least 50% of face value was not generally available. David Landey (a viatical broker) said that he was legally a representative of viators. He said state laws did not distinguish between a broker for a company and a broker for a viator and he thought this could be improved.

Commissioner Pomeroy invited members of the working group as well as the audience to provide written comment with suggestions for any changes to the model law or regulation that might be considered by the working group. He pointed out that the models had been developed when there was very little experience on viatical settlements, and as the industry developed there would probably be opportunity for improvements in the models. He said discussion of the comments would be the main topic at the Winter National Meeting.

David Peterson (Affording Care) commented that he had been involved in the viatical settlement industry since its beginning and his organization published a list of the viatical settlement companies. Commissioner Pomeroy asked if Mr. Peterson was compensated by the industry, and Mr. Peterson replied in the negative. Commissioner Pomeroy said that he had known Mr. Peterson for some time and found that he was one of the nation's foremost experts and pioneers on the viatical settlement industry and would be able to represent the interest of consumers to the working group. Mr. Peterson said that he thought the provisions of the model provided very little assistance for the seriously ill. He said that registration and licensing requirements did not do an ill person any good, and some of the requirements in various states were so onerous that no one would get licensed. In those states that meant a policy could not be viaticated. In this case, he pointed out that a law limited access rather than protecting consumers. Mr. Peterson encouraged the working group to talk to seriously ill individuals or their advocates to gather information on helpful provisions for the model. Mr. Peterson pointed out that the New York law had 12 real consumer protections that were missing from the NAIC's model. One example of a protection was the fact that in New York law a policy that was converted from a group life policy could not begin a new contestability period for the conversion policy. Mr. Peterson also questioned the lack of participation by New York and California in the NAIC's working group because those two states had the most experience with viatical settlement laws. Commissioner Pomeroy responded that he had encouraged New York and California to participate, but so far they had not expressed interest in joining the working group.

Having no further business, the Viatical Settlements Working Group adjourned at 2 p.m.

ATTACHMENT FOUR

Ad Hoc Working Group on Annuities of the Life Insurance (A) Committee Philadelphia, Pennsylvania September 11, 1995

The Ad Hoc Working Group on Annuities of the Life Insurance (A) Committee met in Salon C of the Marriott Hotel in Philadelphia, Pa., at 8 a.m. on Sept. 11, 1995. Jerry Fickes (N.M.) chaired the meeting. The following working group members or their representatives were present: Tom Foley (Fla.); Scott Galenbeck (Iowa); Mary Alice Bjork (Ore.); Ted Becker (Texas); and Dixon Larkin (Utah).

The purpose of the working group meeting was to determine if a request should be made to the Life Insurance (A) Committee to institute a task force next year on annuities under the Life Insurance (A) Committee. Jerry Fickes (N.M.) pointed out that a chart had been distributed at the Summer National Meeting that demonstrated that, with the exception of a few annuity models, few states had adopted the NAIC's model laws or model regulations on annuities. He suggested sending a questionnaire to states that would help the Ad Hoc Working Group on Annuities determine whether there were problems in the area of annuities and if there were insufficient or outdated models that needed to be addressed. Mr. Fickes emphasized that it would not be the committee's intent to duplicate anything already being addressed by other committees. He pointed out that the Life and Health Actuarial Task Force is considering annuity nonforfeiture, the Life Disclosure Working Group is considering annuity illustrations, and the Market Conduct and Consumer Affairs (EX3) Subcommittee is considering the issue of banks and annuities. As an example of a hole that might exist in state statutes, Mr. Fickes said that many states did not regulate charitable gift annuities and he thought this was a possible area for the task force to address.

Barbara Lautzenheiser (Lautzenheiser & Associates) applauded the working group for its awareness of the importance of not duplicating what other groups were doing. She said it was important to emphasize that annuities were an insurance product, and thought that there needed to be a major emphasis on retirement saving in this country.

The working group agreed that it was a good idea to send out a questionnaire to the states within the next two to three weeks asking for information that would be helpful to the working group. The working group authorized Mr. Fickes to derive the questionnaire with the assistance of Carolyn Johnson (NAIC/SSO), the staff support for the working group. A draft of the questionnaire will be circulated to working group members. The working group will ask for the questionnaires to be returned by the end of October and have a conference call in early November to discuss the working group's recommendations to the Life Insurance (A) Committee at the 1995 Winter National Meeting. Several state regulators in attendance at the meeting suggested items to be included on the questionnaire. The staff was requested to contact the EX3 Subcommittee dealing with annuities to see if they had any questions to add to the questionnaire.

Mr. Fickes also pointed out that the working group would need to prepare a fiscal impact statement at the same time as it presented a recommendation to the Life Insurance (A) Committee.

Having no further business, the Ad Hoc Working Group on Annuities adjourned at 9:35 a.m.