

## LIFE INSURANCE AND ANNUITIES (A) COMMITTEE

### Reference:

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Terri Vaughan, Chair—Iowa  
Neil D. Levin, Vice Chair—N.Y.

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### MINUTES

The Life Insurance and Annuities (A) Committee met in Salon IV of the Walt Disney World Dolphin Hotel in Orlando, Fla., at 11 a.m. on Dec. 9, 1998. A quorum was present and Roger Strauss, representing Terri Vaughan (Iowa) chaired the meeting. The following committee members or their representatives were present: Lester Dunlap representing James H. Brown (La.); Cindy Martin representing Linda Ruthardt (Mass.); Clyde Dailey representing Mark O'Keefe (Mont.); Mike Batte representing Chris P. Krahling (N.M.); Dan Keating representing John Crawford (Okla.); and Leslie Jones representing Lee P. Jedziniak (S.C.).

#### 1. Report of Viatical Settlements Working Group

Lester Dunlap (La.) said the working group met Dec. 6, the day following the hearing held by the Life Insurance and Annuities (A) Committee. (A summary of the testimony is Attachment One.) The working group first discussed whether to finish its charge or to go back and review the entire project, based on the discussion at the hearing. The working group decided to finish the redraft of the Viatical Settlements Model Regulation, hopefully completing this work by conference call about Feb. 1, 1999. Mr. Dunlap expressed the desire to bring the completed document to the A Committee for adoption at the Spring National Meeting. Mr. Dunlap said the working group changed Section 5 to reinsert the minimum standards table with the "reasonableness" test as an alternative approach. The working group has several suggested charges for 1999 to pursue other issues identified at the Life Insurance and Annuities (A) Committee hearing. He said the most important project is to develop an "Alert" package to inform regulators, consumers and investors about issues of current concern regarding viatical settlements. Tom Foley (N.D.) offered to head the group working on that project. Mr. Dunlap said that the working group will ask for a charge in 1999 to examine the investor's side of the viatical transaction. He said the group hopes to come to some conclusions that will help regulate that side of

the process. Mr. Dunlap said there are a number of insurance-related issues that were raised at the hearing about insurable interest and sales of policies by healthy individuals. The A Committee may want to appoint a separate working group to consider those issues.

Mike Batte (N.M.) moved and Dan Keating (Okla.) seconded a motion to receive the report of the Viatical Settlements Working Group (Attachment Two). The motion passed.

## 2. Report of the Life Disclosure Working Group

Mr. Foley said he was pleased to present two reports to the Life Insurance and Annuities (A) Committee and in both cases he is able to report a finished product. The Life Disclosure Working Group completed its development of the Annuity Disclosure Model Regulation. This product, in conjunction with the buyer's guide adopted during the last quarter will make a good disclosure package. He said he anticipates that the 1999 activity of the working group will involve life insurance disclosure issues.

Mr. Batte moved and Mr. Keating seconded a motion to adopt the report of the Life Disclosure Working Group (Attachment Three). The motion passed.

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

Mr. Foley reported that the task force continued its discussion of the Actuarial Opinion and Memorandum Regulation and discussed a new concept for a unified valuation law. Lengthy discussion took place on both of these issues and Mr. Foley said he anticipates continued discussion in 1999. The State of Florida will chair a subgroup to continue work on the life nonforfeiture project.

Mr. Foley said the task force adopted revisions to the Valuation of Life Insurance Policies Model Regulation (commonly known as XXX). Mr. Foley said this is important for all of the life insurance industry. He anticipates the model being adopted by many states in early 1999. The insurance industry has committed to support this project.

Mr. Batte moved and Mr. Dunlap seconded a motion to adopt the report of the Life and Health Actuarial (Technical) Task Force. The motion passed.

## 4. Report of the Equity Indexed Products Working Group

Mr. Batte reported that the working group reviewed its charge and work plan to decide if it addressed all of the issues identified earlier in the year. The working group considered a recommendation on agents education and recommends to its parent that insurers train their agents about equity-indexed products and that regulators monitor this training. The working group would like to request a 1999 charge to prepare recommendations on the contract review process.

Mr. Batte moved and Mr. Dunlap seconded a motion to receive the report of the Equity Indexed Products Working Group (Attachment Four). The motion passed.

## 5. Report of the Suitability Working Group

Paul DeAngelo (N.J.) said the Suitability Working Group is reviewing suitability standards in place in related industries and in some of the states and to lay the ground work for a white paper on suitability. The second part of this working group's charge is to draft amendments to the Life Insurance Advertising Model Regulation. Two conference calls will be held after the first of the year, one on each issue. The working group intends to survey states on their views about what should be included in suitability standards. The second conference call will consider amendments to the advertising regulation. Mr. DeAngelo said the working group heard a presentation from a broker-dealer on the suitability standards it uses. The working group requests a continuation of its charge to review the advertising regulation, and a modification of the charge on suitability to say the group will

draft a white paper. Mr. DeAngelo said the conclusions of the white paper may indicate a necessity to develop a model act or regulation on suitability, so a tentative charge for 2000 is included.

Clyde Dailey (Mont.) moved and Mr. Keating seconded a motion to receive the report of the Suitability Working Group (Attachment Five). The motion passed.

#### 6. Report of the Synthetic GIC Working Group

Mark Peavy (NAIC/SSO) said that the working group's materials include a copy of the Synthetic Guaranteed Investment Contract Model Regulation, which the working group recommends for adoption. Larry Gorski (Ill.) also noted at the working group meeting that its mission has been fulfilled and he asks that it be disbanded. Mr. Peavy pointed out that the work of the Synthetic GIC Working Group was coordinated with the Separate Accounts (EX4) Working Group and, if changes are desired to the Synthetic Guaranteed Investment Contract Model Regulation, they need to be coordinated with the Separate Accounts Model Regulation also being considered for adoption.

Mr. Batte moved and Mr. Dunlap seconded a motion to adopt the report of the Synthetic GIC Working Group (Attachment Six).

Scott Cipinko (National Alliance Life Companies—NALC) called the attention of the working group to Section 5 of the model regulation. He said the NALC objects to the requirement of \$1 billion in admitted assets. He said the quality of a company is not dictated by its size and his organization objects to any barriers placed on the market based on company size. He said he brought this request to the working group at each of its meetings and asks the A Committee to consider removal of the language now. Bob Brown (CIGNA) drew the committee's attention to the second sentence of that paragraph, which says the commissioner may set other limits. He opined that this language, added to address the concerns of small companies, gives the commissioner flexibility to set other standards not based on company size. Roger Strauss (Iowa) said that Mr. Cipinko's comments acknowledge that his concerns have been considered by the working group. He noted that it is always an option for a state to change a model and he spoke against making a change to the draft as presented. The motion to adopt the report of the Synthetic GIC Working Group, including the model, passed.

#### 7. Review Charges for 1999 and 2000

Mr. Dailey moved and Mr. Dunlap seconded a motion to adopt the 1999 charges (Attachment Seven) and the 2000 charges (Attachment Eight) developed by the A Committee and its working groups. The motion passed.

Having no further business, the Life Insurance and Annuities (A) Committee adjourned at 11:40 a.m.

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#### ATTACHMENT ONE

##### Hearing on Viatical Settlement Orlando, Florida December 5, 1998

The Life Insurance and Annuities (A) Committee held a hearing on Dec. 5, 1998, at the Walt Disney World Dolphin Hotel in Orlando, Fla., to hear testimony about practices related to viatical settlements. First to testify was Commissioner Glenn Pomeroy (N.D.). Commissioner Pomeroy said the regulators are facing increasingly important questions relative to the viatical settlement industry. The Life Insurance and Annuities (A) Committee is the perfect place to air these issues and make public policy decisions. Commissioner Pomeroy described his first introduction to the viatical settlement industry while he was a securities regulator in North Dakota. He said North Dakota looks at this issue from the view point of protecting insured persons in the state. Potential viators need to understand the tax implications, receive other disclosures, and receive a fair amount in return for signing over the policy to the viatical settlement provider. He said North Dakota has provided for these disclosures with the first generation NAIC Viatical Settlements Model Act. Commissioner Pomeroy emphasized that he believes there is a role for viatical settlements until all insurers offer accelerated death benefits, to meet the needs of people who are in desperate need of cash. However, viatical settlement transactions must be carefully regulated.

He asked the committee to take a look at how this industry has evolved and ask itself whether the regulators are comfortable with the direction the industry is going. He asked if it is appropriate to have life insurance turned into an investment contract—"death futures," investing in a person's death. He asked regulators to consider whether there are insurable interest concerns and to deal with the public policy questions. He thanked the members of the viatical settlement industry who are working with regulators to solve these difficult issues.

Tom Foley (N.D.) described four categories of viatical settlements that need to be considered: 1) people with a life expectancy of no greater than two years; 2) the chronically ill, who do not have a normal life expectancy, but are expected to live more than two years; 3) persons with a normal life expectancy; and 4) people who do not now own life insurance. Activity takes place in all four of these categories that needs to be considered by the regulators. Mr. Foley said that the viatical settlement industry started out with people who had a very short life expectancy and typically had no dependents. The way the NAIC's Viatical Settlements Model Act is current drafted, the term "viator" applies only to categories 1 and 2.

Mr. Foley described some materials that have recently come to his attention. He described a letter to agents encouraging them to look at life insurance policies they have written to identify those who might be approached to viaticate the policies. He noted advertisements that encourage people to buy life insurance and immediately viaticate the policies. He pointed out a newspaper article that said billions of dollars of insurance are being viaticated. It concluded that "homicide becomes more than a remote possibility."

Mr. Foley recommended several courses of action to the A Committee. He asked that an "Alert" be developed to describe for investors, regulators, the media and other interested parties the direction the market is going. He said that inaction on the part of the NAIC will endorse the direction of the market. He asked the A Committee to form a working group to look at all aspects of the insurance issue such as insurable interest, solicitation of those who do not currently own insurance, etc. He asked that the current model act and regulation be frozen in place to await the results of the above activity.

Doug Head (Medical Escrow Society) spoke on behalf of the National Viatical Association and the Viatical Association of America, who have been working together on these issues. He opined that it is time for the working group and the A Committee to adopt the regulation prepared by the working group over the past months. That draft addresses categories 1 and 2 described by Mr. Foley, but does not answer questions related to categories 3 and 4, which he suggested should be a separate project. He noted that life insurance is a form of property and the owner has discretion about what to do with that property. He opined that there is a broad consumer need for viatical settlements or the industry would not have grown to the extent that it has. Holly Roth (Viaticus) suggested that the issues raised by Mr. Foley be addressed by the technical resource advisors that assisted the Viatical Settlements Working Group. She said that set of advisors included representatives from both the viatical settlement industry and the life insurance industry. Because these groups share concerns about the categories 3 and 4 described by Mr. Foley, they should work together. Cindy Martin (Mass.) asked about the position of the viatical settlement industry relative to categories 3 and 4. Mr. Head responded that the viatical associations have taken no position. He said it is an important item for discussion, but it is really not a reason to stop discussion on the Viatical Settlement Model Regulation, which covers Mr. Foley's categories 1 and 2.

Ms. Martin asked if Viaticus is now transacting business in categories 3 and 4. Gary Chodes (Viaticus) said his company currently purchases policies from category 3 individuals with a high net worth. He said in 1998 Viaticus will purchase \$300 million worth of policies, three-fourths of those from well individuals who no longer need the high amounts of coverage they purchased. Mr. Chodes said that the entire viatical settlement industry purchases approximately \$400 to \$500 million worth of insurance per year. He said this is about 4,000 to 5,000 policies. Mr. Chodes opined that it is not financially feasible to buy insurance from well people except for very large policies. Marty Carus (N.Y.) asked if Viaticus purchased policies from New York residents. Mr. Chodes said he was not sure, but he believed so. Mike Batte (N.M.) asked Mr. Chodes if his company was involved in buying structured settlements, lottery winnings, etc. Mr. Chodes responded in the negative. Mr. Carus said he assumed that viatical settlement providers could not buy policies from well individuals in a state with the NAIC model in place. Mr. Foley responded that the NAIC's model does not regulate sales of policies of well individuals, so a viatical settlement provider can do whatever it wants. Mr. Chodes confirmed that his company believes that the model and state laws only apply to terminally and chronically ill so would not prevent the sale of a policy of a well person. Tom Jacks (N.C.) said that his state researched this issue and agrees with the conclusion that it is not illegal even though it is outside the parameters of the Viatical Settlements Act adopted in North Carolina.

Commissioner Terri Vaughan (Iowa) said that three-fourths of the transactions by Viaticus by face amount are for well individuals and asked if that is typical. Mr. Chodes responded that his company is providing the vast majority of funds for sales of policies of well individuals because Viaticus has institutional capital available. Commissioner Vaughan asked if these policies are treated any differently because the individuals are well. Mr. Chodes responded that the disclosure used complies with the Viatical Settlements Model Act but it is modified where irrelevant or inappropriate. He gave as an example disclosure that the sale of a policy by a well individual will not be a tax-free event. Commissioner Vaughan asked Mr. Chodes if he thought brokers understand the difference. Mr. Chodes responded that typically they act with the aid of a financial planner or insurance agent that works with high income individuals. He said his company makes clear that it technically is not a viatical settlement. Commissioner Vaughan asked if the protections in the current draft of the Viatical Settlements Model Regulation include requirements that are not appropriate for well individuals. Mr. Chodes responded that some language is not applicable. For example, the standards for reasonable payment do not fit. Commissioner Vaughan said those testifying have not yet responded to Mr. Foley's concerns about soliciting someone to buy a policy so that it can be viaticated. She asked Mr. Chodes to provide more information. Mr. Chodes responded that his company will buy policies only of people who purchased insurance to meet a need and with the lapse of time that need no longer exists. He said it is always beyond the two-year incontestability period. He said Viaticus would not buy policies that had just been issued and does not condone that practice. He said he believed it is being done by a few agents to generate commissions and it is not clear that many, if any, will actually be purchased by a viatical

settlement provider, because the viatical settlement provider would be betting against the underwriting of the insurer. He opined that this policy would have been taken out in bad faith as a wagering contract.

Mr. Carus expressed concern that, merely because an individual is healthy, the laws on the books do not protect him. Commissioner Vaughan confirmed that the viatical settlement industry and the regulators agree that that is the case and that this subject needs review. Mr. Foley pointed out that, in his opinion, regulators should recognize that the protections in the model are poor at best. Mr. Carus asked if there was a downside to extending protection for all into the draft now and continuing to study the issue to see if there are stronger protections needed for some. Mr. Chodes said that all the definitions would need to be reviewed and changes would be needed in all sections of the model act and regulation to apply to well individuals.

Michael McNerney (Mutual Benefits Corporation) said the privacy issues and reasonable payment issues have been debated at great length in the working group. He said it is not correct to say that these issues have not been addressed, but rather a small minority does not agree with the decisions made by larger states with more experience. He opined that privacy is a code word for "we don't think the viatical settlement industry should exist." He summarized the issues as he saw them: for privacy issues, the working group has a recommendation; for reasonable payments, the working group has a recommendation; and everyone agrees that it is necessary to look at Mr. Foley's 3 and 4. He opined that it would be a mistake to stop work on the regulations covering Mr. Foley's items 1 and 2.

Julie Spiezio (American Council of Life Insurance—ACLI) said the life insurance industry has been supportive of the NAIC's model and said she came before the A Committee to talk about Mr. Foley's categories 3 and 4. She said the life insurance industry is concerned about the buying and selling of insurance on healthy lives. She said she is aware of instances where policies have been viaticated within 10 days of their purchase. People are being approached by agents and encouraged to buy a policy to viaticate. She outlined the most important issues for the life insurance customers and industry: 1) Insurable interest. It is the law that the person purchasing a policy must have an insurable interest. If someone buys a policy and then quickly sells it, he or she has violated the insurable interest law. 2) Increased fraud perpetuated on insurance companies. Individuals may stretch the truth to get the policy and then turn around and sell it, so they don't care what happens. A couple of courts have already required the insurer to pay proceeds to the viatical settlement company even though there was evidence of fraud. 3) The public policy purpose of life insurance is being weakened by this practice. Ms. Spiezio said the ACLI agrees that it would be helpful to set up a group to look at these issues.

John Matthews (Allstate Life) pointed out that more insurers are attending meetings on viatical settlements than ever before. The issues raised by Mr. Foley have gotten the attention of the ACLI and of life insurance companies. Bob Heisler (Ill.) asked if the ACLI has a recommendation on stopping work on the current Viatical Settlement Model Act. Ms. Spiezio responded that the ACLI does not take a position on the current model and traditional viatical settlements. She agreed the model is one way to go. Commissioner Vaughan asked if it was Ms. Spiezio's perception that the market for well individuals was strictly for those with high income. Mr. Spiezio responded that there seem to be some individuals who buy more than one policy and then viaticate all of them.

George Coleman (Prudential) expressed concern with the current draft of the Viatical Settlements Model Regulation, which deletes the minimum payment requirement and replaces it with a "reasonable" standard. He pointed out the model contains no authority to change the viatical settlement if regulators find it to be unreasonable. He noted that in his experience insurance departments do not like to enforce "reasonable" standards. He opined that this will tie up insurance departments' time in review. He noted that his company also had experienced an increase in individuals buying policies and immediately turning around and selling them. He said none of the information on the application would have given the company a clue that the individual planned to turn around and sell the policy. Commissioner Vaughan asked why and Mr. Matthews responded that currently his company does not have a question on its application that would help them determine this.

Lester Dunlap (La.), chair of the Viatical Settlements Working Group, asked how the A Committee wished his working group to proceed. He asked if they should go ahead and finalize the Viatical Settlements Model Regulation or stop work. Commissioner Vaughan responded that they should make recommendations to the A Committee on whether and how to proceed with a model regulation, which would be considered by the parent.

