AMERICAN ACADEMY *of* ACTUARIES

SURVEY OF FIRST-YEAR COMPANY EXPERIENCE UNDER LIFE ILLUSTRATION REGULATIONS BASED ON THE NEW NAIC MODEL

REPORT OF THE DISCLOSURE WORKING GROUP COMMITTEE ON STATE LIFE INSURANCE ISSUES

JUNE 1998

The American Academy of Actuaries is the public policy organization for actuaries of all specialties within the United States. In addition to setting qualification standards and standards of actuarial practice, a major purpose of the Academy is to act as the public information organization for the profession. The Academy is nonpartisan and assists the public policy process through the presentation of clear actuarial analysis. The Academy regularly prepares testimony for Congress, provides information to federal elected officials and congressional staff, comments on proposed federal regulations, and works closely with state officials on issues related to insurance.

This report was prepared by the Academy's Disclosure Work Group of the Committee on State Life Insurance Issues at the request of the Life Disclosure Working Group of the National Association of Insurance Commissioners (NAIC). Members of the Academy work group are:

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Special thanks is owed to the Work Group's Life Illustrations Survey Subgroup. The subgroup took the lead in designing the survey, overseeing its administration and coding and, preparing the analysis for the larger work group. Richard Ostuw chaired the subgroup. Its other members included Donna Claire, John Dinius, Richard Fuerstenberg, Jane Hamrick, and Roger Wiard-Bauer. Special thanks are due Charlotte S. Liptak, J.D., who participated at all stages of the development and analysis of the survey.

I. INTRODUCTION

At the request of the National Association of Insurance Commissioners (NAIC), the American Academy of Actuaries conducted a survey of companies' first year of experience under state regulations based on the NAIC Life Insurance Illustrations Model Regulation. For convenience, this report refers to the model and the array of state regulations as "the Regulation."

This report presents findings from the company survey.

II. METHODOLOGY

The life illustration survey was sent to chief actuaries of U.S. life insurance companies. It requested that the chief actuary coordinate the company's response to the survey. In cases where the company did not have a chief actuary on its internal staff, an attempt was made to route the survey to an appropriate company official. Chief actuaries were identified through the current membership records of the Society of Actuaries. To include companies without chief actuaries, the American Council of Life Insurance (ACLI) and the National Alliance of Life Companies (NALC) agreed to send the survey to their member companies requesting that it be routed to the appropriate respondent.

Responses were collected from mid-January through mid-February 1998. Each response represented an individual life insurance company's experience. A total of 88 companies responded to the survey. Of these, 83 (over 90 percent) responded to most questions. The remaining five companies did not respond to any of the questions. The primary reason given for not responding was a lack of any relevant experience with the new sales illustration regulation. Many of the 83 respondents provided narrative comments in addition to choosing among the pre-coded answers. Narrative responses were recorded and considered throughout the analysis.

The survey was lengthy. This is because the regulation affects many aspects of the business of life insurance including: sales methods, policyholder communications and product design. Moreover, it covered information within several areas of responsibility, including the responsibilities of illustration actuaries and responsible officers, of underwriters and of information systems officers. Although the survey covered several areas of responsibility, each company was requested to provide a single response for each question using judgement concerning the product lines and distribution systems covered.

In order for the Academy to maintain the confidentiality of survey respondents, the identities of companies and details of specific responses are not revealed in this report.

III. SUMMARY OF MAJOR FINDINGS

The NAIC Life Insurance Illustrations Model Regulation has the stated purpose of providing rules for life insurance illustrations that will protect consumers and foster consumer education. During its development, alternatives were considered and efforts made to find workable solutions for logistical and implementation concerns expressed by the industry. Marketplace changes and innovations since the adoption of the model and similar state regulations may need to be considered. The survey gathered information on the companies' perspectives on these issues.

Meeting the Regulation's Purpose

The Regulation seems to have been reasonably successful at meeting its stated purpose. Illustrations are being shown to applicants and signed. They also tend to be longer with some improvement in consumer understanding. A majority of companies are using illustrations for many of their individual life products. Based on the significant increase in the number of pages used for illustrations, more information is being given to consumers. Forty percent of companies that commented on consumer understanding believed that the illustrations were helping consumers more than the previous ones. Another forty percent believed that the effects were not significant. Slightly over half of the companies are having at least 75 percent of illustrations returned with signatures, when the illustrations are mailed by the company.

Workable Solutions

In many cases, solutions proposed during the Regulation's development have been workable. Companies are usually receiving policyholder signatures.

A majority of companies use fully allocated expenses for actuarial testing, while most others use the Generally Recognized Expense Table (GRET) which reflects industry average expenses. A substantial minority made at least minor changes to their expense allocation methods. Some report that the GRET should be more product specific including some adjustments for first-year dump-in premiums on universal life and policies with small face amounts. Some also felt that the GRET was overly strict. Respondents report elements of rate regulation, difficulties in designing products that reward persisting policy holders, and aspects of a non-level playing field among products.

The regulation has had some possible negative impacts. Comments reflected difficulties with worksite products, policies with smaller face amounts, a variety of widely-sold products, and illustration of sophisticated scenarios (e.g., “split dollar”). An adverse impact on the levels of illustrated non-guaranteed elements was reported by a minority of respondents. With respect to the actuarial tests, they also reflected difficulties with persistency bonuses, rapid build ups of cash values, and policies with small face amounts. Thirteen percent of respondents reported a significant adverse impact on sales. A broad variety of reasons were cited for potentially negative sales impacts including the increased length of illustrations.

