



# AMERICAN ACADEMY *of* ACTUARIES

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**Update Regarding a General Revision  
Of Life and Annuity Standard Nonforfeiture Laws  
From the American Academy of Actuaries' Nonforfeiture Improvement Work Group**

**Presented to the National Association of Insurance Commissioners'  
Life and Health Actuarial Task Force**

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The American Academy of Actuaries is a 16,000-member professional association whose mission is to serve the public on behalf of the U.S. actuarial profession. The Academy assists public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

Nonforfeiture Improvement Work Group

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Since the NAIC Winter 2008 National Meeting in December, the American Academy of Actuaries' Nonforfeiture Improvement Work Group and its subgroups have continued to hold weekly and bi-weekly conference calls. The charge from LHATF to the Academy work group is to:

*“Study the feasibility of a new nonforfeiture law for life insurance and annuities to replace the existing nonforfeiture standards. Provide quarterly status reports on this project.”*

This report constitutes the requested quarterly status report on the progress of the Academy work group's activities.

The work group continues to refine the approach to nonforfeiture reform it believes will accomplish the elements contained in its previously-articulated framework for reform. Those elements as of the date of this report are:

- Minimum nonforfeiture values should be based on the prefunding of benefits resulting from premium payments and credited values.
- Minimum nonforfeiture regulatory requirements should provide guidance with respect to minimum nonforfeiture methodologies and the establishment of assumptions; not explicitly defined values or parameters.
- In determining minimum nonforfeiture values, there should be no recognition of a change in insurability status since the date of policy purchase.
- Any minimum nonforfeiture methodology requirements should be the same for life and annuity products.
- Non-guaranteed elements (including dividends) should not be regulated by minimum nonforfeiture regulatory requirements until they are credited.

In addition, in considering any approach to nonforfeiture reform, the Academy work group is cognizant of the need to establish a regulatory framework within which the actuarial aspects of the reform package will operate best for regulators, industry and consumers. Such a framework will include laws, regulations and Actuarial Standards of Practice, within which, in addition to the proposed actuarial approach to reform, appropriate regulatory reporting, consumer disclosure, and industry statistical agent information requirements will be present.

In developing its nonforfeiture reform approach, the Academy work group is attempting to respond to numerous deficiencies in the current formula-based nonforfeiture mandates that have become unresponsive to products emerging in the life insurance and annuity marketplace.

Many of these deficiencies have been highlighted by the public activities of the NAIC Interstate Compact National Standards Working Group (“NAIC working group”), the group charged with developing product standards for policies submitted for approval to the Interstate Insurance Product Regulation Commission (IIPRC) for use in all IIPRC states.

In addition to developing the policy language standards for policy forms under its jurisdiction, the NAIC working group is also charged with developing standards for the Actuarial Memorandum submitted to the IIPRC in support of minimum nonforfeiture values for each product, since nonforfeiture values fall within the “four corners” of the policy form itself. In developing standards for the Actuarial Memorandum, the NAIC working group has had to address a number of situations where the existing life and annuity nonforfeiture law is not clear as to its application to the product under consideration. This process has brought into sharp focus the problems associated with a prescribed formulaic approach to minimum nonforfeiture mandates, as companies seek to market an ever-changing array of new products.

The NAIC working group’s activities in the area of developing standards for minimum nonforfeiture value compliance take place in a “real world” environment. That environment includes the need to attract additional states to join the IIPRC, the desire to have industry players submit policy forms to the IIPRC, and the state and federal political dynamic with respect to regulatory oversight. These imperatives underscore the urgency of the standards development process and hence the immediacy of the need to deal with minimum nonforfeiture compliance issues for certain products. The luxury of an extended time frame to “vet” with various parties each nonforfeiture compliance demonstration approach is not available. The consequence is that nonforfeiture compliance demonstrations for products not fitting neatly into an increasingly archaic nonforfeiture law are more and more being developed by the NAIC working group. Although this group contains numerous regulatory actuaries who have been very active in the process, the necessity to continually interpret a nonforfeiture law that does not adequately address products in the current insurance marketplace is not ideal.

The attached chart, prepared by the Academy work group, indicates the products for which guidance for the determination of minimum nonforfeiture values has been developed by the NAIC working group (or will need to be developed in the near future). The chart indicates for each product listed the NAIC model law governing minimum nonforfeiture values, the current state approach to minimum nonforfeiture value compliance, and the IIPRC approach to minimum nonforfeiture value compliance.

The Academy work group appreciates the opportunity to keep LHATF apprised of its activities with regard to the charge assigned.

## Current Minimum Nonforfeiture Compliance Approaches

Product Category	Product	Current Situation		
		Governing NAIC Model Law	State Approach to Compliance	IIPRC Approach to Compliance
Traditional Non-Variable Life Insurance	WL/Term other than ROP	Life SNFL # 808	Formula driven with minor variations	Formula driven as per SNFL
	Return Of Premium	Life SNFL # 808	No consistency before AG CCC (45); same as Compact after AG 45, as long as compliance with AG 45 is required.	Compliance with AG 45 required, meaning that min NF/CV calc must be done over ROP period for endowment (i.e. prefunding must be recognized and CV required.).
Non-traditional Non-Variable Life Insurance	UL	UL Model #585	UL Model #585	UL Model #585
	UL w 2ndary Guarantees	UL Model #585	UL Model #585, but 2ndary guarantee is ignored. Min values do not consider 2ndary guarantee	UL Model #585, but 2ndary guarantee is ignored. Min values do not consider 2ndary guarantee
	Index-Linked	UL Model #585	UL Model #585	UL Model #585
Variable Life Insurance (SA only)	VUL	VUL Model #270 and AG 24	VUL Model #270 and AG 24	VUL Model #270 and AG 24
Deferred Non-Variable Annuities	Basic	Annuity SNFL # 805; Model Reg 806	Inconsistent interpretation of prospective test.	More restrictive interpretation of prospective test that has only been adopted in a small number of states, generally reducing average duration and level of back end loads.
	Index-Linked	Annuity SNFL # 805; Model Reg 806	Inconsistent interpretation of prospective test (see basic annuity)	More restrictive interpretation of prospective test (see basic annuity)
	Bonus	Annuity SNFL # 805; Model Reg 806	Inconsistent interpretation of prospective test	More restrictive interpretation of prospective test requiring funding of full bonus by Maturity Date.
	MVA	Annuity SNFL # 805; Model Reg 806	Not permitted or Inconsistent interpretation of prospective test	More or less restrictive interpretation of prospective test depending on type of MVA product.
	GMLBs	Annuity SNFL # 805; Model Reg 806	No published or regulatory nonforfeiture requirements	Has not yet addressed.
	Longevity Insurance	Annuity SNFL/Reg # 805/806	Inconsistent interpretation of need for paid up annuity nonforfeiture value	Has not yet addressed.
Deferred Variable Annuities (SA only)	Basic	Model Variable Annuity Reg #250	Literal interpretation of model	Literal interpretation of model
	Bonus	Model Variable Annuity Reg #250	Literal interpretation of model	Literal interpretation of model; bonus to be considered gross consideration.
	MVA	Model MGA #255	Literal interpretation of model, where the state allows MGAs	Literal interpretation of model
	GMLBs	Model Variable Annuity Reg #250	No published or regulatory nonforfeiture requirements	Has not yet been addressed.
Immediate Annuities	W/O Commutation Benefit	Excluded from Ann SNFL	Nonforfeiture not a requirement	Nonforfeiture not a requirement
	W/ Commutation Benefit	Excluded from Ann SNFL	Some states have very limited requirements on commutation	Rigorous new disclosure requirements only.