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## ATTACHMENT TWO

Viatical Settlements Working Group  
Orlando, Florida  
December 6, 1998

The Viatical Settlements Working Group of the Life Insurance and Annuities (A) Committee met in Salon IV of the Walt Disney World Dolphin Hotel in Orlando, Fla., at 3 p.m. on Dec. 6, 1998. Lester Dunlap (La.) chaired the meeting. The following working group members or their representatives were present: Elizabeth Bookwalter for Michael Bownes (Ala.); Kevin McCarty (Fla.); Robert Heisler (Ill.); Marilyn Burch (Kan.); Tom Jacks (N.C.); Tom Foley (N.D.); Dan Keating (Okla.); Louis Littlehales for Joel Ario (Ore.); and Rhonda Myron (Texas).

### 1. Consider Results of Viatical Settlements Hearing

Lester Dunlap (La.) began by summarizing the hearing held by the Life Insurance and Annuities (A) Committee. He said it was an extremely productive undertaking with good presentations on regulatory concerns. Two alternatives were suggested for the

working group: 1) to continue discussion of the Viatical Settlements Model Regulation and bring it to the A Committee for consideration; or 2) go back and reconsider the regulations provisions in light of the concerns raised at the hearing.

Tom Jacks (N.C.) recommended that the working group go forward with the draft as proposed. He said this document is a product of extensive debate. He acknowledged there are still issues regarding privacy and reasonableness but asked that the document not be put on hold while the working group considers issues related to well individuals. He said these other issues cause him great concern but states are waiting for the regulation, so it should be finished quickly. Martin Carus (N.Y.) said the working group should consider whether the draft can be expanded to cover healthy lives. This would prevent regulators from going back to the legislature twice. If the document is easy to amend so it can cover all people who might want to viaticate a policy, that should be done. Mr. Jacks said his insurance department has legislation ready to be considered in January and he does not believe that the working group can evaluate viatical settlements of the healthy by that time. Kevin McCarty (Fla.) said the draft being considered by the working group represents a well-debated model. There may be heated debate on whether the working group's model should even allow viatication of policies by healthy individuals. He suggested the working group needs to put to rest issues on chronically and terminally ill first.

Tom Foley (N.D.) said one of the North Dakota recommendations received no comment at the A Committee hearing. He had suggested development of a "Alert" package to allow regulators, investors and consumers to understand what is going on in the marketplace. He said this type of informational packet might alleviate some of New York's concerns. Marilyn Burch (Kan.) spoke in favor of the Alert package. He said Kansas is in a unique position because the securities commissioner of Kansas is the chair of a task force of securities regulators. He said insurance department staff have met with the securities regulators and have raised concerns and the Kansas Securities Commission is very supportive of the NAIC model. His state would like to go to the legislature with the model in January but would not mind going back later to add provisions for healthy lives. Mike Batte (N.M.) said New Mexico also has a committee sponsoring the model in the legislature and, assuming the model is adopted, the state will then issue regulations under the model. The regulators in New Mexico desperately need something like the Alert package to help with providing information. He suggested a charge for 1999 to look at the other issues raised in the A Committee hearing. Holly Roth (Viaticus) said she had been requested to assist in developing an informational brochure that insurance departments can use (which will become Appendix A of the model regulation) and suggested the information in this packet might be useful for the Alert package. Mr. Jacks said he also was eager to use the Alert materials to help inform consumers. He learned a lot at the hearing about activities in the viatical settlement industry and was eager to share that information with consumers in his state.

George Coleman (Prudential) reminded the working group that he raised the issue at the hearing about the elimination of the minimum payouts for those who have a life expectancy of 24 months or less. He recommend reinstating that table and using the "reasonableness" test for longer life expectancies. Julie Spiezio (American Council of Life Insurance—ACLI) said the life insurance industry has just now become interested in the Viatical Settlements Model Regulation because of their awareness of the viatication of policies by healthy individuals and the solicitation of individuals who are not insured to buy life insurance and immediately viaticate the policy. Because of the life insurance industry's increased concern, they are now looking at the regulation and several have expressed concern about the issue raised by Mr. Coleman. Ms. Spiezio said that the ACLI has supported the adoption of the Viatical Settlements Model Act in states, but cautioned that the organization may not be able to support the new regulation because of the concern expressed over this change.

Mr. Foley said that, like Mr. Jacks, he was astounded by the information he was receiving about activities in the viatical settlement industry. He raised the concern that there could be significant tax changes as a result of this activity. There is a great risk that the Treasury Department may question the tax benefit provided to life insurance minus insurable interest. He said the Alert package would spread this type of information. Andy Plant (Benefits America) agreed that the proliferation of viatical settlement industry information is good but he did not like the idea of calling the document an "alert" because it might raise alarms. Delora Schafer (Okla.) opined that "red alert" would be good. She expressed concern over the experience she had in Oklahoma, which she described as "appalling." Mr. Jacks moved that the working group separate the issues related to the model regulation from the future projects but move forward with the Alert project currently. Mr. Foley seconded the motion and it passed. Mr. Jacks then moved that the working group finish the model regulation so that it can be adopted expeditiously. Mr. McCarty seconded the motion and it passed. Mr. McCarty said that Florida has experienced viatication of thousands of contracts without incident. Unfortunately, the industry has moved dramatically from the viatication of policies of ill individuals. He now gets numerous calls from investors who were told they would get huge returns. He opined that this would have a tremendous impact on the life insurance industry with a great potential for fraud.

## 2. Consider Viatical Settlements Model Regulation

Mr. Dunlap asked the working group to give further consideration to the standards for reasonable payment that were deleted from Section 5 at a prior drafting session. He suggested putting the table back as one alternative, using the Texas standards for reasonableness as a second alternative, and letting each state decide which direction it should go. He also suggested developing a guidance manual to help states determine reasonableness. Mr. Jacks endorsed the idea. He said North Carolina already has the table in its regulation, and he does not plan to delete the table when the North Carolina regulation is revised. He said the draft described by Mr. Dunlap would acknowledge that both are good alternatives. Mr. Burch and Mike Hessler (Ill.) spoke in support of that opinion. The working group agreed to include the two alternatives in the model.

Ms. Roth said she would provide an electronic copy of her submission for Appendix A to Carolyn Johnson (NAIC/SSO) for inclusion in the next draft of the regulation. Mr. Dunlap asked for comments on the changes to the regulation (Attachment Two-A) by Feb. 1, 1999, and said the working group will hold a conference call in February to review the draft. He expressed the hope that the model could be finalized at the Spring National Meeting.

### 3. Consider Charges for 1999 and 2000

The working group considered recommendations for charges based on the discussion items from the prior working group meetings and from the A Committee hearing. Mr. McCarty said the highest priority should be given to the investment side of the viatical settlements. Dan Keating (Okla.) said that the Alert program should also be considered a high priority. Doug Head (Medical Escrow Society) said the Viatical Association of America, which he represents, is delighted that the working group will be looking at the investment side. He opined the insurance regulators are far ahead of their colleagues in the securities divisions. He said that the term "viatical" is an inappropriate term to reference sales of life insurance policies by individuals who are not terminally or chronically ill. He suggested changing the charges from "viatical settlements" to "life insurance sales."

Michael McNerney (Mutual Benefits Corp.) suggested that the charges for 2000 include development of a continuing education program for viatical settlement providers and agents.

Ms. Johnson summarized a recent court case, *Life Partners, Inc. v. Life Insurance Co. of North America*, which will affect state regulators.

Having no further business, the Viatical Settlements Working Group adjourned at 4:45 p.m.

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## ATTACHMENT TWO-A

### Viatical Settlements Model Regulation Draft: December 6, 1998

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#### Section 1. Authority

This regulation is adopted by the commissioner pursuant to the authority in Section [insert reference to state statute equivalent to Section 10 of the Viatical Settlements Model Act].

Drafting Note: States considering adoption of this version of the regulation should be sure the corresponding elements contained in the current Viatical Settlements Model Act have been put in place.

#### Section 2. Definitions

In addition to the definitions in Section [insert reference to equivalent to Section 2 of the Viatical Settlements Model Act], the following definitions apply to this regulation:

##### A. "Chronically ill" means:

- (1) Being unable to perform at least two (2) activities of daily living (i.e., eating, toileting, transferring, bathing, dressing or continence);
- (2) Requiring substantial supervision to protect the individual from threats to health and safety due to severe cognitive impairment; or
- (3) Having a level of disability similar to that described in (1) above as determined by the Secretary of Health and Human Services;

##### B. "Insured" means the person covered under the policy being considered for viatication;

C. "Life expectancy" means the mean of the number of months the individual insured under the life insurance policy to be viaticated can be expected to live as determined by the viatical settlement provider considering medical records and appropriate experiential data.

D. "Net death benefit" means the amount of the life insurance policy or certificate to be viaticated less any outstanding debts or liens;

E. "Patient identifying information" means an insured's address, telephone number, facsimile number, electronic mail address, photograph or likeness, employer, employment status, social security number, or any other information that is likely to lead to the identification of the insured; and

F. "Terminally ill" means having an illness or sickness that can reasonably be expected to result in death in twenty-four (24) months or less.

### Section 13. 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.~~

~~CA. In addition to the information required in Section [insert reference to state law equivalent to Section 3 of the Viatical Settlements Model Act], the commissioner may ask for such additional other information as is necessary to determine whether the applicant for a license as a viatical settlement provider, viatical settlement broker or viatical settlement representative complies with the requirements of Section [insert reference to state law equivalent to Section 3 of Viatical Settlements Model 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.~~

~~CB. 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) and a current copy of a letter of good standing obtained from the filing officer of the applicant's state of domicile. If a viatical settlement provider, viatical settlement broker or viatical settlement representative fails Failure to pay the renewal fee within the time prescribed, or a viatical settlement provider fails to submit the reports required in Section 6 of this Act, such nonpayment or failure to submit the required reports shall result in automatic revocation of the license. If a viatical settlement provider has, at the time of renewal, viatical settlements where the insured has not died, it shall do one of the following:~~

~~(1) Renew or maintain its current license status until the earlier of the following events:~~

~~(a) The date the viatical settlement provider properly assigns, sells or otherwise transfers the viatical settlements where the insured has not died; or~~

~~(b) The date that the last insured covered by viatical settlement transaction has died.~~

~~(2) Appoint, in writing, either the viatical settlement provider that entered into the viatical settlement, the broker who received commissions from the viatical settlement, if applicable, or any other viatical settlement provider or broker licensed in this state to make all inquiries to the viator, or the viator's designee, regarding health status of the viator or any other matters.~~

~~Drafting Note: If fees are covered in state law or a comprehensive fee regulation, delete reference to fees in Subsection B.~~

~~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.~~

~~C. The license issued to a viatical settlement provider, viatical settlement broker or viatical settlement representative shall be a limited license which that allows solicitation only of viatical settlements. It to operate only within the scope of its license.~~



~~D. Preclicensing 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 preclicensing and continuing education.~~

~~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.~~

### Section 4. Appointment Requirements for Viatical Settlement Representatives

A viatical settlement representative, as defined in [insert reference to Section 2 of Viatical Settlement Act], shall not solicit a viatical settlement contract without first obtaining an appointment from a licensed viatical settlement provider or licensed viatical settlement broker.

A. The appointment shall be made on a form required by the commissioner.

B. The appointment shall be accompanied by a fee of \$[insert amount]. The appointment may be renewed yearly by payment of a fee of \$[insert amount]. Failure to pay the renewal fee within the time prescribed may result in automatic expiration of the appointment.

C. If the appointment is revoked by either party, the appointing viatical settlement provider or viatical settlement broker shall notify the commissioner of the revocation within thirty (30) days.

### Section 4.5. Standards for Evaluation of Reasonable Payments

#### [Alternative I]

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

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

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.]

~~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.~~

#### [Alternative II]

[A viatical settlement company or broker shall not enter into a viatical settlement that provides a payment to the viator that is unreasonable or unjust. In determining whether a payment is unreasonable or unjust, the commissioner may consider, among

other factors, the life expectancy of the viator, the applicable rating of the insurance company that issued the subject policy by a rating service generally recognized by the insurance industry, regulators and consumer groups, and the prevailing discount rates in the viatical settlement market in [insert state], or if insufficient data is available for [insert state], the prevailing rates nationally or in other states that maintain this data.]

#### **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. — Reporting Requirement**

On March 1 of each calendar year, each viatical settlement provider licensed in this state shall make a report of all viatical settlement transactions where the viator is a resident of this state and for all states in the aggregate containing the following information for the previous calendar year:

##### A. — For viatical settlements contracted during the reporting period:

- (1) — Date of viatical settlement contract;
- (2) — Viator's state of residence at the time of the contract;
- (3) — Mean life expectancy of the insured at time of contract in months;
- (4) — Face amount of policy viaticated;
- (5) — Net death benefit viaticated;
- (6) — Estimated total premiums to keep policy in force for mean life expectancy;
- (7) — Net amount paid to viator;
- (8) — Source of policy (B-Broker; D-Direct Purchase; SM-Secondary Market);
- (9) — Type of coverage (I-Individual or G-Group);
- (10) — Within the contestable or suicide period, or both, at the time of viatical settlement (yes or no);
- (11) — Primary ICD Diagnosis Code, in numeric format, as defined by the international classification of diseases, as published by the U.S. Department of Health and Human Services; and
- (12) — Type of funding (I-Institutional; P-Private).

##### B. — For viatical settlements where death has occurred during the reporting period:

- (1) Date of viatical settlement contract;
- (2) Viator's state of residence at the time of the contract;
- (3) Mean life expectancy of the insured at time of contract in months;
- (4) Net death benefit collected;
- (5) Total premiums paid to maintain the policy (WP-Waiver of Premium; NA-Not Applicable);
- (6) Net amount paid to viator;
- (7) Primary ICD Diagnosis Code, in numeric format, as defined by the International classification of diseases, as published by the U.S. Department of Health and Human Services;
- (8) Date of death;
- (9) Amount of time between date of contract and date of death in months;
- (10) Difference between the number of months that passed between the date of contract and the date of death and the mean life expectancy in months as determined by the reporting company;
- C. Name and address of each viatical settlement broker through whom the reporting company purchased a policy from a viator who resided in this state at the time of contract;
- D. Number of policies reviewed and rejected; and
- E. Number of policies purchased in the secondary market as a percentage of total policies purchased.

#### Section 67. 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 contract~~, or to such other beneficiary, other than the viatical settlement provider, as the viator may thereafter designate, or in the absence of a ~~designation~~ beneficiary, 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 or cashier's check.
- C. Payment of the proceeds to the viator 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. except where, Installment payments shall not be made unless the viatical settlement company provider has purchased an annuity or similar financial instrument issued by a licensed insurance company or bank, or an affiliate of either. Retention of a portion of the proceeds by the viatical settlement provider or escrow agent is not permissible.~~
- D. A viatical settlement provider, ~~viatical settlement or~~ broker or viatical settlement representative shall not discriminate in the making or solicitation 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 viatical settlement broker or viatical settlement representative~~ shall not pay or offer to pay any finder's fee, commission or other compensation to any ~~viator's insured's~~ physician, or to an 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.~~
- ~~GF. A Viatical settlement provider and brokers shall not knowingly solicit investors who could influence the treatment of have treated or have been asked to treat the illness of the viators insured whose coverage would be the subject of the investment.~~

#### HG. Advertising standards:

- (1) Advertising should related to the viatical settlement shall 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.

H. If a viatical settlement provider enters into a viatical settlement that allows the viator to retain an interest in the policy, the viatical settlement contract shall contain the following provisions;

(1) A provision that the viatical settlement provider will effect the transfer of the amount of the death benefit only to the extent or portion of the amount viaticated. Benefits in excess of the amount viaticated shall be paid directly to the viator's beneficiary by the insurance company;

(2) A provision that the viatical settlement provider will, upon acknowledgment of the perfection of the transfer, either;

(a) Advise the insured, in writing, that the insurance company has confirmed the viator's interest in the policy; or

(b) Send a copy of the instrument sent from the insurance company to the viatical settlement company that acknowledges the viator's interest in the policy; and

(3) A provision that apportions the premiums to be paid by the viatical settlement company and the viator. It is permissible for the viatical settlement contract to specify that all premiums shall be paid by the viatical settlement company. The contract may also require that the viator reimburse the viatical settlement provider for the premiums attributable to the retained interest.

#### Section 8. Disclosure

A. A disclosure document containing the disclosures required in [insert reference to state law enacting Viatical Settlements Model Act] and this regulation shall be provided before or concurrent with taking an application for a viatical settlement contract.

B. The disclosure document shall contain the following language: "All medical, financial or personal information solicited or obtained by a viatical settlement company or viatical settlement broker about a viator and insured, including the viator and insured's identity or the identity of family members, a spouse or a significant other, is confidential." The information shall not be disclosed in any form to any person, unless disclosure:

(1) Is necessary to effect the viatical settlement between the viator and the viatical settlement provider; and

(2) The viator and insured have provided prior written consent to the disclosure.

C. The disclosure shall include advising the viator and insured that the information may be provided to financing entities including individual and institutional purchasers.

#### Section 9. Prohibited Practices

A. A viatical settlement provider, viatical settlement broker or viatical settlement representative shall not provide patient identifying information to any person, unless the insured and viator provide written consent to the release of the information at or before the time of the viatical settlement transaction pursuant to Section 8B.

B. A viatical settlement provider, viatical settlement broker or viatical settlement representative shall obtain from a person that is provided with patient identifying information a signed affirmation that the person or entity will not further divulge the information without procuring the express, written consent of the insured for the disclosure. Notwithstanding the foregoing, if a viatical settlement provider, viatical settlement broker or viatical settlement representative is served with a subpoena and, therefore, compelled to produce records containing patient identifying information, it shall notify the viator and the insured in writing at their last known addresses within five (5) business days after receiving notice of the subpoena.