Other Regulatory Issues and Suggestions For Annuity and Variable Product Regulations

Comments to a variety of general questions cover a wide range of issues and reflect some difficulties with ambiguities under the new regulation and state-to-state variations in requirements. Some support was noted for selective transfer of Q&A and Practice Notes material to the Regulation or Actuarial Standard of Practice (ASOP) Number 24. For example, actuarial testing practices with respect to riders and reinsurance tend to vary.

The survey responses show wide use of illustrations and some indication that the use of laptop computer screen illustrations may continue to grow.

Some expressed concern that regulations applicable to fixed annuities and/or variable life and annuity products should be less burdensome and maintain a level playing field for annuities with non-insurance financial accumulation products. Some comments support increased use of disclosure for certain types of product features, perhaps as a substitute for annuity actuarial testing.

IV. LIFE ILLUSTRATION SURVEY FINDINGS

The questions in the survey focused on impact of the regulation on:

- the marketing process
- agent and policyholder signature requirements
- non-guaranteed elements
- product design
- new sales illustration systems
- annual report systems
- self-support and lapse-support tests, and
- other regulatory issues.

Findings in each area are discussed below. The questionnaire and a question-by-question tabulation of responses are appended.

Impact on Marketing Process

1. Percentage of policies subject to the regulation

The results are very much as expected. The categorized responses indicate that, for 70 percent of the companies, illustrations are potentially required for at least 75 percent of individual life insurance policies sold. However, companies' comments on the question suggest that the percentage may be somewhat higher. It appears that at least a couple of respondents included policies that have only guaranteed benefits. It also appears that if variable policies were covered, the percentage would also increase.

2. Use of laptops in lieu of printed illustrations

Twenty percent of respondents did not know how illustrations were presented for their products. Of those that did, about two-thirds estimate that less than 10 percent of their sales requiring illustrations are based on showing consumers illustrations on a laptop with no printed copy. Comments on this question indicate that the percent using laptop illustrations may increase over time and once the regulations is applicable to variable products.

3. Use of generic vs. individualized quotations in the employer market

About two-thirds of companies either did not respond or commented that they were not in the non-term group-life market . Of the nearly one-third of companies that are in this market, a little over 6 out of 10 indicated that only generic quotations are used. The remaining 38 percent provide each employee with a personalized illustration.

4. Satisfying requirements for direct market sales

Nearly 60 percent of the companies did not have experience with direct market (i.e., non-producer) sales in the individual life insurance market. Of those with experience in direct market sales, at least 60 percent are not using illustrations. Most of the others are providing an illustration based on personalized information.

Agent and Policyholder Signature Requirements

1. Distribution system

In answering questions on signature requirements, 77 of the 80 companies based their responses on producer-sold business. Of the remaining three companies, one based its responses on telemarketed business, and two based their responses on other types of direct marketing.

2. Percent of policies requiring a post-application illustration

Nearly a third of companies said that at least 75 percent of their policies requiring illustrations required that one be provided after an application has been submitted to the company. Some commented that this was because illustrations were automatically sent with policies and because of changes in the crediting rate from time of application.

Another third of the companies said that less than 25 percent of their policies required post-application illustrations. The final third were split about evenly between the 25-to-50 percent and 50-to-75 percent ranges.

3. Percent of customers returning company-sent, post-application illustrations

Over half of the companies are experiencing at least a 75 percent return rate on signed illustrations, when the final illustrations are mailed out by the company. For 20 percent of the companies, the return rate of signed illustrations is under 25 percent.

4. Procedures being used to meet signature requirements

Companies use a range of methods for encouraging that illustrations are signed and returned, and any given company may use more than one method. Responses were fairly evenly split among four procedures: Requiring a signature before processing the application, before issuing the policy, before paying commissions, or by making a good faith effort to get a signature after issuing the policy. Of the seven other procedures that were written in, the most common was initially crediting commissions, but reversing the credit if the signed form was not received within a specified time.

Impact on Consumer Understanding and the Sales Process

1. Improvements in consumer understanding

Eighty percent of those responding for their company felt they had sufficient experience to have an impression of how the new regulations were affecting consumers' understanding of the products they purchase.

Forty-one percent believed that the new illustrations were helping consumers more than the previous ones had, and 40 percent believed that the old and new illustrations contributed about the same to consumer understanding. However, companies are not without concerns. Specific concerns included the length of the illustration, whether the consumer actually read it (even though the information has been improved), and whether there would be sufficient protection in a high interest rate environment.

2. Impact on overall sales of the companies' products

Of the 86 percent of companies with experience to share, nearly 80 percent said that the new regulations have not had a major impact on sales. Of the remaining 20 percent, about two-thirds felt the new regulations had hurt sales while a third felt the new regulations had actually contributed to higher sales.

Comments on how the regulation has hurt sales included: Lack of consumer understanding of the illustrations themselves, and changes in the competitive environment as a result of the new regulation among which was listed difference in interpretations that have caused competitive problems. Other reasons listed for sales having been hurt related to agents. Comments here included individual statements such as the following: giving agents another reason not to sell life products, agents moving to non-illustrated products, agents not making lower premium sales, an increase in time to complete the sale, resistance of the agents to the longer illustration. Finally, there were such reasons as additional paper and signatures, delay in getting compliant illustrations to the field, and clients liking universal life less because they better understand its non-guaranteed design.