C. A viatical settlement provider shall not act also as a viatical settlement broker, whether entitled to collect a fee directly or indirectly, in the same viatical settlement.

D. A viatical settlement broker 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.

E. A viatical settlement provider shall not use a longer life expectancy than is realistic in order to reduce the payout to which the viator is entitled.

Drafting Note: Market conduct examiners should review annual reports closely to detect a pattern of abuse in artificially raising the life expectancy.

#### Section 10. Insurance Company Practices

A. Life insurance companies authorized to do business in this state shall respond to a request for verification of coverage from a viatical settlement provider or a viatical settlement broker within thirty (30) calendar days of the date a request is received, subject to the following conditions:

(1) A current authorization consistent with applicable law, signed by the policyowner or certificateholder, accompanies the request;

(2) In the case of an individual policy, submission of a form substantially similar to Appendix B, which has been completed by the viatical settlement provider or the viatical settlement broker in accordance with the instructions on the form.

(3) In the case of group insurance coverage:

(1) Submission of a form substantially similar to Appendix C, which has been completed by the viatical settlement provider or viatical settlement broker in accordance with the instructions on the form, and

(2) Which has previously been referred to the group policyholder and completed to the extent the information is available to the group policyholder.

B. Nothing in this section shall prohibit a life insurance company and a viatical settlement provider or a viatical settlement broker from using another verification of coverage form that has been mutually agreed upon in writing in advance of submission of the request.

C. A life insurance company may not charge a fee for responding to a request for information from a viatical settlement provider or viatical settlement broker in compliance with this section in excess of any usual and customary charges to contractholders, certificateholders or insureds for similar services.

D. The life insurance company may send an acknowledgment of receipt of the request for verification of coverage to the policyowner or certificateholder and, where the policy owner or certificate owner is other than the insured, to the insured. The acknowledgment may contain a general description of any accelerated death benefit that is available under a provision of or rider to the life insurance contract.

#### Section 11. Effective Date

This regulation is effective [insert date]. A viatical settlement provider, viatical settlement broker or viatical settlement representative transacting business in this state may continue to do so pending approval of the provider, broker or representative's application for a license as long as the application is filed with the commissioner by [insert date].

#### APPENDIX A Informational Brochure [All new material]

Some life insurance policy holders and some investors may be interested in a new option available in the changing life insurance market. Individuals with terminal or chronic illnesses are able to sell their life insurance for a percentage of the face value of the policy, thereby obtaining immediate cash. The transaction is called a viatical settlement. This brochure defines some basic terms and offers other important tips for policyowners considering a viatical settlement. It also explores key questions for potential viatical settlement investors to consider.

##### Common Terms:

- **Viatical Settlement:** The proceeds from the sale or assignment of a life insurance policy, either individual or group, which insures the life of a terminally or chronically ill individual to a third party (known as a viatical settlement provider). The new owner maintains any premium payments, and eventually collects the entire death benefit.
- **Viator (seller):** The owner of a life insurance policy or certificate which is the subject of a viatical settlement.
- **Viatical Settlement Broker:** An individual or company representing the seller (viator) who "shops" the policy to more than one viatical provider, creating competitive bidding for the policy, in return for a commission paid by the viatical settlement provider on the eventual sale. No commission is paid if the viatical settlement is not effected.
- **Viatical Settlement Provider (purchaser/buyer):** The purchaser of a life insurance policy insuring the life of a terminally or chronically ill individual.
- **Viatical Settlement Agent or Representative:** An individual or company representing either a single viatical settlement provider or viatical settlement broker.

A viatical settlement is the sale of a life insurance policy to a third party, (typically a licensed viatical settlement provider) wherein the policy holder receives cash during his or her lifetime. In these transactions, the viatical settlement provider becomes the owner and/or beneficiary of the life insurance policy and maintains the premium payments, collecting the death benefit of the policy upon the death of the insured.

Most life insurance policies, including individual, employer-sponsored group and association life policies, allow for assignment or sale of such coverage to a third party, including a viatical settlement provider. Also, both the Federal Government and the U.S. Military allows its employees or personnel to assign or convert their coverage for viatical settlements.

#### Accelerated Death Benefits

Some insurance companies offer a rider to pay a portion, typically 25% to 50%, of the policy's death benefit, minus any policy debt, before the death of the insured. Such companies will pay this amount for an insured diagnosed as terminally ill, although certain illness limitations may apply, and with a relatively short life expectancy, typically a year or less. Upon the death of the insured, the beneficiaries receive the remainder of the death benefit. In some cases the policy holder may pay an additional premium on the base policy for this option or the insurer may assess a small service fee against the death benefit or accelerated (advanced) payment. You should contact your insurance company or agent to determine if your policy includes such a provision.

#### Viatical Settlements

A viatical settlement can provide a cash benefit before the death of an insured for the policyholder, called a "Viator." The term "viatical" comes from the Latin word "Viaticum" which means supplies for a long journey.

In a viatical settlement, a viator sells the "face value" (the amount payable to the beneficiaries) of a life insurance policy to a viatical settlement provider in return for an immediate cash payment. The viator will receive a negotiated payment for less than the face value. In return, the viatical provider, investor or trust will become the owner of and/or beneficiary under the life insurance policy.

A viatical settlement, like any complex financial or legal transaction, requires close scrutiny. When considering such a settlement, you may wish to consult one or more of the following: an attorney, physician, life insurance agent or company, tax advisor, accountant or financial planner. A viatical settlement may not be in the best interest of a viator since each individual has specific financial and personal needs. In certain cases, alternative options include: borrowing from your policy's cash value; or canceling the policy and using its surrender value; or borrowing against the value of your policy from a lending institution. Additionally, you may wish to contact representatives of any government agency which may be providing government benefits or entitlements, as the proceeds from a viatical settlement may affect eligibility for such government programs and services.

The (STATE) Department (REGULATES/DOES NOT REGULATE) viatical settlement providers and brokers, and their representatives. For special requirements affecting viatical settlements, and a complete list of authorized providers, brokers, and their representatives in the state of (STATE) call the Department of Insurance at (PHONE).

#### The Process

Viators who are contemplating a viatical settlement should understand how the process works and the timing of its various phases. The entire viatical settlement process takes 2 to 6 weeks depending on turn-around time at each phase, which varies from case to case, and can take longer.

##### Phase 1—Underwriting process:

Once a viatical settlement broker or provider receives a viator's application and the necessary signed authorizations for the release of medical and other pertinent information, the broker or provider contacts the appropriate:

1. Attending physician and/or clinic for complete medical records. The viatical settlement provider utilizes these records in determining the insured's life expectancy and may use in-house or third-party medical reviewers, or a combination of both. Depending on their methods and assumptions, life expectancies may vary from one provider to the next. All medical information obtained is subject to state law relating to confidentiality of medical information.
2. Insurance company for policy information. The broker and provider utilize this information to determine if the policy has any limitations or restrictions that would affect or impede the viatical settlement. With group life insurance, the broker or provider may also need to contact the administrator of a policy.

Each of the brokers or providers you have applied with will contact your doctor for medical records and insurance company for policy information.

##### Phase 2—Offer process:

The viatical settlement provider(s), using the information obtained in the underwriting phase, determine(s) an offer. In determining a proposal, a viatical settlement provider takes into account various factors, including:

- Estimated life expectancy and medical condition of the insured. Generally, the shorter the life expectancy of the insured, the more the viatical settlement provider will offer for the policy.

- The amount of life insurance coverage.
- Loans or advances, if any, previously taken against the policy.
- Amount of premiums necessary to keep the life insurance policy in force.
- The rating of the issuing insurance company.
- Prevailing interest rates.
- State laws, if any, that may affect the policy or transaction.

#### Phase 3—Closing process:

1. Upon accepting the offer, a closing package is forwarded to the viator. While closing documents will vary from one funding company to another, they typically include an offer letter, a viatical settlement contract, and the applicable insurance company change forms necessary to transfer the policy.
2. The closing documents are then returned to the provider for signature.
3. The viatical provider will place the proceeds in escrow (See General Consumer Tips) and send the signed insurance change forms to the insurance company for recording.

#### Phase 4—Funding process:

Once the insurance company notifies the viatical settlement provider that the changes on the life insurance policy have been recorded, funds are released to the viator, usually the next business day.

This is a relatively simple procedure similar to the process associated with selling a house. A property is listed or offered by the owner; an offer is extended; an offer is accepted and funds are escrowed; the sale is closed only with the agreement of all parties and the assets are transferred.

#### General Consumer Tips for Viators:

If after reading this brochure you decide to pursue a viatical settlement, consider the following guidelines for making an informed decision:

- In order to determine the market value of your policy, you may wish to contact several viatical settlement providers or use a viatical settlement broker to contact several providers for you.
- Remember that you are not obligated to accept a particular viatical settlement offer. You can delay a sale or ask for new offers at any time before the settlement is completed. In most states, you have the right to change your mind about the settlement up to 15 days after you receive the proceeds, provided that you return all of the proceeds. Be sure your right of rescission is clearly stated in the viatical contract.
- Make sure the purchaser uses an escrow account with an independent escrow agent or financial institution to ensure the safe transfer of proceeds. Like a real estate transaction, you want assurance of the proper transfer of your money, and the viatical settlement provider or investor should ensure this by depositing the full value of the offer you accept into the escrow account.
- Prior to accepting an offer, you should ask what will happen to any dividends, additional increases in the face amount of the policy, accidental death benefits or other benefits under the policy once you have entered into the viatical settlement. Depending on your policy and the issuing company, you may be able to retain these additional benefits. You may wish to seek the advice of your insurance agent.
- Make sure you are comfortable with the confidentiality provisions offered by each party to the viatical settlement. You will want to note the conditions under which there may be an obligation, both during the settlement process and after the settlement is complete, to release further medical information, or to disclose other information about your life insurance policy or your medical condition. Parties to the transaction may include any or all of the following: a viatical settlement provider, a viatical settlement broker, or a representative of either of these entities; an escrow agent; an individual investor; a medical underwriter; other advisors or consultants.
- Understand the time frame for your viatical settlement. While each transaction varies, the probable time frame is 2 to 6 weeks from the initial call. Various circumstances, which a broker or provider can discuss with you, can lengthen that time.
- Understand where the viatical settlement provider obtains fund to purchase the policy. In general, there are three financial structures: self-funding, institutional funding and individual investors. To purchase policies: self-funded companies use their own financial resources as capital; institutionally-funded companies rely on institutional investors, like lending establishments or pension funds; and individual investor-funded companies use capital obtained from individual investors.
- The purchaser is allowed to contact the viator after the settlement has taken place, but there are limitations. For the purpose of determining the health of the insured, a viatical settlement provider, viatical settlement broker or viatical settlement representative may contact you up to once every three months for insureds with a life expectancy of more than one year, and no more than once per month for insureds with a life expectancy of one year or less.

- As a result of passage of the 1996 Health Insurance Portability and Accountability Act, the proceeds from these settlements are free of federal tax for two groups of people: (1) persons who have been diagnosed with a terminal illness and with a life expectancy of 24 months or less and (2) certain chronically ill individuals. If you qualify for this federal tax-free advantage, you must use a viatical settlement provider who is licensed in the state where you live, or, in states where licensing is not required, who complies with the standards of the National Association of Insurance Commissioners Model Viatical Settlement Act. Check with your financial or tax adviser.

Viators should understand that some states regulate viatical settlements and some states do not. The National Association of Insurance Commissioners has adopted model legislation for such transactions with the intent of protecting the viator.

#### General Tips for Viatical Settlement Investors.

People make investments for many reasons. But most rely on this fundamental understanding; investments which offer high returns usually involve greater risk. Viatical settlement investors should carefully weigh the risk of losing their investment against the potential return. Some key issues to understand include the following:

- Determine who holds the responsibility to pay premiums on the policy. A lapse in premium payments may lead to the loss of your entire investment.
- The life expectancy of the insured is a medical estimate, not a guarantee. The actual life span of the insured, not the estimate, will determine when an investor is paid. This, in turn, will impact the actual return on the investment. Ask who is making the life expectancy estimate and their credentials/experience. Additionally, inquire about medical research regarding the success of new treatments or drug advancements for the treatment of the illness or illnesses suffered by the insured.
- What type of statements will investors receive about the status of their investment? Are there extra fees for this service? How will the investor know when their investment has matured? Who will obtain the death certificate and file the claim with the insurance company and will this involve an extra fee?
- What control do you retain over your investment? If you personally suffer some emergency, is there any provision for the return of all or a part of your investment? What would be the cost of such an event?
- Could you lose or tie up investment dollars indefinitely if the provider company or the insurance company go bankrupt? What financial information or written statements will the provider disclose to you about the provider's history or reliability?
- Will the insurer and potential heirs of the viator agree to a change of beneficiary? Do the heirs have any lawsuits pending against the viator which may affect the security of your designation as beneficiary?
- With respect to financial stability, how do rating services, such as A.M. Best, Standard & Poor's Corp., and Moody's Investor Services, rate the insurance company offering the policy?

The Viatical Association of America developed the following standard disclosures for investors which should be part of your understanding and agreement with the provider when you provide investment funds.

- The annual return on a viatical settlement transaction depends on the accurate estimate of the insured's life expectancy and the timing of his/her demise. An "annual return" can never be "guaranteed."
- Know the identity of the party or parties who would be responsible for future premiums after the investor purchases the policy, and how these premium payments are guaranteed. If premiums are prepaid in escrow for a certain period of time, the identity of the party who would pay premiums if the insured lives beyond his/her life expectancy. The policy may lapse if premiums are not paid.
- If a policy is on waiver of premium, and the insured's health improves to where he/she is no longer disabled, the member company shall disclose who would be responsible for the payment of premiums.
- There are certain risks peculiar to group policies, owned by employers or other organizations. The primary risk is the possibility that the owner or the insurance company may terminate the group policy. This termination will trigger the need to convert the group coverage to an individual policy. Member companies shall disclose if there are any limitations or caps in the conversion rights and that additional premiums will have to be paid once the policy is converted, as well as identify the party responsible for the payment of such additional premiums.
- Viatical settlement companies shall disclose who determines the life expectancy of the insured, e.g., with in-house staff, independent physicians, specialty firms that weigh medical and actuarial data, etc. These parties make the determination of life expectancy based on medical evidence presented to the viatical company by the insured's physician and/or hospital. Developments in medical treatments or unexpected changes in the insured's medical condition could affect the accuracy of such determination.
- Insurance companies may contest death claims for policies that have not been in effect for more than two years at the date of death and the death benefit payment could be denied on various grounds. If the insured commits suicide within two years of the issuance of the policy, the insurance company may not pay the death benefits.
- The purchase of a viatical settlement should not be considered a liquid investment, since it is impossible to predict the exact timing of its maturity and the funds may not be available until the death of the insured.



- Member companies should not offer purchasers examples of matured policies and rates of return without disclosing how many other policies purchased by that company are still outstanding—or have matured—beyond the estimated life expectancy of the insured.
- Under certain conditions, the insurance company may cancel the waiver of premium status on certain policies. In this event, premium payments will then be required and member companies shall identify the party or parties who shall be required to make those payments.

Investors should understand that some states regulate viatical settlements and some states do not.

**APPENDIX B** [All new material]

**Standardized Viatical Settlement  
Verification Of Coverage For Individual Policies**

**Section One: (To be completed by the Viatical Settlement Provider or Viatical Settlement Broker)**

Insurance Company: _____	Name of Policyowner: _____
Policy Number: _____	Owner's Social Security Number: _____
Name of Insured: _____	Policyowner's Address: _____
	Street
Insured's date of birth: _____	City/State

Please provide the information requested in Section Two (below) with regard to the policy identified above and in accordance with the attached authorization.

In addition, please provide the forms checked below which are available from your company to complete a viatical settlement transaction:

- ☐ Absolute Assignment/Change of Ownership/Viatical Assignment Form
- ☐ Change of Beneficiary
- ☐ Release of Irrevocable Beneficiary (if applicable)
- ☐ Waiver of Premium Claim Form
- ☐ Disability Waiver of Premium Approval Letter

_____ Date	_____ Signature of a representative of Viatical Settlement Broker or Viatical Settlement Provider  _____ _____ Full name and address of Viatical Settlement Broker or Viatical Settlement Provider
---------------	---

**Section Two: (To be completed by the life insurance company)**

- 1) Face amount of policy: \$ \_\_\_\_\_
- 2) Original date of issue: \_\_\_\_\_ / \_\_\_\_\_ / \_\_\_\_\_ Month/Date/Year)
- 3) Was face amount increased after original issue date? ☐ no ☐ yes
  - a) If yes, when: \_\_\_\_\_ / \_\_\_\_\_ / \_\_\_\_\_
- 4) Type of Policy: \_\_\_\_\_ (Term/Whole Life/Universal Life/Variable Life)
- 5) Is policy participating? ☐ no ☐ yes
  - a) If yes, what is current dividend election? \_\_\_\_\_
- 6) Current Net Death Benefit: \_\_\_\_\_ (Enter full amount payable, including any additional insurance, and/or dividends accumulated at interest, minus policy loans, outstanding interest on policy loans and/or accelerated death benefits paid)

7) Current cash value: \$ \_\_\_\_\_ (Enter full amount, including cash value of any additional insurance and/or dividends accumulated at interest, minus policy loans and outstanding interest on policy loans)

8) Terms of policy loans:

- a) Amount of policy loans: \$ \_\_\_\_\_  
 b) Amount of outstanding interest on policy loan: \$ \_\_\_\_\_  
 c) Current interest rate: \_\_\_\_\_

9) Is policy in force? ☐ no ☐ yes

- a) If yes, has policy ever been reinstated? ☐ no ☐ yes  
 If yes, date of reinstatement: \_\_\_\_\_/\_\_\_\_\_/\_\_\_\_\_

10) Has policy lapsed? ☐ no ☐ yes

- a) If yes, when did policy lapse? \_\_\_\_\_/\_\_\_\_\_/\_\_\_\_\_  
 If policy has lapsed, is coverage continued under non-forfeiture option? ☐ no ☐ yes  
 If yes, indicate which option, amount of coverage, duration, etc.: \_\_\_\_\_

11) Amount of Contract/Scheduled premiums: \$ \_\_\_\_\_

12) Current premium mode: \_\_\_\_\_ (Monthly, semi-annually, etc.)