Impact on Non-guaranteed Elements

1. Impact on the level of illustrated non-guaranteed elements

Of those companies with experience, the overall level of non-guaranteed elements did not change for 68 percent. They became less favorable for 31 percent of companies. Only one of the 72 companies with experience in this area said that illustrated non-guaranteed elements become more favorable to the policyholder.

2. Paid vs. illustrated non-guaranteed elements

The vast majority of companies are crediting and charging the same non-guaranteed elements as illustrated.

Impact on Product Design

1. Product design modifications

Nearly half of companies have not changed their products in response to the new regulation of sales illustrations nor do respondents think that any change is likely.

The other half of the companies already have or expect to change the design of some or all of their products. Moreover, the list of possible areas for modification is fairly long, including commissions, charge-backs, guarantees provided, credited interest rates, current mortality charges, current expense charges, and product illustration. Very few companies identified changes to surrender charges and loan programs.

In their comments companies mentioned other product design features for potential modification including persistency bonuses, elimination of annuity side funds, issue limit changes (e.g., age range, minimum amount), current premiums on indeterminate premium products, and shifts in load structure to earlier years.

2. Products and features that do not fit well under the regulation or actuarial tests

On treatment under the regulation, comments reflected difficulties with worksite products, indeterminate premium products, adjustable life products, concept illustrations (e.g., split dollar), how to handle certain scenarios in the numeric summary, equity-indexed products, concern about portfolio rates being used when new money rates are lower, and certain whole life situations (e.g., premium offset, withdrawals).

On treatment under actuarial tests, comments reflected difficulties with the no-lapse assumption after the fifth policy duration, persistency bonuses, indeterminate premium products, products with rapid build up of early cash values, and small face amount policies.

Comments were made related to the application of the current-version GRET first-year factors, particularly for universal life dump-ins.

3. Impact of the lapse-support test on product innovations

Close to 80 percent said that the lapse-support test did not cause problems with product innovations. Of those that did find the test troublesome, a number indicated the test was too strict, particularly with respect to the inability to adjust mortality and expense assumptions. Others said that third party administrator costs, levelized commissions and reinsurance arrangements did not model well.

New Sales Illustration Systems

1. Cost of sales illustration systems for new sales

About 40 percent of companies spent under $100,000 modifying their existing or building a new illustration system for new sales. An additional 45 percent spent somewhere $100,000 and $500,000. For a significant 17 percent minority, the cost exceeded half a million dollars. One of the 77 responding companies incurred costs of over $1.0 million.

2. Controls on illustrated scales

Over 90 percent of companies have some type of system in place to control the level of non-guaranteed elements that the agent can illustrate. Moreover, it is generally true that the only non-guaranteed element the agent can change is the credited rate. This was indicated repeatedly in supplementary comments which were made for all of the response categories.

3. Average length of illustrations for new sales

Fewer than 10 percent have illustrations that average five or fewer pages. Much longer illustrations are clearly the rule. A little over 40 percent of companies report illustrations that average at least 10 pages.

4. Change in length of illustration for new sales

For over 95 percent of companies, illustrations are longer under the new regulations. For 40 percent, illustrations are 3 or 4 pages longer. And, for nearly 45 percent, illustrations are 5 or more pages longer, the highest category specified in the questionnaire. The increased length of illustrations was a significant complaint, and perhaps the greatest one, of many of the companies that responded.

5. Use of supplemental illustrations

Supplemental illustrations are used for a variety of purposes--primarily for concept illustrations (e.g., for split dollar) and voluntary policyholder actions (e.g., loans).

In-force Illustration Systems

1. Cost of illustration systems for in-force business

Half of the companies spent under $100,000 modifying or building illustration systems for in-force business. Another 43 percent spent between $100,000 and $500,000. Only a small minority (6 percent) spent over half a million dollars, and no one reported spending over $1.0 million.

2. Average length of illustrations for in-force business

Illustrations for in-force business are usually substantially shorter than those for new sales. Of the companies that were providing in-force illustrations, slightly over half have illustrations that average 5 or fewer pages. An additional 30 percent had illustrations of less than 8 pages. Only 7 percent had illustrations that averaged 10 or more pages.

Annual Report Systems

1. Annual report format for policies subject to and not subject to the regulation

Of the 91 percent of companies using annual reports, 85 percent were creating a new format for business subject to the new regulations. Over 60 percent will use the new format for both business subject and not subject to the new illustration requirements.

2. Costs for new or revised annual report systems

Eight-two percent of companies that use annual reports said there was some initial cost to revising annual report systems. A large majority (85 percent) said the cost was under $100,000. Most of the rest reported costs of between $100,000 and $200,000. Ten percent of those with start-up costs reported costs of $200,00 or more.

Self Support and Lapse Support Tests for New Sales and In-force business

1. On-going annual costs

It appears that the on-going costs of completing the new illustration regulations' testing and certification requirements have not significantly increased expenses. Eighty-five percent said the costs were $100,000 or less and no one said the costs exceeded $200,000.

Of those companies that specified the source of additional costs, the time commitment of the illustration actuary was the most common reply.

2. Additional *initial* costs

The initial cost of implementing the certification requirements also appears modest for most companies, with 10 percent incurring no extra first-year costs and 75 percent incurring $100,000 or less. This was not true for all companies, 14 percent reported costs between $100,00 and $500,000 and one company reported as costs between $500,000 and $1.0 million. Some of the higher initial expenses were due to the cost of hiring consultants to review the testing process and the cost of having illustration actuaries attend seminars.

3. Modification of expense allocations

For over half (55 percent) of companies, it was not necessary to update expense assumptions. Of the 40 percent who did modify expense allocations, slightly more than half described the changes as "some refinements", rather than as "a thorough review." Several said they had planned to review expense allocations anyway. Of the 18 percent of companies that thoroughly reviewed and updated their expense allocations, four-out-of-ten ended up using the GRET. The rest used fully allocated.

Of the companies who elaborated on their responses, most described minor reallocations of commissions and other expenses within a line of business. One company reported that it was forced to abandon macro-pricing methods as a result of the new regulation's requirements.

4. Expense method used

About 65 percent of companies are using fully allocated expenses. Most of the remainder use GRET; only 5 percent use marginal expenses. Some respondents indicated that their answer to this question was their current expense allocation method, and not necessarily the one they used when the new sales illustration regulations were first implemented.

5. GRET implementation problems

More than three-quarters of the companies did not report a problem implementing the GRET. Of the roughly 20 percent that did, the most common problems were:

- Unusually high expenses allocated to first-year dump-ins on universal life products, which was mentioned by a number of companies.
- GRET does not adequately distinguish between large and small policies, causing problems for policies with smaller face amounts.
- GRET needs to be product-specific.

6. Modifications to investment income allocation

Virtually all companies said that they either made no change or made only some minor refinements. Of the five companies that made more major changes, two said that they implemented a portfolio crediting strategy to make it easier to demonstrate compliance with the new regulation.

7. Illustration of alternative forms of payout

Most companies do not illustrate alternative forms of payout. Of those that do, 14 illustrate more than one of the forms listed. Some companies indicated that their response to this question does not apply to all illustrated products.

8. Testing of Riders

Six out of ten companies indicated that riders were tested separately from the base policy and were not used to help the basic coverage pass. Several companies explained that rider cash flows were aggregated with the basic coverage cash flows only if necessary to help the basic coverage pass. Some companies stated that they spent little time on riders either because their cash flows had a de minimus effect on aggregate cash flows or because the riders had no non-guaranteed elements.

9. Reinsurance

Roughly half of the companies with reinsurance have incorporated the resulting cash flows in their testing. Of those companies that did not include reinsurance, some said that ignoring the reinsurance was deemed to be conservative, while others said the impact of the reinsurance treaty was not material. Of those that used reinsurance cash flows, none indicated whether they were necessary in order to get products to pass the self-support and lapse-support tests. A few companies indicated that new reinsurance arrangements were created and incorporated.

10. Additional comments on self-support and lapse support

Additional comments regarding the Regulation fell into three broad categories: positive impacts, undesirable consequences of the prescribed rules, and the burden of creating and maintaining the required documentation. Specific comments in these categories were:

<u>Positive Impacts</u>

- Companies are more aware of their expense levels.
- Better expense allocation mechanisms may be developed.
- Illustrations will be more standardized.
- Illustrated and expected values should be closer together.

<u>Undesirable Consequences</u>

- Despite the best intentions, there is an element of rate regulation involved.
- The development of products that reward persisting policyholders will be limited.
- Standards are different for single life and last-survivor policies.
- It should not be acceptable to reinsure the lapse risk via levelized mortality charges.
- A reasonable inflation rate should be prescribed.
- Companies may be encouraged to purchase less secure investments to get a better yield, and there is no requirement to reflect a cost for the additional risk taken.
- Companies may be encouraged to allocate more expense to unaffected divisions.
- Companies may be encouraged to adjust pricing assumptions to pass the tests.
- Future recovery of DAC tax should be factored in (if it is not currently permitted).

<u>Paperwork Burden</u>

- Some relief is needed for minor assumption changes.
- Record keeping to support in-force illustration requirements for closed blocks of business will become very cumbersome.

Other Regulatory Issues

1. Training agents

Companies' agent training practices vary widely, ranging from training manuals and other written materials to face-to-face training, video and audio tapes, teleconferences, and follow-up bulletins. Many companies, of course, use multiple methods of training. About 60 percent send agents brief sets of instructions. In addition, about the same percent have some fact-to-face training program, and nearly a third provide extensive training manuals.

2. Ways of dealing with conflicting requirements of old regulations

While waiting for regulatory relief, many companies comply with both old and new regulatory requirements even when they are inconsistent or contain outright conflicts. Some companies seek guidance from the state insurance department; some comply with the newer regulation in the case of inconsistency or outright conflict.

3. Areas of ambiguity and state-to-state variations

Ambiguities and state-by-state variations in regulatory requirements occur in the following areas: computer screen illustrations, hardcopy illustration output and delivery, definition of other than as applied for, applicability to corporate sponsored plans, in-force illustrations, in-force illustrations and annual statements on plans not originally illustrated, and annual statements for some term plans with only guaranteed elements in certain years. For actuarial support testing, ambiguities include: definition of policy form, acceptable methods of allocating expenses including corporate overhead, GRET allocations and permitted variations, tax effects, inclusion or exclusion of term riders, variations in voluntary actions by policy owners (e.g., policy loans and premium payment patterns), reflections of reinsurance, and annual compliance reporting (e.g., is the certification for the past year or the upcoming year?).