- a) When is next premium due? \_\_\_\_\_/\_\_\_\_\_/\_\_\_\_\_ (Month/Day/Year)

13) Does the policy include a Disability Premium Waiver provision/rider? ☐ no ☐ yes

- a) If yes, are premiums currently being waived? ☐ no ☐ yes  
 b) If yes, since when? \_\_\_\_\_/\_\_\_\_\_/\_\_\_\_\_  
 c) How often is continued eligibility reviewed? \_\_\_\_\_  
 d) When is next review? \_\_\_\_\_/\_\_\_\_\_/\_\_\_\_\_

14) Can payment of all or part of the death benefit be accelerated under this policy? ☐ no ☐ yes

- a) If yes, by what method is the benefit calculated, the lien method or the discount method? \_\_\_\_\_  
 b) If lien method, what is the interest rate? \_\_\_\_\_

15) Has a claim for Accelerated Death Benefit been submitted? ☐ no ☐ yes

- a) If yes, was payment made under this provision? ☐ no ☐ yes  
 Amount paid: \_\_\_\_\_ Date paid: \_\_\_\_\_

16) Do current records show any assignments of record? ☐ no ☐ yes

17) Do current records show any outstanding liens or encumbrances of record? ☐ no ☐ yes

18) Please identify current primary beneficiaries: \_\_\_\_\_

- a) Are they named irrevocably, or is owner otherwise limited in designation of new beneficiaries? ☐ no ☐ yes

19) Have any riders been added to this policy after issue? ☐ no ☐ yes

If yes, please identify: \_\_\_\_\_

20) If an ownership or beneficiary change or assignment were to be made on this policy, to whom would the completed forms be sent?

Name: \_\_\_\_\_ Title: \_\_\_\_\_

Company Name: \_\_\_\_\_ Department: \_\_\_\_\_

Address (No P.O. Box, please) \_\_\_\_\_

City: \_\_\_\_\_ State: \_\_\_\_\_ ZIP: \_\_\_\_\_

Telephone No: \_\_\_\_\_ Fax: \_\_\_\_\_

The answers provided reflect information contained in the company's records as of: \_\_\_\_\_ (date)

Signature: \_\_\_\_\_ Name: (Printed) \_\_\_\_\_

Title: \_\_\_\_\_

Company: \_\_\_\_\_

Direct Telephone No: \_\_\_\_\_ Direct Fax No: \_\_\_\_\_

APPENDIX C [All new material]STANDARDIZED VIATICAL SETTLEMENT VERIFICATION OF  
GROUP LIFE INSURANCE BENEFITS

Section One: (To be completed by the viatical settlement provider or viatical settlement broker)

Insurance Company

Name of Employee/Member

Employer/Policyholder Name

Insured's Date of Birth

Policy Number

Insured's Social Security Number

Certificate Number

Employee/Membership Number

Please provide the information requested in Section Two or Section Three, as appropriate, with regard to the individual and coverage described, in accordance with the attached authorization.

In addition, please provide the forms checked below which are available from your company to complete a viatical settlement transaction:

- ☐ Absolute Assignment  
☐ Change of Beneficiary (irrevocable if applicable)  
☐ Disability Waiver of premium claim or  
☐ Disability Waiver of premium award letter

Date

Signature of a representative of Viatical Settlement Broker  
or Viatical Settlement ProviderFull name and address of Viatical Settlement Broker  
or Viatical Settlement Provider

Section Two: (To be completed by the employer/group policyholder)

## 1) BASIC COVERAGE:

- a) Is the plan self-insured or is coverage provided under a group policy issued by a life insurance company? \_\_\_\_\_  
 If by a group policy, please provide the name of the insurance company for BASIC life insurance coverage: \_\_\_\_\_  
 b) Effective date of BASIC life insurance coverage: \_\_\_\_\_  
 c) Face amount of BASIC life insurance: \_\_\_\_\_  
 d) Does BASIC coverage plan have contestable provisions? ☐ no ☐ yes  
 e) Is BASIC coverage subject to a suicide provision? ☐ no ☐ yes  
 f) Monthly premium paid by employer/group policyholder for BASIC life insurance: \$ \_\_\_\_\_  
 g) Monthly premium paid by employee/insured for BASIC life insurance: \$ \_\_\_\_\_  
 h) Is BASIC life insurance coverage ☐ Term ☐ Universal Life?  
 i) If Universal Life, please indicate cash value, if any: \_\_\_\_\_ Is this amount payable in  
 addition to the face amount? ☐ no ☐ yes  
 i) Is coverage in force? ☐ no ☐ yes  
 j) When is next premium due? \_\_\_\_\_  
 k) Has employee's coverage under this plan ever been reinstated? ☐ no ☐ yes  
 i) If yes, date of reinstatement: \_\_\_\_\_

## 2) SUPPLEMENTAL (OPTIONAL) COVERAGE

- a) Insurance Company for SUPPLEMENTAL life insurance coverage: \_\_\_\_\_  
 b) Effective date of SUPPLEMENTAL life insurance coverage: \_\_\_\_\_  
 c) Face amount of SUPPLEMENTAL life insurance: \_\_\_\_\_  
 d) Does SUPPLEMENTAL coverage plan have contestable provisions? ☐ no ☐ yes  
 e) Is SUPPLEMENTAL coverage subject to a suicide provision? ☐ no ☐ yes  
 f) Monthly premium paid by employer/group policyholder for SUPPLEMENTAL life insurance: \$ \_\_\_\_\_  
 g) Monthly premium paid by employee/insured for SUPPLEMENTAL life insurance: \$ \_\_\_\_\_

h) Is SUPPLEMENTAL life insurance coverage ☐ Term ☐ Universal Life?  
 i) If Universal Life, please indicate cash value, if any: \_\_\_\_\_ Is this amount payable in addition to the face amount? ☐ no ☐ yes  
 i) Is coverage in force? ☐ no ☐ yes  
 j) When is next premium due? \_\_\_\_\_  
 k) Has employee's coverage under this policy ever been reinstated? ☐ no ☐ yes  
 i) If yes, date of reinstatement: \_\_\_\_\_

3) **DISABILITY WAIVER OF PREMIUM**  
 a) Does plan provide for waiver of premium in the event of employee/insured's disability?  
 BASIC ☐ no ☐ yes What is the waiting period? \_\_\_\_\_  
 SUPPLEMENTAL ☐ no ☐ yes What is the waiting period? \_\_\_\_\_  
 b) Are premiums currently being waived under disability premium waiver?  
 BASIC? ☐ no ☐ yes  
 SUPPLEMENTAL? ☐ no ☐ yes  
 c) Who pays premiums under disability premium waiver?  
 BASIC ☐ Insurance carrier ☐ Employer  
 SUPPLEMENTAL ☐ Insurance carrier ☐ Employer  
 d) What was the date of approval? \_\_\_\_\_  
 e) Next review date? \_\_\_\_\_  
 f) If the insured is no longer eligible for waiver, what amount of coverage can be converted to an individual policy? \$ \_\_\_\_\_  
 i) Will a new suicide/contestability clause be in effect for the converted policy? ☐ no ☐ yes  
 ii) Will assignee be notified if insured is no longer eligible for waiver? ☐ no ☐ yes

4) **BENEFICIARIES, ASSIGNMENTS AND LIMITATIONS**  
 a) Who are the primary beneficiaries of the coverage(s)?  
 BASIC \_\_\_\_\_  
 SUPPLEMENTAL \_\_\_\_\_  
 b) Is any beneficiary under this policy designated irrevocably, or is insured otherwise limited in designation of new beneficiaries? ☐ no ☐ yes  
 c) Can this coverage be assigned?  
 BASIC ☐ no ☐ yes  
 If yes, to a corporation? ☐ no ☐ yes To someone not related to insured? ☐ no ☐ yes  
 SUPPLEMENTAL ☐ no ☐ yes  
 If yes, to a corporation? ☐ no ☐ yes To someone not related to insured? ☐ no ☐ yes  
 d) Do records show any assignments of record? ☐ no ☐ yes  
 e) Do records show any outstanding liens or encumbrances of record? ☐ no ☐ yes  
 f) Will an Assignee be notified if the master policy is canceled? ☐ no ☐ yes  
 g) Can Assignee convert the coverage without the permission of insured? ☐ no ☐ yes

5) **ACCELERATED DEATH BENEFITS**  
 a) Is there an Accelerated Death Benefit available under the coverage?  
 BASIC ☐ no ☐ yes  
 SUPPLEMENTAL ☐ no ☐ yes  
 b) Has request for Accelerated Death Benefit been made? ☐ no ☐ yes  
 c) Has payment been made to insured under this provision? ☐ no ☐ yes  
 i) Amount paid: \_\_\_\_\_ Date paid: \_\_\_\_\_  
 ii) Is this amount a lien against death proceeds? ☐ no ☐ yes Interest rate \_\_\_\_\_

6) **MISCELLANEOUS**  
 a) Is coverage portable?  
 BASIC ☐ no ☐ yes  
 SUPPLEMENTAL ☐ no ☐ yes  
 b) If insured is no longer eligible for coverage under the group, will Assignee be notified? ☐ no ☐ yes  
 c) Is this plan administered by a third party? ☐ no ☐ yes  
 If yes, please provide the name, address and telephone number of administrator:  
 Name: \_\_\_\_\_ Title: \_\_\_\_\_  
 Company name: \_\_\_\_\_ Department: \_\_\_\_\_  
 Street Address: \_\_\_\_\_  
 (No P.O. Box please)  
 City: \_\_\_\_\_ State: \_\_\_\_\_ ZIP: \_\_\_\_\_  
 Telephone number: ( ) \_\_\_\_\_ Fax: ( ) \_\_\_\_\_

If a change of beneficiary form or assignment were to be made for this coverage, to whom should the completed forms be sent?

Name: \_\_\_\_\_ Title: \_\_\_\_\_

Company name: \_\_\_\_\_ Department: \_\_\_\_\_

Street Address: \_\_\_\_\_  
(No P.O. Box please)

City: \_\_\_\_\_ State: \_\_\_\_\_ ZIP: \_\_\_\_\_

Telephone number: ( ) \_\_\_\_\_ Fax: ( ) \_\_\_\_\_

The answers provided reflect information in our files as of \_\_\_\_\_ (date).

Signature: \_\_\_\_\_ Name: \_\_\_\_\_

Date: \_\_\_\_\_ Title: \_\_\_\_\_

Company: \_\_\_\_\_

Direct telephone number: ( ) \_\_\_\_\_ Direct fax number: ( ) \_\_\_\_\_

Information not provided by the employer may be obtained from the insurance company if different from administrator identified above:

Name: \_\_\_\_\_ Title: \_\_\_\_\_

Company name: \_\_\_\_\_ Department: \_\_\_\_\_

Address: \_\_\_\_\_

City: \_\_\_\_\_ State: \_\_\_\_\_ ZIP: \_\_\_\_\_

Telephone number: ( ) \_\_\_\_\_ Fax: ( ) \_\_\_\_\_

### Section Three:

Under the terms of Section 10 of the NAIC Model Viatical Settlement Regulation covering insurance company practices, the insurance company or the third-party administrator named above is requested to complete the information not provided by the employer in Section Two, above, Items number: \_\_\_\_\_

The answers provided to the identified questions reflect information in the files of the insurance company as of \_\_\_\_\_ (date).

Signature: \_\_\_\_\_ Name: \_\_\_\_\_

Date: \_\_\_\_\_ Title: \_\_\_\_\_

Company: \_\_\_\_\_

Direct telephone number: ( ) \_\_\_\_\_ Direct fax number: ( ) \_\_\_\_\_

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### ATTACHMENT THREE

Life Disclosure Working Group  
Orlando, Florida  
December 7, 1998

The Life Disclosure Working Group of the Life Insurance and Annuities (A) Committee met in Salon E3 of the Walt Disney World Dolphin Hotel in Orlando, Fla., at 10 a.m. on Dec. 7, 1998. Tom Foley (N.D.) chaired the meeting. The following working group members or their representatives were present: John Hartnedy (Ark.); Sheldon Summers (Calif.); Roger Strauss (Iowa); Lester Dunlap (La.); Paul DeAngelo (N.J.); Mike Batte (N.M.); Louis Belo (N.C.); Dan Keating (Okla.); and Mary Keller (Texas).

### 1. Consider Adoption of Annuity Disclosure Model Regulation

Roger Strauss (Iowa) said the only substantive issue left to discuss is whether the free look should be 15 or 30 days. Mr. Strauss moved to adopt a 15-day free look with the proviso that, if a free look is already in place in the state, this runs concurrent with the already existing provision. The motion was seconded by Lester Dunlap (La.). Tom Foley (N.D.) summarized that the model would then require the buyer's guide to be delivered at or before the time of application in a face-to-face meeting; but if no face-to-face meeting occurs, the buyer's guide would be delivered within five days and a 15-day free look would be allowed after the contract was received. Mary Keller (Texas) asked how the 15-day period was measured. She asked if it starts to run when the purchaser receives the contract or when the company mails it. She asked also when the period ends; when the applicant sends the contract back or when the company receives it. Julie Spiezio (American Council of Life Insurance—ACLI) said all 50 states and the District of Columbia now have a free-look period for life insurance, so this is not something new for insurers to deal with. The practice is to count from the day the insurer expects the applicant would receive the contract and to end with the postmark on the returned contract or the date the individual gives it to the agent. She said companies have had no trouble interrupting the provisions now in place and opined that it was not necessary to add these specifics in the model regulation. The motion to adopt the 15-day free-look period passed.

Mr. Strauss pointed out that the technical resource advisors submitted several comments for technical corrections to the model and he expressed support for those changes. Paul DeAngelo (N.J.) questioned the provision of Section 5A(2)(a) that considers the issue of Internet sales. He asked if a person can always print off a document that is on a Web site or whether some individuals might not have that technical capacity. Mr. Foley suggested rephrasing the provision to say that insurers should maximize the ability to view and print the buyer's guide. The working group agreed to this suggestion. Howard Greene (Teachers Insurance and Annuity Association—TIAA) pointed out a comment in his company's submission that suggests offering the opportunity to get a buyer's guide from the insurance department or the insurer. The working group agreed to that change. The working group reviewed several other technical changes suggested by the technical resource advisors and agreed to include those in Section 5. Mr. Strauss moved and Mr. DeAngelo seconded a motion to adopt the Annuity Disclosure Model Regulation (Attachment Three-A). The motion passed.

### 2. Give Direction to American Academy of Actuaries on Self Support and Lapse Support Tests for Annuities

Mr. Foley said the American Academy of Actuaries (AAA) has been reviewing the issues of self support and lapse support for the prior year. Under consideration is whether to take concepts from the Life Insurance Illustrations Model Regulation and apply those to annuities. He said the project has been losing steam because it appears that insurers seldom use annuity illustrations. Mr. Foley said he was more comfortable that the current level of disclosure alerts applicants that they need to understand the "trust me" concept so that they will deal with reputable companies. He said he no longer thinks the self support and lapse support tests need to be pursued by the AAA. Don Pearsall (N.Y.) said a new law mandates the department to have self support and lapse support tests. Barbara Lautzenheiser (Lautzenheiser & Associates), on behalf of the AAA, said the New York law deals with the *issue* of the contract, whereas the working group was considering *disclosure*. The AAA intends to assist New York in developing its standards and, if the working group decides to include them later, the New York efforts can hopefully be modified.

### 3. Issues Related to Life Insurance Illustrations

Mr. Foley said he asked Carolyn Johnson (NAIC/SSO) to identify issues related to life insurance illustrations that had been discussed at prior meetings (Attachment Three-B). Mr. Foley asked the members of the working group and interested parties to review that list and to be prepared to discuss it at the Spring National Meeting. He invited participants to change or add to that list as necessary. George Coleman (Prudential) said interested parties have worked hard in advocating consistency in state adoptions of the Life Insurance Illustrations Model Regulation. He said they would not want to see wholesale changes made to the model that has been adopted by 32 states. Mr. Foley asked if those adoptions are generally uniform. Mr. Coleman responded that there have been several minor deviations but most states have been very faithful to the model. Most of the changes that did occur have not required any software modifications by the companies. Mr. Coleman pointed out that there are no programmers available now to deal with software changes, so he would not want to see major changes made to the model. Mr. Foley agreed that the intent of the working group is to make technical changes to the model that were identified when the Life Disclosure Working Group prepared questions and answers to assist in implementation of the Life Insurance Illustrations Model Regulation.

### 4. Adopt Minutes of Oct. 20, 1998, Conference Call

Mr. Strauss moved and Mr. Dunlap seconded a motion to adopt the minutes of the Oct. 20, 1998, conference call (Attachment Three-C). The motion passed.

### 5. Consider Charges for the Working Group

The working group reviewed the 1998 charges and identified that only one of the four charges applicable to this working group have been completed. The working group decided to move the other charges to 1999. Mr. Foley suggested a 2000 charge to review the Annuity Disclosure Model Regulation and the buyer's guide for possible changes. Mr. DeAngelo said that the Suitability Working Group is identifying problems with the Life Insurance Advertising Model Regulation and will include issues related to illustrations and disclosure in its review.

Having no further business, the Life Disclosure Working Group adjourned at 11:45 a.m.

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## ATTACHMENT THREE-A

Annuity Disclosure Model Regulation  
 Draft: December 7, 1998  
 Adopted by the Life Insurance and Annuities (A) Committee

## Table of Contents

Section 1.	Purpose
Section 2.	Authority
Section 3.	Applicability and Scope
Section 4.	Definitions
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Section 6.	Report to Contract Owners
Section 7.	Penalties
Section 8.	Separability
Section 9.	Effective Date
Appendix A.	Buyer's Guide

## Section 1. Purpose

The purpose of this regulation is to provide standards for the disclosure of certain minimum information about annuity contracts to protect consumers and foster consumer education. The regulation specifies the minimum information which must be disclosed and the method for disclosing it in connection with the sale of annuity contracts. The goal of this regulation is to ensure that purchasers of annuity contracts understand certain basic features of annuity contracts.

## 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].

## Section 3. Applicability and Scope

This regulation applies to all group and individual annuity contracts and certificates except:

- A. Registered or non-registered variable annuities or other registered products;
- B. Immediate and deferred annuities that contain no nonguaranteed elements;
- C. (1) Annuities used to fund:
  - (a) An employee pension plan which is covered by the Employee Retirement Income Security Act (ERISA);
  - (b) A plan described by Sections 401(a), 401(k) or 403(b) of the Internal Revenue Code, where the plan, for purposes of ERISA, is established or maintained by an employer;
  - (c) A governmental or church plan defined in Section 414 or a deferred compensation plan of a state or local government or a tax exempt organization under Section 457 of the Internal Revenue Code; or
  - (d) A nonqualified deferred compensation arrangement established or maintained by an employer or plan sponsor.
- (2) Notwithstanding Paragraph (1), the regulation shall apply to annuities used to fund a plan or arrangement that is funded solely by contributions an employee elects to make whether on a pre-tax or after-tax basis, and where the insurance company has been notified that plan participants may choose from among two (2) or more fixed annuity providers and there is a direct solicitation of an individual employee by a producer for the purchase of an annuity contract. As used in this subsection, direct solicitation shall not include any meeting held by a producer solely for the purpose of educating or enrolling employees in the plan or arrangement;
- D. Structured settlement annuities;
- E. [Charitable gift annuities; and]
- F. [Funding agreements].

Drafting Note: States that regulate charitable gift annuities should exempt them from the requirements of this regulation. States that recognize or regulate funding agreements as annuities should exempt them from the requirements of this regulation.

#### Section 4. Definitions

For the purposes of this regulation:

- A. ["Charitable gift annuity" means a transfer of cash or other property by a donor to a charitable organization in return for an annuity payable over one or two lives, under which the actuarial value of the annuity is less than the value of the cash or other property transferred and the difference in value constitutes a charitable deduction for federal tax purposes, but does not include a charitable remainder trust or a charitable lead trust or other similar arrangement where the charitable organization does not issue an annuity and incur a financial obligation to guarantee annuity payments.]
- B. "Contract owner" means the owner named in the annuity contract or certificate holder in the case of a group annuity contract.
- C. "Determinable elements" means elements that are derived from processes or methods that are guaranteed at issue and not subject to company discretion, but where the values or amounts cannot be determined until some point after issue. These elements include the premiums, credited interest rates (including any bonus), benefits, values, non-interest based credits, charges or elements of formulas used to determine any of these. These elements may be described as guaranteed but not determined at issue. An element is considered determinable if it was calculated from underlying determinable elements only, or from both determinable and guaranteed elements.
- D. ["Funding agreement" means an agreement for an insurer to accept and accumulate funds and to make one or more payments at future dates in amounts that are not based on mortality or morbidity contingencies.]
- E. "Generic name" means a short title descriptive of the annuity contract being applied for or illustrated such as "single premium deferred annuity."
- F. "Guaranteed elements" means the premiums, credited interest rates (including any bonus), benefits, values, non-interest based credits, charges or elements of formulas used to determine any of these, that are guaranteed and determined at issue. An element is considered guaranteed if all of the underlying elements that go into its calculation are guaranteed.
- G. "Non-guaranteed elements" means the premiums, credited interest rates (including any bonus), benefits, values, non-interest based credits, charges or elements of formulas used to determine any of these, that are subject to company discretion and are not guaranteed at issue. An element is considered non-guaranteed if any of the underlying non-guaranteed elements are used in its calculation.
- H. "Structured settlement annuity" means a "qualified funding asset" as defined in section 130(d) of the Internal Revenue Code or an annuity that would be a qualified funding asset under section 130(d) but for the fact that it is not owned by an assignee under a qualified assignment.

#### Section 5. Standards for the Disclosure Document and Buyer's Guide

- A. (1) Where the application for an annuity contract is taken in a face-to-face meeting, the applicant shall at or before the time of application be given both the disclosure document described in Subsection B and the Buyer's Guide contained in Appendix A.
- (2) Where the application for an annuity contract is taken by means other than in a face-to-face meeting, the applicant shall be sent both the disclosure document and the Buyer's Guide no later than five (5) business days after the completed application is received by the insurer.
  - (a) With respect to an application received as a result of a direct solicitation through the mail:
    - (i) Providing a Buyer's Guide in a mailing inviting prospective applicants to apply for an annuity contract shall be deemed to satisfy the requirement that the Buyer's Guide be provided no later than five (5) business days after receipt of the application.
    - (ii) Providing a disclosure document in a mailing inviting a prospective applicant to apply for an annuity contract shall be deemed to satisfy the requirement that the disclosure document be provided no later than five (5) business days after receipt of the application.
  - (b) With respect to an application received via the Internet:
    - (i) Taking reasonable steps to make the Buyer's Guide available for viewing and printing on the insurer's Web site shall be deemed to satisfy the requirement that the Buyer's Guide be provided no later than five (5) business day of receipt of the application.
    - (ii) Taking reasonable steps to make the disclosure document available for viewing and printing on the insurer's Web site shall be deemed to satisfy the requirement that the disclosure document be provided no later than five (5) business days after receipt of the application.



(c) A solicitation for an annuity contract provided in other than a face-to-face meeting shall include a statement that the proposed applicant may contact the insurance department of the state for a free annuity Buyer's Guide. In lieu of the foregoing statement, an insurer may include a statement that the prospective applicant may contact the insurer for a free annuity Buyer's Guide.

(3) Where the Buyer's Guide and disclosure document are not provided at or before the time of application, a free look period of no less than fifteen (15) days shall be provided for the applicant to return the annuity contract without penalty. This free look shall run concurrently with any other free look provided under state law or regulation.

B. At a minimum, the following information shall be included in the disclosure document required to be provided under this regulation:

(1) The generic name of the contract, the company product name, if different, and form number, and the fact that it is an annuity;

(2) The insurer's name and address;

(3) A description of the contract and its benefits, emphasizing its long-term nature, including examples where appropriate:

(a) The guaranteed, non-guaranteed and determinable elements of the contract, and their limitations, if any, and an explanation of how they operate;

(b) An explanation of the initial crediting rate, specifying any bonus or introductory portion, the duration of the rate and the fact that rates may change from time to time and are not guaranteed;

(c) Periodic income options both on a guaranteed and non-guaranteed basis;

(d) Any value reductions caused by withdrawals from or surrender of the contract;

(e) How values in the contract can be accessed;

(f) The death benefit, if available and how it will be calculated;

(g) A summary of the federal tax status of the contract and any penalties applicable on withdrawal of values from the contract; and

(h) Impact of any rider, such as a long-term care rider.

(4) Specific dollar amount or percentage charges and fees shall be listed with an explanation of how they apply.

(5) Information about the current guaranteed rate for new contracts that contains a clear notice that the rate is subject to change.

C. Insurers shall define terms used in the disclosure statement in language that facilitates the understanding by a typical person within the segment of the public to which the disclosure statement is directed.

#### Section 6. Report to Contract Owners

For annuities in the payout period with changes in non-guaranteed elements and for the accumulation period of a deferred annuity, the insurer shall provide each contract owner with a report, at least annually, on the status of the contract that contains at least the following information:

A. The beginning and end date of the current report period;

B. The accumulation and cash surrender value, if any, at the end of the previous report period and at the end of the current report period;

Drafting Note: States adopting this regulation with an effective date before July 1, 2000, should consider a delayed effective date for including the cash surrender value that is after June 30, 2000, because it appears programming changes may be required for many insurers.

C. The total amounts, if any, that have been credited, charged to the contract value or paid during the current report period; and

D. The amount of outstanding loans, if any, as of the end of the current report period.

## Section 7. 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 8. 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 9. Effective Date

This regulation shall become effective [insert effective date] and shall apply to contracts sold on or after the effective date.

## Appendix A Buyer's Guide

[The Buyer's Guide has already been adopted by the NAIC, and is currently an appendix to the Annuity and Deposit Fund Disclosure Model Regulation, which this model will replace. It is not reproduced here.]

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## ATTACHMENT THREE-B

### Life Insurance Illustrations Issues

1. Technical amendments to model
2. Fix model regarding laptop illustrations with no print-out
3. Reinsurance in cash flow testing
4. Illustrations still too complex?
5. Generally Recognized Expense Table (GRET)
6. Including an in-force illustration in the annual report (too long)
7. Conflicts with other models (disclosure, advertising, universal life, etc.)
8. Length of illustrations
9. Equity-indexed life insurance
10. Modifications for certain indeterminate premium policies (see attached letter)
11. Suggestion by American Academy of Actuaries to transfer some practice note material into the regulation
12. Add variable life

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## ATTACHMENT THREE-C

### Life Disclosure Working Group Conference Call October 20, 1998

The Life Disclosure Working Group of the Life Insurance and Annuities (A) Committee met by conference call at 1 p.m. on Oct. 20, 1998. Tom Foley (N.D.) chaired the meeting. The following working group members or their representatives participated: Harold Phillips for Sheldon Summers (Calif.); Roger Strauss (Iowa); Lester Dunlap (La.); Cindy Martin (Mass.); Paul DeAngelo (N.J.); and Ted Becker (Texas).

Roger Strauss (Iowa) suggested that the working group's comments be limited to the issue regarding delivery of the Annuity Buyer's Guide. Tom Foley (N.D.) said it was his impression that the working group members are in agreement on the rest of the Annuity Disclosure Model Regulation. He suggested that the buyer's guide issue be dealt with first, and then if there is additional time remaining on the call, any other issues can be discussed.

Mr. Foley said it appears that everyone is agreed that, in a face-to-face meeting, delivery of the buyer's guide will be at that time. Riva Kinslick (Prudential) said this is a concern among some companies, but most can live with that requirement. John Mathews (Allstate Life) referred the working group members to his written comments that note there are costs involved with this provision. The regulators affirmed that they had received Mr. Mathew's comment. Mr. Foley said that the difficulty comes in other than face-to-face meetings. Mr. Strauss said he looked favorably toward the written comment from William Geiger (Aegon) and suggested putting this in the regulation in place of Section 5A and B of the Sept. 15, 1998, draft. Mr. Geiger's suggestion does not include a number of days to be inserted as a requirement. The members of the working group agreed that five days is a reasonable requirement. Paul DeAngelo (N.J.) expressed concern that a five-day turnaround would mean that the individual got the contract, the buyer's guide and the disclosure document all at the same time. Peg VanDrise (American Express Financial) affirmed that would be true for her company. It would be much more expensive to send the documents separately. Mr. Foley asked Ms. VanDrise what free-look period her company used and Ms. VanDrise responded that it was 30 days. Mr. Strauss said he would be comfortable with a five-day turnaround and a 30-day free-look period. Ms. Kinslick opined that a 15-day free look is more than adequate. Because of the disintermediation problem, 30 days is too long. Harold Phillips (Calif.) said his state already requires a 30-day free-look period for senior citizens but the amount returned is the

current account value rather than the face value. Cindy Martin (Mass.) and Lester Dunlap (La.) also spoke in favor of the 30-day free-look period. Mr. Phillips asked what additional cost is involved in the extra days of the free-look period. Roger Wiard-Bauer (LifeUSA) said the company needs to sell assets that it has just invested, so this could result in a higher cost if interest rates have moved during this time period. The insurer would be investing for the long term, not the short term. He said the problem is that many people will choose to return the contract if there has been a dramatic change in the interest rates. The working group agreed to revise the draft as Mr. Strauss suggested and to include an option for either 15 or 30 days for the free-look period. Mr. Foley asked those who are concerned about the cost for this longer period to provide information on what those costs are and the working group will make a decision at the Winter National Meeting. Ms. Kinstlick agreed to provide that information to the working group. Ms. Kinstlick asked about the free-look period in a face-to-face sale. She asked if the industry could assume that no free-look period would be provided. Mr. Foley said it would be the current free look, which in most states is 10 days. Ms. VanDrisse suggested adding language that started the time running when a *completed* application was received so that two mailings are not necessary.

Mr. Dunlap said that he did not have a problem with the elimination of Section 5B, but he would like to see reference to the attempt to broadly distribute the buyer's guide someplace. Mr. DeAngelo said it is really the job of the regulator to disseminate the buyer's guide generally, and asked how the industry would feel about a proposal that solicitations be required to suggest that consumers contact the insurance department for a buyer's guide. He said the buyer's guide developed by this group is on the New Jersey Web site and this requirement would let people know that insurance regulators have the document available. The regulators agreed this was a good idea. Mr. Geiger asked if the suggestion from Mr. DeAngelo was meant to only apply to direct solicitation and Mr. DeAngelo responded that it should be available in any case except face-to-face where they are receiving the buyer's guide. Mr. Phillips said he objected violently to the comment in one of the letters that it was the responsibility of insurance regulators to educate the public. He opined that the industry has some responsibility too.

Ms. Kinstlick suggested that in Internet sales it would be redundant to suggest contacting the insurance department for a buyer's guide, when the Internet site had the buyer's guide available. Mr. Foley responded that it would still be useful because someone might not be able to print the buyer's guide and then would have the option of calling the insurance department. Walter Wells (Hartford) suggested that it is not always clear when the free-look period starts. He asked if this would be measured from the time the company mails the buyer's guide. Mr. Foley responded that it might instead be when the buyer's guide was received by the insured, but Mr. Wells asked how the company would know when the guide had been received.

Mr. Strauss suggested having another conference call to make sure there is agreement on all issues, so that the model can be adopted at the Winter National Meeting. Mr. Foley suggested that any regulators or interested parties with concerns should address those concerns in writing to Carolyn Johnson (NAIC/SSO) within 10 days after the revised draft is mailed by Ms. Johnson. Mr. Johnson agreed to mail the document by Oct. 28, and regulators and interested parties should have comments to Ms. Johnson by Nov. 13. If there is need for a conference call, one will be scheduled after Nov. 13.

Having no further business, the Life Disclosure Working Group adjourned at 2:10 p.m.

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#### ATTACHMENT FOUR

##### Equity Indexed Products Working Group Orlando, Florida December 7, 1998

The Equity Indexed Products Working Group of the Life Insurance and Annuities (A) Committee met in Salon IV of the Walt Disney World Dolphin Hotel in Orlando, Fla., at 3 p.m. on Dec. 7, 1998. Mike Batte (N.M.) chaired the meeting. The following working group members were present: Alfred Franz (Del.); Roger Strauss and Rosanne Mead (Iowa); Lester Dunlap (La.); Frank Cote (Mont.); Dan Keating (Okla.); and Leslie Jones (S.C.).

#### 1. Review 1998 Charges and Work Plan

Mike Batte (N.M.) said this group was organized in March and developed a work plan for its projects. The group gathered information from states on contract filing guidelines and distributed those at the 1998 Summer National Meeting. The group reviewed market conduct treatment for equity-indexed products in the *Market Conduct Examiners Handbook* and decided that the handbook is broad enough to cover issues related to equity-indexed products. The working group heard a presentation on agents' training for variable products and gathered samples of training materials from insurers. The working group also discussed guaranty fund issues and referred that question to the Guaranty Fund Issues (EX5) Working Group.

Frank Cote (Mont.) said the working group needs to discuss agents training more extensively and opined that the working group's charge will then be completed.

#### 2. Consider Recommendation on Agents Education

Mr. Cote asked the working group to recollect its discussion at the last meeting and said that the working group had encouraged agents groups and others to comment at the Winter National Meeting. Lester Dunlap (La.) said he would like to hear more from companies about who sells the product and what training they receive. Reese Boyd (American Council of Life Insurance—ACLI) said he provided samples with specific information including sample videos, software, etc., that companies use when training agents. He said he thought that answered questions from the working group. Mr. Cote said it seems to him

the working group is leaning in the direction of requiring companies to train their agents and to demonstrate that as part of the contract approval process. He asked if the industry is comfortable with that approach. Mr. Boyd responded that states are already looking at training as part of the filing process and none of the companies have expressed concern to him.

Mr. Cote moved that the working group suggest to its parent that companies should be required to demonstrate that they train their agents as part of the contract filing process. Leslie Jones (S.C.) seconded the motion for discussion purposes. Roger Strauss (Iowa) asked if the working group will come up with a model or a white paper on this issue. Mr. Batte responded that it is the working group's responsibility to decide if more work needs to be done and make recommendations. He said the working group has already accumulated information about what other states are doing. Dan Keating (Okla.) said he thought it would be helpful to provide more specific information on what states should look at. He opined that it does not serve our purpose to just say "look at agents' training." He suggested looking at state filing requirements and asking which of these are most valuable and compiling those in a recommendation in the parent committee. The motion made by Mr. Cote passed.

Mr. Keating opined that the charge to the working group is vague and he asked what it means to "consider issues." He noted that one of the parts of the filing requirements normally reviewed is nonforfeiture. Mr. Batte responded that this working group does not want to duplicate other groups' work. This issue is being addressed by the Life and Health Actuarial (Technical) Task Force. This group's responsibility is to make sure all of the issues are being addressed and to consider those issues not being addressed elsewhere. Don Pearsall (N.Y.) said that, as a result of a new derivatives law passed in New York recently, companies will now be able to sell equity-indexed products. He said he would appreciate more specific direction from the working group.