4. Transferring practice note material into the model regulation

Suggested transfers of information to the model regulation or ASOP No. 24 occur in the following areas: computer screen illustrations, illustration of multiple premium patterns for term insurance, formats for annual compliance communications to states, use of an interest margin versus specified interest rates in testing, testing of indeterminate premium term insurance, two-tier product requirements, application of inflation assumptions (especially to the GRET), and more general inclusion of the Q&A and Practice Notes.

5. Aspects of the illustration regulation applicable to annuities and variable life

Respondents addressed a wide variety of issues when asked to note aspects of the Life Illustration Regulation that *should* be applied to fixed annuity or variable life and annuity illustration regulations. Some expressed concern about a level playing field for annuities versus other financial products and a desire that annuity illustrations be simpler and shorter than the life illustrations. Disclosure concerning fixed annuity first-year bonus interest rates is noted. Disclosure for variable products is generally deemed to be adequate. Some disclosure concerning gimmicks is noted. Some concern about state-by-state variations in regulatory requirements. There was some support for standard illustration formats for each major family of products.

Some support was reported for actuarial standards and self-support tests for fixed annuities and variable products with some (numerically different) GRET's to be made available and the use of a mid-point scale for fixed annuities. However, concerns were expressed about the burden of actuarial support testing and some opposition to actuarial support testing is noted in responses to question 6 below and a desire to focus on disclosure as an alternative to support testing.

6. Aspects not applicable to annuities and variable life

Respondents addressed a wide variety of issues when asked to note aspects of the Life Illustration Regulation that *should not* be applied to fixed annuity or variable life and annuity illustration regulations. Some concern about state-by-state variations in regulatory requirements is noted. A desire was expressed to maintain consistency with current variable product disclosure requirements and maintain the 12 percent interest rate cap. The regulation should not require illustrations, should permit annuity illustrations to be simpler and shorter than life illustrations, and should not require signatures. Concerns were expressed about maintaining a level playing field for annuities versus other financial products. For fixed annuities, the definition of currently payable scale may need to be more flexible; the prevalence of new money products was noted. Some assert that actuarial support testing should not be required for fixed annuities and variable products, instead, focus should be placed on disclosure requirements. A desire to minimize or eliminate the narrative summary requirements was noted.

7. Additional comments on the new regulations and this survey

Concerns were expressed about: burdens on small companies and distributors, state-by-state variations in regulatory requirements, short notice between adoption of a regulation and the effective date, the length of illustrations helping to confuse consumers, the relative riskiness of assets not being reflected in assumed investment yield rates, and difficulty in treating temporary excess expenses as a capital investment for illustration purposes. A practice of filing two nearly identical policy forms, one for illustration and one not-to-be-illustrated, was noted. A desire was expressed for the elimination of actuarial support testing for a product once it reached the end of the twentieth year from issue.

APPENDIX A

SURVEY QUESTIONS AND TABULATION OF RESPONSES

<u>Cover Memorandum to Chief Actuaries</u>

To:	Chief Actuaries
From:	Stephen Rentner, Public Policy Analyst
Re:	Survey of Company Experience Under Life Illustration Regulations
Date:	January 21, 1998

At the request of the National Association of Insurance Commissioners (NAIC), the American Academy of Actuaries is conducting a survey concerning the first year of experience under state life insurance illustration regulations (collectively referred to as "the Regulation") that have been based on the NAIC's model regulation. The Academy will tabulate the survey results by question. The identities of companies and details of specific surveys will be held confidential by the Academy.

This survey is lengthy because the Regulation impacts many aspects of selling life insurance, communicating with policy holders after the sale, and developing new products. We appreciate your patience with this survey's length. The feedback from this survey will potentially:

1. Help improve the Life Illustration Regulation, and
2. Impact the anticipated development of an NAIC Model Fixed Annuity and/or Variable Life and Annuity Regulation.

This survey covers ground within several areas of responsibility for many life insurance companies, which includes responsibilities of illustration actuaries, responsible officers, underwriters, information systems officers, etc.

Given the several areas of responsibility involved, we ask that you or your designee:

1. **Allocate responsibility for specific questions among your colleagues, and**
2. **Provide one coordinated set of responses on behalf of your company.**

All individual company responses and associated material will be kept confidential. Envelopes have been provided for this purpose.

Your cooperation and assistance will be greatly appreciated. The Academy wishes to provide a report of the results of the survey to the NAIC at its March meeting. As a result, we ask that you complete and return the survey by Friday, February 13, 1998.

All surveys should be returned to:
The American Academy of Actuaries
1100 17th Street, NW, Seventh Floor
Washington, DC 20036

Survey Directions

Most questions have a list of answers from which to choose. Also, each question has a comment area, plus there is additional space at the end of the survey for comments.

Please note that the phrase "nonguaranteed elements" as used in this survey includes all items set at the discretion of the company, including policyholder dividends on participating products.