### 3. Report on Guaranty Fund Issues

Rob Sweeney (ACLI) reported that he and Mr. Boyd made a proposal to the Guaranty Fund Issues (EX5) Working Group to suggest changes to the Life and Health Insurance Guaranty Association Model Act to cover equity-indexed products in what the ACLI considers to be an appropriate fashion. That working group is now discussing the proposal. He offered to provide further information to the working group so it also could consider these issues. Mr. Batte said this issue is being considered in the appropriate working group, and there is no need to duplicate that effort here.

### 4. Consider Need for 1999 Charges

Ms. Jones said she thought it would be an appropriate charge to develop contract filing guidelines, even if it just a compilation of what other states have already. She said that South Carolina uses the American Academy of Actuaries (AAA) report on equity-indexed products, which contains a section on filing guidelines. She said she would like to see the working group develop something along that line. Mr. Keating opined that if the working group does a list of recommendations, the AAA report is the place to start. He said he certainly is not recommending drafting a model or something else more formal. He hoped for a short list that would identify issues and make recommendations to the states. Mr. Keating moved that the working group ask for a charge to develop a work product consisting of a list of items states should consider in reviewing contract filings and agents training. Ms. Jones seconded the motion and it passed.

Having no further business, the Equity Indexed Products Working Group adjourned at 4 p.m.

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## ATTACHMENT FIVE

Suitability Working Group  
Orlando, Florida  
December 8, 1998

The Suitability Working Group of the Life Insurance and Annuities (A) Committee met in Salon IV of the Walt Disney World Dolphin Hotel in Orlando, Fla., at 2 p.m. on Dec. 8, 1998. Paul DeAngelo (N.J.) chaired the meeting. The following working group members were present: Lester Dunlap (La.); Cindy Martin (Mass.); Robert Commodore (Minn.); Stephen Stark (Mo.); Louis Belo (N.C.); Joel Ario (Ore.); and Mary Keller (Texas).

### 1. Consider Life Insurance Advertising Model Regulation

Paul DeAngelo (N.J.) said that comments on the regulation have been received from Texas to add to the earlier comments from Massachusetts and Louisiana. He encouraged other states that have comments on specific provisions of the regulation to provide those to Carolyn Johnson (NAIC/SSO) by Jan. 15, 1999. He said a conference call will be scheduled on Jan. 27, 1999, to discuss the Life Insurance Advertising Model Regulation.

### 2. Suitability Issues

Mr. DeAngelo referred to a memorandum he asked Ms. Johnson to prepare outlining suitability provisions in existing NAIC models (Attachment Five-A). Ms. Johnson reported that only two NAIC models contain suitability requirements for the insurer and several models have a duty to provide information that might be helpful so that an individual could determine suitability for himself. Mr. DeAngelo commented that the brevity of the list may help the working group determine whether it should prepare a model regulation on suitability of purchase of life insurance and annuities.

Mr. DeAngelo referred the working group members to a memorandum prepared by Ms. Johnson for the Annuities (A) Working Group in the spring of 1997. He said that the Annuities Working Group surveyed states asking their opinion about suitability requirements for annuity purchasers. He pointed out that three states had standards in place and one more intended to adopt a law or regulation. He also thought it was interesting that 19 states that responded to the survey thought the NAIC should develop a model regulation with suitability requirements. He suggested following up on that memo to see what those states thought were important provisions to include in a model.

George Coleman (Prudential) pointed out that the NAIC has nearly finished work on an Annuity Disclosure Model Regulation that may help people make an intelligent decision about suitability of purchase, so that standards may not need to be developed by this working group. Mr. DeAngelo said in his mind there is a distinction between putting the onus on the buyer to decide for himself whether a purchase is suitable and putting the onus on the company to determine suitability. Joel Ario (Ore.) suggested it would also be helpful to get information from the states that have suitability standards. They should be asked whether these standards help in market conduct examinations and complaint handling. Mr. DeAngelo asked for suggestions for appropriate questions to ask states on a survey. He asked those with input to submit it to Ms. Johnson by Jan. 29, 1999. A survey will then be prepared and reviewed by the working group in a conference call. Mr. Commodore said that even though many states do not have standards in their laws or regulations, a number of them attempt to deal with these issues on a case-by-case basis. He suggested asking states to describe cases they have seen and the resolution. This might help point the working group in the direction it needs to go.

Mr. DeAngelo said he offered at the interim conference call to draft an outline for a suitability white paper. He said the group might need to ask for a modification to its charge to prepare this paper. Mr. Ario suggested a change to the white paper outline and Mr. DeAngelo agreed to include that in the outline (Attachment Five-B). Cindy Martin (Mass.) asked about the timetable for the white paper. Mr. DeAngelo responded he did not think it was realistic to expect a first draft before June.

### 3. Adopt Minutes of Nov. 12, 1998, Conference Call

Robert Commodore (Minn.) moved and Stephen Stark (Mo.) seconded a motion to adopt the minutes of the Nov. 12, 1998, conference call (Attachment Five-C). The motion passed.

### 4. Presentation from Edward Jones

Laura Ellenhorn and Richard Link (Edward Jones) presented information to the working group about the suitability practices used by their firm. Ms. Ellenhorn said that Edward Jones sells securities and insurance. They are required to follow rules from the National Association of Securities Dealers and from the New York Stock Exchange. Both of these have suitability requirements. Mr. Link said the organization considers several suitability factors: the investment objectives of the client, need for diversification in relation to other investments, the age of the individual, and the need for liquidity. He said suitability for life insurance is measured by the following standards: whether the amount of the insurance purchased matches the individual's needs, whether the premium payments match his or her income, how long insurance will be needed, and the risk tolerance of the individual. Members of the working group expressed appreciation to Ms. Ellenhorn and Mr. Link for their presentation, which was very informative.

Having no further business, the Suitability Working Group adjourned at 3 p.m.

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## ATTACHMENT FIVE-A

To: Suitability Working Group  
 From: Carolyn J. Johnson, CLU, Senior Counsel (NAIC)  
 Date: December 1, 1998  
 Re: Suitability Provision in NAIC Models

A number of NAIC models contain suitability provisions. They can be divided into two types: those that impose a duty on the agent or insurer to determine suitability, and those that require the agent or insurer to provide information to make it easier for the applicant to determine for himself whether a purchase is suitable.

### DUTY TO DETERMINE SUITABILITY OF PURCHASE

1. Long-Term Care Insurance Model Regulation (#641). Insurers must develop standards for suitability of purchase and train their agents in use of the standards. It is the responsibility of the agent and the insurer to measure whether a purchase is suitable. The Appendices include a worksheet for the consumer to use in determining if the purchase is suitable, helpful information and a sample letter for the insurer to use when it appears a purchase is unsuitable.

2. Model Regulation to Implement the Medicare Supplement Insurance Model Act (#651). The agent should make reasonable efforts to determine if a purchase is suitable.

### DUTY TO PROVIDE INFORMATION

1. Annuity Buyer's Guide (adopted Dec. 7, 1998). The guide has information to help an individual decide if an annuity is right for him.

2. Credit Insurance Model Act (#360). Section 6A includes a requirement to disclose to the consumer that, if he has other insurance, he may not need or want credit insurance.
3. Life Insurance Disclosure Model Regulation (#580). The Guide to Buying Life Insurance After Age 60 makes the agent or company responsible for providing information to help the buyer determine if his policy will cost more than his beneficiary will receive in death benefits. Another appendix to the regulation includes the Life Insurance Buyer's Guide, with information to help a consumer determine if this is a suitable purchase.
4. Life Insurance Illustrations Model Regulation (#582). A readable illustration will help a consumer determine if the policy he is considering will help meet his goals.
5. Replacement of Life Insurance and Annuities Model Regulation (#613). The notice of replacement cautions the purchaser to consider whether replacement of his current policy is suitable. The notice lists some reasons why replacement may not be suitable.

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## ATTACHMENT FIVE-B

## Proposed Outline for Suitability Working Group White Paper

1. Introduction
2. Survey Results
3. State Suitability Statutes and Standards
4. NASD/SEC Suitability Standards
5. NASD Enforcement Procedures
6. Applicable Caselaw
7. Voluntary Suitability Standards
  - A. Insurance Marketplace Standards Association (IMSA)
  - B. Other
8. Industry Viewpoint
9. Conclusions and Recommendations
  - A. Life Products
  - B. Annuity Contracts

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## ATTACHMENT FIVE-C

Suitability Working Group  
Conference Call  
November 12, 1998

The Suitability Working Group of the Life Insurance and Annuities (A) Committee met by conference call, at 1 p.m. on Nov. 12, 1998. Paul DeAngelo (N.J.) chaired the meeting. The following working group members or their representatives participated: Erin Klug (Ariz.); Rosanne Mead (Iowa); Lester Dunlap (La.); Cindy Martin (Mass.); Robert Commodore (Minn.); Phil Bisesi and Kip May (Ohio); Joel Ario (Ore.); Mary Keller and Bill Goodman (Texas); and Tom Van Cooper (Vt.).

Paul DeAngelo (N.J.) stated that the charge of the working group is to look at issues regarding suitability of purchase of life insurance and annuities and also to recommend whether any changes need to be made to the Life Insurance Advertising Model Regulation.

1. Suitability

Mr. DeAngelo thanked Rosanne Mead (Iowa) for her review of case law on suitability standards in the sale of securities and insurance products. He also thanked Joel Ario (Ore.) for his review of existing state suitability statutes for insurance products. Mr. DeAngelo responded that he had also provided some materials to the working group on the current suitability standards of the National Association of Securities Dealers (NASD). He said these three sets of materials provide background material that should be helpful to the working group. He suggested that the working group needs this background information to draft a white paper and needs a white paper before the group can decide whether it is useful to draft a model act or regulation. Mr. Ario agreed with that approach and also pointed out that it would be helpful for the working group to get more written information from companies about their own standards for self-policing suitability of purchases. He also pointed out that the Insurance Marketplace Standards Association (IMSA) might have some useful information. Mr. DeAngelo responded that Edward Jones will make a presentation at the Winter National Meeting and IMSA and the NASD have both agreed to make presentations at the NAIC Spring National Meeting in Washington, D.C. He speculated that the working group would then be in a position to release a white paper draft by the 1999 Summer National Meeting. Mr. Ario suggested that companies become involved in the IMSA presentation. He said the IMSA standards require companies to have provisions in place, and it would be helpful to hear from companies about their standards.

Tom Van Cooper (Vt.) said that he found a review of Ms. Mead's paper very interesting but he was not clear about how the standards used in a court varied from the suitability standards that an insurance department might use for enforcement actions. Mr. DeAngelo agreed that this is an important issue. Mr. Ario noted that he is following up with the five states that have the most relevant standards for suitability (Iowa, Kansas, Minnesota, Vermont and Wisconsin) and will report at the Winter National Meeting as to how the suitability standards in these five states work in practice. Mr. DeAngelo said he would come to the Winter National Meeting with the beginnings of an outline for the white paper. Mary Keller (Texas) suggested that it would also be useful to identify the magnitude of the problem that a state faces when it has no standards for suitability. She said Texas has had a number of lawsuits and the state had to look for other methods of dealing with these issues because Texas has no suitability standard. She suggested doing a survey to get state experience. Mr. DeAngelo asked that any states with litigation in this area send a copy to Carolyn Johnson (NAIC/SSO) so that examples can be incorporated in the white paper. Mr. Ario said he recognized that states fill out a lot of surveys but he opined that a survey on these problems would be useful. Mr. DeAngelo recalled that the Annuities Working Group had done a similar survey on issues related to suitability for annuity sales to seniors and he asked Ms. Johnson to bring that material to the Winter National Meeting.

## 2. Review of the Life Insurance Advertising Model Regulation

Mr. DeAngelo thanked Cindy Martin (Mass.) for her submission to the working group. Massachusetts went through the entire Life Insurance Advertising Model Regulation and highlighted the discussion items that will be reviewed at the Winter National Meeting. In addition, Mr. DeAngelo noted that he made specific assignments to states for input on sections of that model. He thanked Lester Dunlap (La.) for his submission and asked the other states with specific assignments to have that material to Ms. Johnson before the Winter National Meeting so that it is available for discussion in Orlando. Mr. DeAngelo asked Ms. Johnson if the NAIC staff would provide input about suitability standards in existing NAIC models.

Marybeth Stevens (American Council of Life Insurance—ACLI) asked why this working group was considering changes to the advertising regulation. Mr. DeAngelo responded that it has been a long time since this model was updated, and some states have added provisions to their own regulations that would be helpful additions to the NAIC model. In addition there are many new products that did not exist when the model was last updated, life illustration standards have been developed, and direct marketing is a more common method of solicitation. All of these contribute to a need to update the Life Insurance Advertising Model Regulation.

Having no further business, the Suitability Working Group adjourned at 1:35 p.m.

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## ATTACHMENT SIX

Synthetic GIC Working Group  
Orlando, Florida  
December 6, 1998

The Synthetic GIC Working Group of the Life Insurance and Annuities (A) Committee met in Salon V of the Walt Disney World Dolphin Hotel in Orlando, Fla., at 1 p.m. on Dec. 6, 1998. Larry Gorski (Ill.) chaired the meeting. The following working group members or their representatives were present: Sheldon Summers representing Woody Girion (Calif.); Jack Gies (Conn.); and Paul DeAngelo representing Neil Vance (N.J.).

The sole topic of the meeting was to finalize changes to the Dec. 2, 1998, draft of the Synthetic Guaranteed Investment Contracts Model Regulation. During the discussions on that draft, the following changes were agreed to:

1. Add definitions of "appointed actuary" and "valuation actuary" consistent with the definitions included in the Separate Accounts Funding Guaranteed Minimum Benefits Under Group Contracts Model Regulation.
2. Modify the definition of "qualified actuary" to be consistent with the definition found in the separate accounts model.
3. Change all references in the draft to "valuation actuary" from either "qualified actuary" or "appointed actuary," as appropriate.
4. Change the reference in Section 3 to "Section 4W."
5. Change "request" to "requests" in Section 5B(2).
6. Insert the word "the" in front of the word "difference" in Section 6B(2)(c).
7. Remove the word "percentage" prior to the word "deduction" in Section 10A(4).
8. Change the word "adequate" to "appropriate" in Section 10B(5)(b) and eliminate the phrase "including the cost of capital" at the end of that Subsection.
9. Replace the wording of Section 10B(4)(b) with the following: "an opinion paragraph expressing the valuation actuary's opinion with respect to the matters described in Subparagraphs 5A and 5B below."

10. In Section 10A(2)(a) replace the phrase "one year" with "one-half year."

With those changes Jack Gies (Conn.) moved and Sheldon Summers (Calif.) seconded a motion to adopt the model. The motion passed without objection. Attachment Six-A is a copy of the adopted model.

Doug Barnert (Barnert and Associates) submitted a statement for attachment to these minutes; his statement is included as Attachment Six-B.

Larry Gorski (Ill.) stated that the charge of the working group had been fulfilled and that a request would be forwarded to the Life Insurance and Annuities (A) Committee to disband the working group. Finally, Mr. Summers moved and Mr. Gies seconded a motion to adopt the Nov. 10, 1998, minutes of the joint conference call with the Separate Accounts Working Group. (Those minutes are attached to the report of the Separate Accounts Working Group to the Accounting Practices and Procedures (EX4) Task Force.) The motion passed without objection.

Having no further business, the Synthetic GIC Working Group adjourned at 2:30 p.m.

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## ATTACHMENT SIX-A

### Synthetic Guaranteed Investment Contracts Model Regulation Draft: December 9, 1998 Adopted by the Life Insurance and Annuities (A) Committee

#### Table of Contents

Section 1.	Authority
Section 2.	Purpose
Section 3.	Scope and Application
Section 4.	Definitions
Section 5.	Financial Requirements and Plan of Operation
Section 6.	Required Contract Provisions and Filing Requirements
Section 7.	Investment Management of the Segregated Portfolio
Section 8.	Purchase of Annuities
Section 9.	Unilateral Contract Terminations
Section 10.	Reserves
Section 11.	Severability
Section 12.	Effective Date

#### Section 1. Authority

This rule is issued pursuant to the authority vested in the commissioner of the State of [insert state] under [insert citation for authority].

#### Section 2. Purpose

##### A. The purpose of this regulation is to prescribe:

- (1) The terms and conditions under which life insurance companies may issue group annuity contracts and other agreements that in whole or in part establish the insurer's obligation by reference to a segregated portfolio of assets that is not owned by the insurer;
- (2) The essential operational features of the segregated portfolio of assets; and
- (3) The reserve requirements for these group annuity contracts and agreements.

B. This regulation is intended to aid in the timely approval of such products by the commissioner, and recognizes that timely approval is essential given the competitive nature of the market for these products.

#### Section 3. Scope and Application

This regulation applies to that portion of a group annuity contract or other agreement described in Section 4W and issued by a life insurer that functions as an accounting record for an accumulation fund and has benefit guarantees relating to a principal amount and levels of interest at a fixed rate of return specified in advance. The fixed rates of return will be constant over the applicable rate periods, and may reflect prior and current market conditions with respect to the segregated portfolio but may not reference future changes in market conditions. It applies to all contracts issued after the effective date of this regulation. Contracts that have been negotiated prior to the effective date need not be refiled with the commissioner.

Drafting Note: This explanation of the fixed rate of return is intended to clarify the fact that the regulation excludes products such as those that guarantee the future performance of a stated index. It is recognized that versions of synthetics other than



those described in the scope section may evolve over time; the intent of the regulation is not to preclude the issuance of such products, but rather to describe how a specific set of synthetics (those described in the scope) should be regulated.

**Drafting Note:** It is expected that individual regulators, where applicable, will retain the right to withdraw approval of previously filed contract forms for new issuance if they do not conform to the regulation. Therefore, no language explicitly withdrawing approval of previously filed forms was included.

#### Section 4. Definitions

As used in this regulation, the following terms shall have these meanings:

- A. "Account assets" means the assets in the segregated portfolio plus any assets held in the general account or a separate account to meet the asset maintenance requirements.
- B. "Actuarial opinion and memorandum" means the opinion and memorandum of the valuation actuary required to be submitted to the commissioner pursuant to Section 10B of this regulation.
- C. "Affirmatively approved" means approval of an insurer's plan of operation for a class of contracts containing the form of contract under review, after the plan of operation associated with the class of contracts has been reviewed by the insurer's domiciliary insurance department, and the plan of operation has been found to be in compliance with the NAIC Synthetic Guaranteed Investment Contracts Model Regulation by the domiciliary insurance department. Affirmatively approved does not mean approval as a result of the deemer provision.
- D. "Appointed actuary" means the qualified actuary appointed or retained either directly by or by the authority of the board of directors through an executive officer of the company to prepare the annual statement of actuarial opinion for the company as a whole pursuant to Section [insert reference to standard valuation law].
- E. "Asset maintenance requirement" means the requirement to maintain assets to fund contract benefits in accordance with Section 10 of this regulation.
- F. "Class of contracts" means the set of all contracts to which a given plan of operation pertains.
- G. "Contract value record" means an accounting record, provided by the contract in relation to a segregated portfolio of assets, that is credited with a fixed rate of return over regular periods, and that is used to measure the extent of the insurer's obligation to the contractholder. The fixed rate of return credited to the contract value record is determined by means of a crediting rate formula or declared at the inception of the contract and valid for the entire term of the contract.
- H. "Crediting rate formula" means a mathematical formula used to calculate the fixed rate of return credited to the contract value record during any rate period and based in part upon the difference between the contract value record and the market value record amortized over an appropriate period. The fixed rate of return calculated by means of this formula may reflect prior and current market conditions with respect to the segregated portfolio, but may not reference future changes in market conditions.
- I. "Date of filing," with respect to a filing for approval of a contract form under this regulation, means the date as defined by the applicable statutes or regulations of the state of issue with regard to contract filings.

**Drafting Note:** Individual states may wish to insert a specific reference to the applicable statute or regulation.

- J. "Duration" means, with respect to the segregated portfolio assets or guaranteed contract liabilities, a measure of price sensitivity to changes in interest rates, such as the Macaulay duration or option-adjusted duration.
- K. "Fair market value" means a reasonable estimate of the amount that a knowledgeable buyer of an asset would be willing to pay, and a knowledgeable seller of an asset would be willing to accept, for the asset without duress in an arm's length transaction. In the case of a publicly traded security, the fair market value is the price at which the security is traded or, if no price is available, a price that appropriately reflects the latest bid and asked prices for the security. In the case of a debt instrument that is not publicly traded, the fair market value is the discounted present value of the asset calculated at a reasonable discount rate. For all other non-publicly traded assets, fair market value will be determined in accordance with valuation practices customarily used within the financial industry.
- L. "Guaranteed minimum benefits" means contract benefits on a specified date that may be either:
  - (1) A principal guarantee, with or without a fixed minimum interest rate guarantee, related to the segregated portfolio;
  - (2) An assurance as to the future investment return or performance of the segregated portfolio; or
  - (3) The fair market value of the segregated portfolio, to the extent that the fair market value of the assets determines the contractholder's benefits.
- M. (1) "Hedging instrument" means:

(a) An interest rate futures agreement or foreign currency futures agreement, an option to purchase or sell an interest rate futures agreement or foreign currency futures agreement, or any option to purchase or sell a security or foreign currency, used in a bona fide hedging transaction; or

(b) A financial agreement or arrangement entered into with a broker, dealer or bank, qualified under applicable federal and state securities or banking law and regulation, in connection with investment in one or more securities in order to reduce the risk of changes in market valuation or to create a synthetic investment that, when added to the portfolio, reduces the risk of changes in market valuation.

(2) An instrument shall not be considered a hedging instrument or a part of a bona fide hedging transaction if it is purchased in conjunction with another instrument where the effect of the combined transaction is an increase in the portfolio's exposure to market risk.

N. "Investment guidelines" means a set of written guidelines, established in advance by the person with investment authority over the segregated portfolio, to be followed by the investment manager. The guidelines shall include a description of:

- (1) The segregated portfolio's investment objectives and limitations;
- (2) The investment manager's degree of discretion;
- (3) The duration, asset class, quality, diversification, and other requirements of the segregated portfolio; and
- (4) The manner in which derivative instruments may be used, if at all, in the segregated portfolio.

O. "Investment manager" means the person (including the contractholder) responsible for managing the assets in the segregated portfolio in accordance with the investment guidelines in a fiduciary capacity to the owner of the assets.

P. "Market value record" means an accounting record provided by the contract to reflect the fair market value of the segregated portfolio.

Q. "Permitted custodial institution" means a bank, trust company or other licensed fiduciary services provider.

Drafting Note: When adopting this regulation, individual regulators may wish to review their applicable state laws to ensure that this definition hasn't inadvertently authorized an entity to act as a custodial institution that it would not wish to do so.

R. "Plan of operation" means a written plan meeting the requirements of Section 5B(1) of this regulation.

S. "Qualified actuary" means an individual who meets the qualification standards set forth in [insert reference to section of the regulations related to actuarial opinions and memoranda].

T. "Rate period" means the period of time during which the fixed rate of return credited to the contract value record is applicable between crediting rate formula adjustments.

U. "Segregated portfolio" means:

- (1) A portfolio or sub-portfolio of assets to which the contract pertains that is held in a custody or trust account by the permitted custodial institution and identified on the records of the permitted custodial institution as special custody assets held for the exclusive benefit of the retirement plans or other entities on whose behalf the contractholder holds the contract; and
- (2) Any related cash or currency received by the permitted custodial institution for the account of the contractholder and held in a deposit account for the exclusive benefit of the retirement plans or other entities on whose behalf the contractholder holds the contract.

V. "Spot rate" corresponding to a given time of benefit payment means the yield on a zero-coupon non-callable and non-prepayable United States government obligation maturing at that time, or the zero-coupon yield implied by the price of a representative sampling of coupon-bearing, non-callable and non-prepayable United States government obligations in accordance with a formula set forth in the plan of operation. To the extent that guaranteed contract liabilities are denominated in the currency of a foreign country rated in one of the two (2) highest rating categories by an independent nationally recognized United States rating agency acceptable to the commissioner and are supported by investments denominated in the currency of the foreign country, the spot rate may be determined by reference to substantially similar obligations of the government of the foreign country. For liabilities other than those described above, the spot rate shall be determined on a basis mutually agreed upon by the insurer and the commissioner.

W. "Synthetic guaranteed investment contract" or "contract" means a group annuity contract or other agreement that in whole or in part establishes the insurer's obligations by reference to a segregated portfolio of assets that is not owned by the insurer.

X. "Unilateral contract termination event" means an event allowing the insurer to unilaterally and immediately terminate the contract, without future liability or obligation to the contractholder.

Y. "United States government obligation" means a direct obligation issued, assumed, guaranteed or insured by the United States of America or by an agency or instrumentality of the United States government.

Z. "Valuation actuary" means the appointed actuary or, alternatively, a qualified actuary designated by the appointed actuary to render the actuarial opinion pursuant to Section 10. Written documentation of any such designation shall be on file at the company and available for review by the commissioner upon request.

#### Section 5. Financial Requirements and Plan of Operation

A contract may not be delivered or issued for delivery in this state unless the issuing insurer is licensed as a life insurance company in this state and is financially qualified under the provisions of Subsection A of this section. In addition, a domestic insurer may not deliver or issue for delivery, either in this state or outside this state, a contract belonging to a specific class of contracts unless the insurer has satisfied the requirements of Subsection B of this section with respect to that class.

A. An insurer will be financially qualified under this section if its most recent statutory financial statements reflect at least \$1 billion in admitted assets or \$100 million in capital and surplus, and its risk-based capital results do not place it at a regulatory level of action. In lieu of the requirements in the preceding sentence, the insurer may be required to satisfy such other financial qualification requirements set forth by the commissioner as having been deemed necessary or appropriate in a particular case to protect the insurer's policyholders and the public.

B. A domestic insurer will satisfy the requirements of this section with respect to a class of contracts if the insurer has filed a plan of operation pertaining to the class of contracts, together with copies of the forms of contract in the class, with the commissioner and the filing of the plan of operation has been approved or has not been disapproved within the sixty-day period following the date of filing, in which event the plan of operation shall be deemed approved.

(1) The plan of operation for a class of contracts shall describe the financial implications for the insurer of the issuance of contracts in the class, and shall include at least the following:

(a) A statement that the plan of operation will be administered in accordance with the requirements prescribed by the commissioner pursuant to this regulation, along with a statement that the insurer will comply with the plan of operation in its administration of the contract;

(b) A statement describing the methods and procedures used to value statutory liabilities for purposes of Section 10;

(c) A description of the criteria used by the insurer in approving the investment manager for the segregated portfolio of assets associated with a contract in the class, if the investment manager is an entity other than the insurer or its wholly owned subsidiary;

(d) A description of the insurer's requirement for reports concerning the assets in each segregated portfolio and transactions involving the assets, and a description of how the insurer can use the information in a report to determine that the segregated portfolio is being managed in accordance with its investment guidelines. The insurer shall require that the report be prepared no less frequently than quarterly, and include a complete statement of segregated portfolio holdings and their fair market value;

(e) A demonstration of financial results for one or more sample contracts from the class of contracts, showing at a minimum the projected contract value records, the applicable fixed rate or rates of return, and the projected market value records, describing how the investments in the segregated portfolio reflect provision for benefits insured by the contract and how the contract value and market values and the rates of return may be affected by changes in the investment returns of the segregated portfolio and reasonably anticipated deposits to and withdrawals from the segregated portfolio by the contractholder, as well as any advances made by the insurer to the contractholder. The sample contracts shall be chosen to reasonably represent the range of results that could be expected from possible combinations of contract provisions of all contracts within the class. The demonstration shall include at least three (3) hypothetical return scenarios (level, increasing and decreasing) and for each of these scenarios, at least three (3) withdrawal scenarios (zero, moderate and high) shall be modeled. The commissioner may require additional scenarios if deemed necessary to fully understand the risks under the class of contracts. The demonstration period shall be the greater of five (5) years or the minimum period the insurer must underwrite the risk;

(f) A statement that all contracts in the class of contract satisfy the requirement of Section 9 regarding unilateral contract terminations, together with a description of all termination events, discontinuation triggers and options, notice requirements, corrective action procedures, all other contract safeguards, and the procedures to be followed when a unilateral contract termination event occurs;

(g) A description of the allowable investment parameters (such as objectives, asset classes, quality, duration and diversification requirements applied to the assets held within the segregated portfolio) to be reflected in the investment guidelines applicable to each contract issued in the class to which the submitted plan of operation

applies; and a description of the procedures that will be followed by the insurer in evaluating the appropriateness of any specific investment guidelines submitted by the contractholder. If the insurer chooses to operate a contract in accordance with investment guidelines not meeting the criteria established pursuant to this subparagraph, the non-conforming set of investment guidelines shall be filed with the commissioner in accordance with the filing requirements of this subsection;

(h) An unqualified opinion by a qualified actuary with expertise in these matters as to the adequacy of the consideration charged by the insurer for the risks it has assumed with respect to the contracts in the class to which the plan of operation applies;

(i) A statement that the actuarial opinion and memorandum required by Section 10 shall include, with respect to the class of contracts to which the plan of operation applies:

(i) If a payment has been made by the insurer in the prior reporting period under a contract in the class, the amount of aggregate risk charges (net of administrative expenses) for contracts in the class, and the aggregate amount of any losses incurred; and

(ii) An inventory of all material unilateral contract termination events in the class that have not been cured within the time period specified and that have occurred during the prior reporting period but where the company decided not to terminate the contract.

(2) Review of the plan of operation by the commissioner may necessitate requests for information to supplement that furnished pursuant to Paragraph (1). Replies made in compliance with this paragraph should be made in sufficient detail that any follow-up correspondence can be held to a minimum.

#### Section 6. Required Contract Provisions and Filing Requirements

**Drafting Note:** This section may be omitted in its entirety if a state does not require contracts to be filed for approval, and the state wishes to eliminate required contract provisions. Subsection B of this section may be omitted if a state does not require contracts to be filed for approval, but wishes to maintain required contract provisions.

A contract may not be delivered or issued for delivery in this state unless the contract satisfies the requirements of Subsection A of this section and the issuing insurer has satisfied the requirements of Subsection B of this section with respect to the contract.

##### A. The contract shall:

(1) Provide that the assets to which the contract pertains and for which a contract value record is established will be maintained in a segregated portfolio of a permitted custodial institution;

(2) Grant the insurer the right to perform audits and inspections of assets held in the segregated portfolio from time to time upon reasonable notice to the permitted custodial institution;

(3) Provide that the insurer will receive prior notice of and the right to approve any appointment or change of investment managers;

(4) Give a description of how the contract value record will be determined, and, where applicable, adjusted by a crediting rate formula;

(5) State the maximum rate period between crediting rate formula recalculations that will be permitted, if any;

(6) Provide the insurer with the right to refuse to recognize any new deposits to the segregated portfolio unless there is a written agreement between the insurer and the contractholder as to the permissible levels and timing of new deposits;

(7) Clearly identify all circumstances under which insurer payments or advances to the contractholder are to be made;

(8) Clearly identify the types of withdrawals made on a market value basis;

(9) Provide either a fixed maturity schedule or a settlement option permitting the contractholder to receive the contract value record over time, provided that no unilateral contract termination event has occurred; and

(10) Include a provision stating, or substantially similar to, the following:

"No waiver of remedies by the insurer that is a party to this agreement, following the breach of any contractual provision of the agreement or of the investment guidelines applicable to it, or failure to enforce the provisions or guidelines, which constitutes grounds for termination of this agreement for cause by the insurer, and is not cured within thirty (30) days following the insurer's discovery of it,

shall be effective against an insurance commissioner in any future rehabilitation or insolvency proceedings against the insurer unless approved in advance in writing by the commissioner."

Drafting Note: An adopting state may wish to add an "entire contract" provision in this section if such a provision is not required elsewhere in the adopting state's insurance code.

B. An insurer will satisfy the filing and approval requirements of this section with respect to a contract if the insurer has filed the form of the contract with the commissioner and it is accompanied by the items specified in Paragraphs (1), (2), and (3) of this subsection, and the form has been approved or has not been disapproved within the thirty-day period following the date of filing, in which event the form of contract shall be deemed approved. Notwithstanding the foregoing, the requirement for filing and approval of the form of contract may be waived at the discretion of the commissioner.

(1) The form of contract filed for approval shall be accompanied by a statement that the contract meets the conditions of Subsection A of this section.

(2) The form of contract filed for approval shall be accompanied by a statement:

(a) Specifying the range of variation of variable contract provisions, if any, that could have a material effect on the risk assumed by the insurer under the contract, including withdrawal methodology, crediting rate formula and termination events;

Drafting Note: Contract forms covered by this regulation frequently incorporate variable provisions. The statement required by this subparagraph is intended to provide the information regulators need to evaluate the risks associated with such variability.

(b) Describing how the fair market value will be determined, including a description of the rules for valuing securities and other assets that are not publicly traded;

(c) Describing the crediting rate formula, if any, and how it will operate to take into account the difference between the market value record and the contract value record over time; and

(d) Listing events that give the insurer the right to terminate the contract immediately.

(3) (a) In the case that the plan of operation pertaining to the class of contracts to which the contract belongs has been affirmatively approved by the commissioner of the state in which the issuing insurer is domiciled, the form of contract filed for approval shall be accompanied by a statement indicating the receipt of approval, and that the approval was an affirmative approval.

(b) In the case that the plan of operation pertaining to the class of contracts to which the contract belongs has been deemed approved in the state in which the issuing insurer is domiciled, the form of contract filed for approval shall be accompanied by a statement indicating that the issuing insurer has met the requirements for deemed approval.

(c) In the case that the plan of operation pertaining to the class of contracts to which the contract belongs has not been approved, either affirmatively or by deemer, in the state in which the issuing insurer is domiciled, the form of contract filed for approval shall be accompanied by a statement of this fact, together with a plan of operation pertaining to the contract.

Drafting Note: The state of filing may request the plan of operation for informational purposes and may take it into account in deciding whether to approve the form. It is not anticipated that the state of filing would review and approve the plan of operation, but may use it in connection with the review of the form of contract.

Drafting Note: In the case that the plan of operation has not been approved, either affirmatively or by deemer, in the state of domicile of the issuing insurer, the state of issue, in issuing contract approvals, may wish to establish requirements to be met by the issuing insurer (e.g., notice requirement if the plan of operation subsequently changes, or requirement that the contract be operated in compliance with the plan of operation) in order to maintain its approval.

#### Section 7. Investment Management of the Segregated Portfolio

A. The investment manager must have full responsibility for, and control over, the management of all segregated portfolio assets within the constraints specified in the investment guidelines.

Drafting Note: In the event that the segregated portfolio has multiple managers, all of these managers will be covered by the investment guidelines.

B. The investment guidelines shall be submitted to the insurer for underwriting review before the contract becomes effective.

C. If the insurer accepts a proposed change to the investment guidelines or allows the contract to operate in accordance with investment guidelines not meeting the criteria established in Section 5B(1)(g), approval of the non-conforming investment guidelines must be obtained pursuant to Section 5B.

## Section 8. Purchase of Annuities

For contracts that are group annuity contracts, and that make available to the contractholder the purchase of immediate or deferred annuities for the benefit of individual members of the group, an annuity may not be purchased without the delivery of the contractually agreed upon consideration in cash to the insurer from the segregated portfolio for allocation to the insurer's general account or a separate account. The insurer shall collect adequate consideration for the cost of annuities purchased under contract option by transfer from the segregated portfolio.