Count	Percent	Survey Question	
		Impact on the Marketing Process	
		1. What percentage of total individual life insurance policies sold that are potentially subject to the regulation are being designated as requiring the use of a sales illustration?	
7	9	a.	Under 25%.
9	11	b.	25% up to 50%.
8	10	c.	50% up to 75%.
56	70	d.	75% and over.
80	100		
		2. For the policies designated as using an illustration, are the agents for your company using computer screen displays **without** a printed illustration to sell the insurance?	
41	53	a.	Under 10% of the sales seem to be based on showing information to consumers on a computer screen.
10	13	b.	Between 10% and up to 25% of sales seem to be based on showing information to consumers on a computer screen.
4	5	c.	Between 25% and up to 50% of sales seem to be based on showing information to consumers on a computer screen.
6	8	d.	50% or more of the sales seem to be based on showing information to consumers on a computer screen.
16	21	e.	No experience to share on this question.
77	100		

Count	Percent	Survey Question	
		-	
		3. Employer Market - Are "generic quotations" for "non term group life" being used in employee meetings?	
1	2	a.	Yes, the company's policy is that everyone gets the same quotation of only one or two ages, policy sizes, and premium pattern examples.
5	8	b.	Yes, the company's policy is that everyone gets a quotation with a number of different ages, policy sizes, and premium patterns.
4	7	c.	Yes, the company's policy is that each individual gets a quotation with a few specific examples for their age and/or salary level.
6	10	d.	Yes quotations are used, but the agent determines what quotations will be provided.
34	56	e.	Other (please explain below)
10	17	f.	No, each employee gets a personalized illustration.
60	100		

4. Direct (non producer-sold) Market - How are illustration requirements being satisfied?

Count	Percent		
15	20	a.	Policies are designated by the company to be sold without an illustration.
0	*	b.	A pre-packaged illustration containing information for a number of sample issue ages is being provided, and none of the other information is based on the individual customer.
2	3	c.	A pre-packaged illustration is used based on the person's issue age and gender, and none of the other information is based on the individual customer.
48	66	d.	No experience in this market.
8	11	e.	Other (please explain below).
73	100		

Agent and Policyholder Signature Requirements (**Please base the responses in this section of the survey on the type of distribution system indicated in the response to the first question.)**

1. Are the responses in this section of the survey based on:

Count	Percent		
77	96	a.	producer-sold business
2	3	b.	directly-marketed other than telemarketed business
1	1	c.	telemarketed business
80	100		

Count	Percent	Survey Question
		-

Count	Percent	Survey Question
		-
		2. For policies designated to be sold with an illustration, what percent of the issued policies need to have an illustration provided to the consumer after the application has been sent to the company. (The agent or company provides an illustration later, including, for example, policies issued other than applied for)?
26	34	a. less than 25%.
15	19	b. % up to 50%.
13	17	c. 50% up to 75%.
23	30	d. 75% or above.
77	100	
		3. For those policies mailed to the customer by the company that contain an illustration, what percent of these customers are sending back a copy with their signatures?
12	20	a. less than 25%.
7	12	b. 25% up to 50%.
8	14	c. 50% up to 75%.
32	54	d. 75% or above.
59	100	
		4. What procedures has the company put in place with respect to the signature requirements? (Please mark all that apply)
24	21	a. The company requires a signed form before the application will be processed.
24	21	b. The company will process the application, but will not issue a policy without a signed form.
28	25	c. The company withholds commissions until a form is signed.
30	27	d. The company issues the policy and completes a "good faith effort" to get a signature from the policyholder, such as including a postage paid return envelope for the policyholder to use.
0	*	e. No experience to share on this item.
7	6	f. Other (please explain below).
113	100	

Count	Percent	Survey Question
		-
		Impact on Consumer Understanding and the Sales Process
		1. Is it your impression, based on your company's experience, that consumers understand their purchases better by receiving illustrations under the Regulation compared to the pre-Regulation illustrations?
8	10	a. No, the old illustrations we used before helped consumers more.
26	31	b. About the same - the old and new illustrations are about the same.
21	26	c. Yes, the new illustrations are helping consumers a little more than the old illustrations.
6	7	d. Yes, the new illustrations are much better than the old illustrations.
16	20	e. No experience to share on this question.
5	6	f. Other (please explain below).
82	100	
		2. Is it your impression that the Regulation has had the following impacts on overall company sales (please mark all that apply):
13	14	a. No experience to share on this question.
2	2	b. Sales are hurt by the Regulation due to lack of consumer understanding of the illustration.
1	1	c. Sales are hurt by the Regulation due to better consumer understanding of the illustration
2	2	d. Sales are helped by the Regulation due to better consumer understanding.
7	7	e. Sales are hurt by the Regulation due to a change in the competitive environment.
7	7	f. Sales are helped by the Regulation due to a change in the competitive environment.
14	15	g. Sales are hurt by the Regulation for other reasons (please list below).
2	2	h. Sales are helped by the Regulation for other reasons (please list below).
48	50	i. The Regulation has not had a major impact on sales.
96	100	
		Impact on Nonguaranteed Elements
		1. For your company, the overall level of illustrated nonguaranteed elements:
49	64	a. Has not been impacted by the Regulation.

Count	Percent	Survey Question
		-
22	29	b. Has become less favorable to the policyholder due to the Regulation.
1	1	c. Has become more favorable to the policyholder due to the Regulation.
5	6	d. No experience to share on this question.
77	100	

Count	Percent	Survey Question
		-
		2. For your company, the level of credited and charged nonguaranteed elements and the level of illustrated nonguaranteed elements are:
68	91	a. The same.
6	8	b. In aggregate effect, the credited and charged NGE's are generally more favorable to the policyholder than those illustrated.
1	1	c. No experience to share on this question.
75	100	

Impact on Product Design

1. For your company, has the impact of the Regulation contributed to or is likely to contribute to modifications in product designs? (Please mark all that apply.)