## Section 9. Unilateral Contract Terminations

A contract subject to this regulation shall allow the insurer to unilaterally and immediately terminate, without future liability of the insurer or obligation to provide further benefits, upon the occurrence of any one of the following events that is material and that is not cured within thirty (30) days following the insurer's discovery of it:

- A. The investment guidelines are changed without the advance consent of the insurer and the investment manager is not controlling, controlled by or under common control with the insurer;
- B. The segregated portfolio, if managed by an entity that is not controlling, controlled by or under common control with the insurer, is invested in a manner that does not comply with the investment guidelines; or
- C. Investment discretion over the segregated portfolio is exercised by or granted to anyone other than the investment manager.

## Section 10. Reserves

### A. Asset maintenance requirements for segregated portfolios governed by this regulation.

(1) At all times an insurer shall hold minimum reserves in the general account or one or more separate accounts, as appropriate, equal to the excess, if any, of the value of the guaranteed contract liabilities, determined in accordance with Paragraphs (6) and (7) of this subsection, over the market value of the assets in the segregated portfolio less the deductions provided for in Paragraph (2) of this subsection. The reserve requirements of this subsection shall be applied on a contract-by-contract basis.

(2) In determining compliance with the asset maintenance requirement and the reserve for guaranteed contract liabilities specified in Paragraph (1) of this subsection, the insurer shall deduct a percentage of the market value of an asset as follows:

- (a) For debt instruments, the percentage shall be the NAIC asset valuation reserve "reserve objective factor," but the factor shall be increased by fifty percent (50%) for the purpose of this calculation if the difference in durations of the assets and liabilities is more than one-half year.
- (b) For assets that are not debt instruments, the percentage shall be the NAIC asset valuation reserve "maximum reserve factor."

(3) To the extent that guaranteed contract liabilities are denominated in the currency of a foreign country and are supported by segregated portfolio assets denominated in the currency of the foreign country, the percentage deduction for these assets under Paragraph (2) of this subsection shall be that for a substantially similar investment denominated in the currency of the United States.

(4) To the extent that guaranteed contract liabilities are denominated in the currency of the United States and are supported by segregated portfolio assets denominated in the currency of a foreign country, and to the extent that guaranteed contract liabilities are denominated in the currency of a foreign country and are supported by segregated portfolio assets denominated in the currency of the United States, the deduction for debt instruments under Paragraph (2) of this subsection shall be increased by fifteen percent (15%) of the market value of the assets unless the currency exchange risk on the assets has been adequately hedged, in which case the percentage deduction under Paragraph (2) of this subsection shall be increased by one-half percent (.5%). No guaranteed contract liabilities denominated in the currency of a foreign country shall be supported by segregated portfolio assets denominated in the currency of another foreign country without the approval of the commissioner. For purposes of this paragraph, the currency exchange risk on an asset is deemed to be adequately hedged if:

- (a) It is an obligation of
  - (i) A jurisdiction that is rated in one of the two (2) highest rating categories by an independent nationally recognized United States rating agency acceptable to the commissioner;
  - (ii) Any political subdivision or other governmental unit of such a jurisdiction, or any agency or instrumentality of jurisdiction, political subdivision or other governmental unit; or
  - (iii) An institution that is organized under the laws of any such jurisdiction; and

(b) At all times the principal amount of the obligation and scheduled interest payments on the obligation are hedged against the United States dollar pursuant to contracts or agreements that are:

(i) Issued by or traded on a securities exchange or board of trade regulated under the laws of the United States or Canada or a province of Canada;

(ii) Entered into with a United States banking institution that has assets in excess of \$5 billion and that has obligations outstanding, or has a parent corporation that has obligations outstanding, that are rated in one of the two (2) highest rating categories by an independent, nationally recognized, United States rating agency, or with a broker-dealer registered with the Securities and Exchange Commission that has net capital in excess of \$250 million; or

(iii) Entered into with any other banking institution that has assets in excess of \$5 billion and that has obligations outstanding, or has a parent corporation that has obligations outstanding, that are rated in one of the two (2) highest rating categories by an independent, nationally recognized, United States rating agency and that is organized under the laws of a jurisdiction that is rated in one of the two (2) highest rating categories by an independent, nationally recognized United States rating agency.

(5) These contracts may provide for the allocation to one or more separate accounts of all or any portion of the amount needed to meet the asset maintenance requirement. If the contract provides that the assets in the separate account shall not be chargeable with liabilities arising out of any other business of the insurer, the insurer shall maintain in a distinct separate account that is so chargeable:

(a) That portion of the amount needed to meet the asset maintenance requirement that has been allocated to separate accounts; less

(b) The amounts contributed to separate accounts by the contractholder in accordance with the contract and the earnings on the contract.

(6) For purposes of this section, the minimum value of guaranteed contract liabilities is defined to be the sum of the expected guaranteed contract benefits, each discounted at a rate corresponding to the expected time of payment of the contract benefit that is not greater than the maximum multiple of the spot rate supportable by the expected return from the segregated portfolio assets, and in no event greater than 105 percent of the spot rate as described in the plan of operation (pursuant to Section 5) or the actuary's opinion and memorandum, (pursuant to Section 10B), except that if the expected time of payment of a contract benefit is more than thirty (30) years, it shall be discounted from the expected date of payment to year thirty (30) at a rate of no more than eighty percent (80%) of the thirty-year spot rate and from year thirty (30) to the date of valuation at a rate not greater than 105 percent of the thirty-year spot rate.

(7) In calculating the minimum value of guaranteed contract benefits:

(a) All guaranteed benefits potentially available to the contractholder on an ongoing basis shall be considered in the valuation process and analysis, and the reserve held must be sufficient to fund the greatest present value of each independent guaranteed contract benefit. For purposes of this subparagraph, the right granted to the contractholder to exit the contract by discharging the insurer of its guarantee obligation under the contract and taking control of the assets in the segregated portfolio shall not be considered a guaranteed benefit.

(b) To the extent that future guaranteed cash flows are dependent upon the benefit responsiveness of an employer-sponsored plan, a best estimate based on company experience, or other reasonable criteria if company experience is not available, shall be used in the projections of future cash flows.

#### B. Actuarial opinion and memorandum for segregated portfolios governed by this regulation.

(1) An insurer that issues a synthetic guaranteed investment contract subject to this regulation shall submit an actuarial opinion and, upon request, a memorandum to the commissioner annually by March 1 following the December 31 valuation date showing the status of the accounts as of the prior December 31. The actuarial opinion and memorandum shall be in form and substance satisfactory to the commissioner.

Drafting Note: The state may wish to include the information contained in the actuarial opinion and memorandum as a part of its overall filing requirements, rather than mandating a separate filing for synthetic guaranteed investment contracts.

(2) The actuarial memorandum required by this regulation is deemed to be confidential to the same extent, and under the same conditions, as the actuarial memorandum required by [insert reference to state law equivalent to Section 3 of the NAIC Model Standard Valuation Law].

Drafting Note: A thorough review should be performed of the specific laws and regulations in a state which may affect the confidential status of the memorandum.

(3) Except in cases of fraud or willful misconduct, the valuation actuary shall not be liable for damages to any person (other than the insurance company and the commissioner) for any act, error, omission, decision, or conduct with respect to the actuary's opinion.

- (4) The statement of actuarial opinion submitted in accordance with Section 10B(1) shall consist of:
- (a) A paragraph identifying the valuation actuary and his or her qualification;
  - (b) A scope paragraph identifying the subjects on which the opinion is to be expressed and describing the scope of the valuation actuary's work;
  - (c) A reliance paragraph describing those areas, if any, where the valuation actuary has deferred to other experts in developing data, procedures or assumptions;
  - (d) An opinion paragraph expressing the valuation actuary's opinion with respect to the matters described in Subparagraphs 5A and 5B below; and,
  - (e) One or more additional paragraphs may be needed in individual company cases as follows:
    - (i) If the valuation actuary considers it necessary to state a qualification of his or her opinion;
    - (ii) If the valuation actuary must disclose an inconsistency in the method of analysis used at the prior opinion date with that used for this opinion;
    - (iii) If the valuation actuary chooses to add a paragraph briefly describing the assumptions which form the basis of the actuarial opinion.
- (5) Contents of the opinion paragraph of the actuarial opinion.
- (a) The actuarial opinion shall state that, after taking into account any risk charge payable, the segregated portfolio assets, and the amount of any reserve liability with respect to the asset maintenance requirement, the account assets make adequate provision for contract liabilities.
  - (b) The opinion shall also state that:
    - (i) Reserves for contract liabilities are calculated pursuant to the requirements of Section 10A(1);
    - (ii) After taking into account any reserve liability with respect to the asset maintenance requirement, the amount of the account assets satisfied the asset maintenance requirement;
    - (iii) The fixed-income segregated portfolio conformed to and justified the rates used to discount contract liabilities for valuation pursuant to Section 10A(6);
    - (iv) Whether any rates used pursuant to Section 10A(6) to discount guaranteed contract liabilities and other items applicable to the segregated portfolio were modified from the rate or rates described in the plan of operation filed pursuant to Section 5; and,
    - (v) The level of risk charges, if any, retained in the general account was appropriate in view of such factors as the nature of the guaranteed contract liabilities and losses experienced in connection with account contracts and other pricing factors.
- (6) The opinion shall be accompanied by a certificate of an officer of the insurance company responsible for monitoring compliance with the asset maintenance requirements for synthetic guaranteed investment contracts describing the extent to and manner in which, during the preceding year:
- (a) Actual benefit payments conformed to the benefit payment estimated to be made as described in the plan of operation;
  - (b) The determination of the fair market value of the segregated portfolio conformed to the valuation procedures described in the plan of operation, including a statement of the procedures and sources used during the year; and,
  - (c) Any assets were transferred to or from the insurer's general account, or any amounts were paid to the insurer by any contractholder to support the insurer's guarantee.
- (7) The actuarial memorandum shall:
- (a) Substantially conform with those portions of Section [insert reference to section of the regulations related to actuarial memoranda] of these regulations that are applicable to asset adequacy testing and either:
    - (i) Demonstrate the adequacy of account assets based upon cash flow analysis, or
    - (ii) Explain why cash flow testing analysis is not appropriate, describe the alternative methodology of asset adequacy testing used, and demonstrate the adequacy of account assets under that methodology;



- (b) Clearly describe the assumptions the valuation actuary used in support of the actuarial opinion, including any assumptions made in projecting cash flows under each class of assets, and any dynamic portfolio hedging techniques utilized and the tests performed on the utilization of the techniques;
  - (c) Clearly describe how the valuation actuary has reflected the cost of capital.
  - (d) Clearly describe how the valuation actuary has reflected the risk of default on obligations and mortgage loans, including obligations and mortgage loans that are not investment grade;
  - (e) Clearly describe how the valuation actuary has reflected withdrawal risks, if applicable, including a discussion of the positioning of the contracts within the benefit withdrawal priority order pertaining to the contracts;
  - (f) If the plan of operation provides for investments in segregated portfolio assets other than United States government obligations, demonstrate that the rates used to discount contract liabilities pursuant to Section 10A(6) conservatively reflect expected investment returns, taken into account any foreign exchange risks;
  - (g) If the contracts provide that in certain circumstances they would cease to be funded by a segregated portfolio and, instead would become contracts funded by the general account, clearly describe how any increased reserves would be provided for if and to the extent these circumstances occurred;
  - (h) State the amount of account assets maintained in a separate account that are not chargeable with liabilities arising out of any other business of the insurance company;
  - (i) State the amount of reserves and supporting assets as of December 31 and where the reserves are shown in the annual statement; and
  - (j) State the amount of any contingency reserve carried as part of surplus.
  - (k) State the market value of the segregated asset portfolio.
  - (l) Where separate account assets are not chargeable with liabilities arising out of any other business of the insurance company, describe how the level of risk charges payable to the general account provides an appropriate compensation for the risk taken by the general account.
- C. When the insurer issues a synthetic guaranteed investment contract and complies with the asset maintenance requirements of Section 10A, it need not maintain an asset valuation reserve with respect to those account assets.
- D. This section describes the reserve valuation requirements for contracts subject to this regulation.
- (1) Reserves for synthetic investment contracts subject to this regulation shall be an amount equal to the sum of the following:
    - (a) The amounts determined as the minimum reserve as required under Section 10A(1);
    - (b) Any additional amount determined by the insurer's valuation actuary as necessary to make adequate provision for all contract liabilities; and
    - (c) Any additional amount determined as necessary by the commissioner due to the nature of the benefits.
  - (2) The amount of any reserves required by Paragraph (1) of this subsection may be established by either:
    - (a) Allocating sufficient assets to one or more separate accounts; or
    - (b) Setting up the additional reserves in the general account.

#### Section 11. Severability

If any provision of this regulation or its application to any person or circumstances is judged invalid by a court of competent jurisdiction, the judgment shall not affect or impair the validity of the other provisions of this regulation.

#### Section 12. Effective Date

This regulation shall take effect [insert date].

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## ATTACHMENT SIX-B

To: Separate Accounts Working Group  
 Synthetic GIC Working Group  
 From: Doug Barnert (Barnert Associates)  
 Date: December 6, 1998  
 Re: Recommended Changes to the Dec. 2, 1998, Draft of the Synthetic Guaranteed Investment Contracts Model Regulation

Amend the minutes of the joint conference call of the Separate Accounts and Synthetic GIC Working Groups by adding the following paragraph before to final paragraph to read as follows:

There was some discussion among regulators and interested persons regarding the reporting path to adopt each model. The Separate Accounts Working Group reports to the Accounting Practices and Procedures (EX4) Task Force and the Synthetic GIC Working Group reports to the Life Insurance (A) Committee. However, since both working groups seek to maintain harmonization of the two models whenever possible and members were concerned that on separate paths, different amendments could find their way into the models. Also, there are accounting issues and life insurance issues in both models which should be approved by each parent entity.

One suggestion was to make a joint referral at the December meeting to the Accounting Practices and Procedures (EX4) Task Force and the Life Insurance (A) Committee, however, no decision was reached.

The joint working groups agreed to consider the issue, consult with staff and the leaders of each parent entity and decide the question at the December NAIC Meeting.

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## ATTACHMENT SEVEN

1999 Charges  
 Life Insurance And Annuities (A) Committee

The mission of the Life Insurance and Annuities (A) Committee is to consider issues relating to life insurance and annuities, review new life insurance products and establish priorities of the Life and Health Actuarial (Technical) Task Force.

1. Review Life Insurance Illustrations Model Regulation for possible changes necessitated by revision of the Life Insurance Nonforfeiture Law and development of equity-indexed life insurance products and state experience in implementing the model. Make technical changes identified as necessary during discussion of the model. Complete by Winter National Meeting.
2. Continue review and amendment process for model laws with potential for that conflict with the Life Insurance Illustrations Model Regulation.
3. Review other NAIC model laws for potential conflicts with the Annuities Disclosure and Sales Illustrations Model Regulation and revise as necessary.
4. Review Universal Life Model Regulation and revise as necessary.
5. Establish model requirements for policy illustrations or ledger information disclosed or made available to consumers of variable life insurance and variable annuities by the Fall National Meeting, subject to coordination with regulatory initiatives of the Securities and Exchange Commission and the National Association of Securities Dealers.
6. Complete revision of the Viatical Settlements Model Regulation by the Spring National Meeting.
7. Consider appropriate regulatory response to issues related to investments in viatical settlements. Make recommendations by the Fall National Meeting.
8. Develop an "Alert" program to describe for regulators, media and investors the viatical settlement industry and the considerations for those regulating or investing in the market. Develop a packet of materials for distribution by the Summer National Meeting.
9. Consider issues related to insurable interest, fraud and the impact on the traditional role of life insurance to address practices related to soliciting individuals to purchase insurance with the purpose of viaticating the policy. Report by the Winter National Meeting.
10. Develop a handbook to assist regulators in interpretation of viatical settlement data submitted by companies to determine reasonableness of payments. Report on progress by Winter National Meeting.
11. Consider development of an NAIC model covering life insurance sales by healthy individuals. Report on progress at Winter National Meeting.

12. Make recommendations for changes to Life Insurance Advertising Model Regulation. Consider replacement issues related to advertising and coordinate with group working on disclosure issues. Complete by Fall National Meeting.

13. Draft a white paper discussing issues related to suitability of sales of life insurance and annuities. Make recommendations as to the advisability of drafting a model law or regulation giving insurers responsibility to determine suitability of sales of life insurance and annuities.

14. Develop a list of items that should be addressed by regulators when reviewing contract filings for equity-indexed products, including agent training by the insurer.

15. Consider issues related to sales of structured settlement annuities for immediate cash.

16. Oversee changes and provide technical assistance as appropriate for the production of the *Market Share Reports for the Top 125 Life and Fraternal Insurance Groups and Companies by State*. This is an on-going charge.

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#### ATTACHMENT EIGHT

##### 2000 Charges Life Insurance And Annuities (A) Committee

The mission of the Life Insurance and Annuities (A) Committee is to consider issues relating to life insurance and annuities, review new life insurance products and establish priorities of the Life and Health Actuarial (Technical) Task Force.

1. Develop a handbook to assist regulators in interpretation of viatical settlement data submitted by companies to determine reasonableness of payments by Winter National Meeting.
2. Develop an NAIC model covering life insurance sales by healthy individuals by the Winter National Meeting.
3. Develop continuing education requirements for viatical settlement representatives and brokers.
4. Complete drafting of a white paper discussing issues related to suitability of sales of life insurance and annuities. Implement recommendation to develop a model law, or take other steps recommended, if necessary.
5. Review Annuity Disclosure Model Regulation to determine if technical changes are needed, or if illustration requirements should be developed.
6. Oversee changes and provide technical assistance as appropriate for the production of the *Market Share Reports for the Top 125 Life and Fraternal Insurance Groups and Companies by State*. This is an on-going charge.