Count	Percent	
28	17	a. None for any products
6	4	b. Surrender charges
10	6	c. Commissions or charge-backs
13	8	d. Guarantees provided
25	15	e. Credited Interest Rates
17	10	f. Current mortality charges
16	10	g Current expense charges
18	10	h. Any other nonguaranteed elements (including dividends)
3	2	i. Loan program
13	8	k. Other product design features (please list in comment section below)
16	10	l. How a product was illustrated
165	100	

2. Please describe any products or features that <u>did not fit well under the Regulation or the self-support or lapse-support testing</u> (please include the "how's and why's").

A partial list of items to consider is shown below:

Term	Surrender Charges
Indeterminate premium	Loans
Equity Indexed Life	Persistency Bonuses
Whole Life	Group Insurance
Joint - first to die	Joint - last to die
UL	Worksite marketing
Direct marketing	Other
Target Premium	

Count	Percent	Survey Question
		-
		3. Has the 100% persistency assumption in years six and later for the lapse-support test impacted product innovations? (Please identify areas that the lapse test fail to give reasonable results and identify whether the tests were too easy or too hard in the comment section below).
56	77	a. No difficulties were experienced.
2	3	b. Third party administrator costs did not model well under the tests.
2	3	c. Levelized commissions did not model well under the tests.
5	7	d. Reinsurance arrangements did not model well.
7	10	e. Other (please list in comment section).
72	100	

New Sales Illustration Systems

1. What additional costs were experienced to modify or build an illustration system for new sales? "Additional costs" include software, hardware, other information system costs, development and production of written materials video etc., training of producers and distribution management, additional compliance supervision, etc.

Count	Percent		
3	4	a.	None
26	34	b.	up to $100,000.
19	25	c.	$100,000 up to $200,000.
16	21	d.	$200,000 up to $500,000.
12	15	e.	$500,000 up to $1,000,000.
1	1	f.	$1,00,000 up to $2,000,000.
0	*	g.	$2,000,000 or more.
77	100		

2. Under the Regulation, what controls are used on the illustrated scale of nonguaranteed elements(NGE's)?

Count	Percent		
22	27	a.	Only the official NGE's can be illustrated and a new copy of the software is provided to the agent when the scale of NGE's changes.
12	15	b.	Only the official NGE's can be illustrated and a "key" is provided to the agent when changes are made, but a new copy of the software is not needed.
30	36	c.	Software supports agent illustration of any scale of NGE's not more favorable to the policyholder than the official NGE's.
9	11	d.	Software supports agent illustration of any scale of NGE's.
9	11	e.	Other (please explain below).

Count	Percent	Survey Question
		-
82	100	

Count	Percent	Survey Question
		-
		3. What is the average length of the new sales illustration given to consumers?
7	8	a. 5 pages or less.
21	26	b. 6 or 7 pages.
17	21	c. 8 or 9 pages.
23	28	d. 10 or 11 pages.
11	13	e. 12 or more pages.
3	4	f. Not applicable.
82	100	
		4. How many pages longer is the Regulation's format than the format your company used to use?
1	1	a. It is shorter.
2	2	b. It is the same.
6	8	c. It is 1 to 2 pages longer.
31	40	d. It is 3 or 4 pages longer.
34	44	e. It is 5 or more pages longer.
4	5	f. Not applicable (such as no illustrations where used before, etc.).
78	100	
		5. Please describe how Supplemental Illustrations are being used by your company and/or its producers. (Please mark all that apply.)
21	18	a. Used less frequently than before
12	10	b. Used more frequently than before
9	8	c. Used to illustrate the effect of changes in scales of NGE’s
34	29	d. Used to illustrate the effects of voluntary policyholder actions (e.g., partial withdrawals, loans, premium dump-ins, partial withdrawals)
14	12	e. Used to illustrate results when combined with other financial products
26	23	f. Other (please explain, below.)
116	100	

Count	Percent	Survey Question

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In-force Illustration Systems

1. What additional costs were experienced to modify or build an illustration system for in-force business? "Additional costs" include software, hardware, other information system costs, development and production of written materials video etc., training of producers and distribution management, additional compliance supervision, etc.

Count	Percent		
6	9	a.	None
29	42	b.	up to $100,000.
21	31	c.	$100,000 up to $200,000.
8	12	d.	$200,000 up to $500,000.
4	6	e.	$500,000 up to $1,000,000.
0	*	f.	$1,00,000 up to $2,000,000.
0	*	g.	$2,000,000 or more.
68	100		

2. For in-force illustrations that are not part of an annual report, what is the average length of the in-force illustration given to consumers?

Count	Percent		
36	47	a.	5 pages or less.
21	27	b.	6 or 7 pages.
8	11	c.	8 or 9 pages.
4	5	d.	10 or 11 pages.
1	1	e.	12 or more pages.
7	9	f.	Not applicable.
77	100		

Annual Report Systems

1. Are the same annual reports planned to be used for business covered and not covered by the Regulation?

Count	Percent		
7	9	a.	Not applicable, annual reports were not used.
15	19	b.	No, separate formats will be used.
11	14	c.	Yes, the old format will be used for both.
45	58	d.	Yes, a new format will be used for both.
78	100		

Count	Percent	Survey Question

-

2. What additional costs were experienced to modify or build a system for annual reports? "Additional costs" include software, hardware, other information system costs, development and production of written materials video etc., training of producers and distribution management, additional compliance supervision, etc.

Count	Percent		
6	8	a.	None
49	70	b.	up to $100,000.
10	14	c.	$100,000 up to $200,000.
5	7	d.	$200,000 up to $500,000.
0	*	e.	$500,000 up to $1,000,000.
1	1	f.	$1,00,000 up to $2,000,000.
0	*	g.	$2,000,000 or more.
71	100		

Self-support and Lapse-support tests (New Sales and Inforce)

1. What on-going costs to conduct a complete annual Illustration Actuary testing and certification process were incurred? Please exclude the "additional costs" defined as part of Question 2. below.

Count	Percent		
5	7	a.	None
65	85	b.	up to $100,000.
6	8	c.	$100,000 up to $200,000.
0	*	d.	$200,000 up to $500,000.
0	*	e.	$500,000 up to $1,000,000.
0	*	f.	$1,00,000 up to $2,000,000.
0	*	g.	$2,000,000 or more.
76	100		

2. What additional costs were experienced to prepare the company to conduct Illustration Actuary testing leading to certification? "Additional costs" include software, hardware, other information system costs, education and training, and review of new policies and procedures.

Count	Percent		
8	10	a.	None
59	75	b.	up to $100,000.
7	9	c.	$100,000 up to $200,000.
4	5	d.	$200,000 up to $500,000.
1	1	e.	$500,000 up to $1,000,000.
0	*	f.	$1,00,000 up to $2,000,000.
0	*	g.	$2,000,000 or more.
79	100		

Count	Percent	Survey Question
		-
		3. Did the Regulation result in a modification of expense allocations? (Please note that it is assumed any such allocations followed generally accepted expense allocation methodologies).
14	18	a. Yes, it caused a thorough review and updating of expense allocations.
18	23	b. Yes, some refinements were made prior to or during the testing process.
43	55	c. No, no updating was necessary.
3	4	d. Any other situation (please explain below).
78	100	
		4. What expense method was used by your company?
51	63	a. Fully allocated.
24	30	b. The Generally Recognized Expense Table (GRET).
4	5	c. Marginal.
2	2	d. Not applicable.
81	100	
		5. If the GRET was used, were there any implementation problems experienced? If so, please explain.
6	22	a. Yes
21	78	b. No
27	100	
		6. Were modifications made to the investment income allocations? (Please note that it is assumed that any such allocations follow generally recognized allocation methodologies).
1	1	a. Yes, it caused a thorough review and updating of allocations.
12	15	b. Yes, some refinements were made prior to or during the testing process.
64	80	c. No, no updating was necessary.
3	4	d. Any other situation (please explain below).
80	100	
		7. Please identify which of the following alternative payout forms are illustrated (please mark as many as apply):
9	10	a. Extended term.
20	21	b. Reduced paid up.
16	17	c. Annuity payouts.

Count	Percent	Survey Question	
		-	
47	50	d.	None of the above.
2	2	e.	Other (please explain below).
94	100		

Count	Percent	Survey Question
		-
		8. How was testing on riders completed?
47	61	a. Riders were tested on the side as stand alone and the positive accumulated cash flows were <u>not used</u> to help pass the basic insurance coverage.
7	9	b. Riders were calculated on the side and the cash flows were aggregated with the basic insurance coverage cash flows.
19	25	c. Riders were combined from the start and were part of the aggregated cash flows.
4	5	d. Other (please explain below).
77	100	
		9. For your company, was reinsurance incorporated into the testing? (please mark as many as apply):
32	35	a. Reinsurance was not incorporated.
35	37	b. YRT reinsurance was incorporated.
17	18	c. Other types of reinsurance arrangements were incorporated.
5	5	d. New reinsurance arrangements were created and incorporated.
2	2	e. No reinsurance arrangements existed to incorporate.
3	3	f. Other (please explain below).
94	100	
		10. Please list any additional thoughts on how the self-support and lapse-support rules or the related Actuarial Standard of Practice <u>are</u> or <u>are not</u> working:

Other Regulatory Issues

1. In what ways did your company communicate to and train its producers in the requirements of the Regulation? (Please mark all that apply.)

Count	Percent	Survey Question
47	36	a. Sent them a brief set of instructions.
24	19	b. Sent them a more extensive training manual.
2	2	c. Sent them written material and a video tape.
45	35	d. Had some type of face-to-face training program.
11	8	e. Other (Please explain below).
129	100	

2. How has your company handled possibly conflicting requirements in some states between older laws or regulations and the new Regulation?

3. Are there any areas of ambiguity in the Regulation that, in your opinion, need to be clarified?

4. Are there parts of the Q&A and/or the Practice Notes that you believe should be transferred to the Regulation and/or Actuarial Standard of Practice No. 24.?

5. Based on your experience with the Life Illustration Regulation, are there any aspects of the Regulation that you believe should be applied to fixed annuity or variable life and annuity contracts when the NAIC develops a Fixed Annuity Illustration Regulation and Variable Product Regulation?

6. Based on your experience with the Life Illustration Regulation, are there any aspects of the Regulation that you believe should not be applied to fixed annuity or variable life and annuity contracts when the NAIC develops a Fixed Annuity Illustration Regulation and Variable Product Regulation?

7. If you have any additional comments on the Regulation or this survey, please list them below:

Thank you for your comments in this survey.