

NATIONAL CONFERENCE OF INSURANCE LEGISLATORS
LIFE INSURANCE AND FINANCIAL PLANNING COMMITTEE
WASHINGTON, D.C.
MARCH 8, 2013
MINUTES

The National Conference of Insurance Legislators (NCOIL) Life Insurance & Financial Planning Committee met at the Hyatt Regency on Capitol Hill in Washington, D.C., on Friday, March 8, 2013, at 8:15 a.m.

Sen. Mike Hall of West Virginia, chair of the Committee, presided.

Other members of the Committee present were:

Rep. Greg Wren, AL	Sen. Jake Corman, PA
Sen. Travis Holdman, IN	Rep. Marguerite Quinn, PA
Sen. Dan Morrish, LA	Rep. Brian Kennedy, RI
Rep. Pete Lund, MI	Rep. Charles Curtiss, TN
Rep. George Keiser, ND	Rep. Bill Botzow, VT

Other legislators present were:

Sen. William Haine, IL	Sen. Jim Marleau, MI
Rep. Kevin Cotter, MI	Sen. David O'Connell, ND
Rep. Tom Leonard, MI	Sen. Dale Schultz, WI

Also in attendance were:

Susan Nolan, Nolan Associates, NCOIL Executive Director
Candace Thorson, Nolan Associates, NCOIL Deputy Executive Director
Ed Stephenson, Nolan Associates, NCOIL Director of Legislative Affairs–DC
Eric Ewing, Nolan Associates, NCOIL Director of Legislative Affairs

MINUTES

Upon a motion made and seconded, the Committee unanimously approved the minutes of its November 15, 2012, meeting in Point Clear, Alabama.

TAX TREATMENTS FOR LIFE INSURANCE AND ANNUITIES

Walter Welsh of the American Council of Life Insurers (ACLI) reported that tax reform at the federal level can have an impact on state tax codes. Mr. Welsh commented that Congress looks to raise revenue without raising taxes by eliminating income tax expenditures. He said that some states have considered getting ahead of the federal government by eliminating state-allowed expenditures now, pointing to Massachusetts as an example.

Bill Anderson of the National Association of Insurance & Financial Advisors (NAIFA) stated that Oregon is an example of a state that has proposed eliminating existing tax treatments for death benefits and for the “inside buildup” of life insurance and annuities. He commented that states are desperately looking for money. Mr. Anderson stated that 75 million American families depend upon life insurance products for financial security. He noted that the industry pays out \$1.5 billion a day in life insurance and annuities.

Jason Berkowitz of the Insured Retirement Institute (IRI) stated that the IRI survey found that among middle-income baby boomers, 77 percent consider tax deferrals an important criterion when selecting a retirement product. He said 24 percent reported they would be

less likely to save for retirement if those features were reduced or eliminated. He commented that the road to tax reform would be long and difficult and that the industry would appreciate any assistance from NCOIL in protecting tax incentives.

During Committee discussion, Rep. Keiser asked panel members if they supported tax reform. Mr. Welsh responded that the industry supports the idea. Mr. Welsh argued that legislators shouldn't take away items that have been part of the income tax system from the beginning, not just because they are long-standing but because they are "the right way to tax these products."

Rep. Lund asked the panel what rationale—other than revenue—there is for eliminating expenditures. Mr. Welsh said that some federal policymakers feel that a simplified tax code would make things easier for taxpayers.

PRINCIPLES-BASED RESERVING

Commissioner Julie McPeak of Tennessee stated that the National Association of Insurance Commissioners (NAIC) adopted in 2009 by a supermajority a revised Standard Valuation Law (SVL), which allows for principles-based reserving (PBR). She said PBR replaces the current formulaic approach with a method that allows for better alignment of policy reserves with the risks inherent in highly complex products. Commissioner McPeak stated that the improved alignment is expected to reduce redundant reserves for some products and increase reserves for products whose significant risks are not captured by the current methodology.

Commissioner McPeak commented that the Valuation Manual (VM) will support uniformity across states and that even the process of changing valuation and regulation will be more efficient than it is under the current valuation law. She said that once PBR is operative there will be a three-year transition period. Commissioner McPeak said that since adopting the SVL, the NAIC has created an implementation task force to ensure that states and insurers are ready for PBR, including changes in the financial reporting analysis tools, training for regulators, and resources available at the state and NAIC levels.

Nancy Bennett of the American Academy of Actuaries (AAA) reiterated AAA support for the SVL and PBR methodology. She stated that the current approach is static and does not work well for certain products, notably term and universal life. Ms. Bennett stated that PBR will "right-size" reserves in the industry and that as a result some companies will see their reserves increase while others will decrease. Ms. Bennett stated that for term and universal life products, prescribed reserves could drop anywhere from 30 to 50 percent.

Rob Easton, Executive Deputy Superintendent for Insurance in the New York Dept. of Financial Services, commented that this is the wrong time for state legislatures to consider moving forward with PBR. Mr. Easton commented that insurers are under a great deal of stress from a protracted low-interest rate environment that has no foreseeable end. He commented that PBR represented a cession of state regulatory authority to the industry. He stated that reserves will drop, that there is no accompanying consumer benefit, and that there has been no evidence that PBR will result in lower prices. He suggested that legislators who choose to move forward with PBR might consider legislation that would return some of the savings to consumers.

Mr. Easton said that PBR could create pressure on consumer offerings and insurer solvency. He stated that in some states insurers are already "right-sizing" reserves through opaque and complex transactions, but commented that these would not fall away under a PBR

regime because PBR does not go far enough for the industry and does not drop reserves enough. He argued that the very problem PBR is intended to target would not go away even with its passage.

Paul Graham of the American Council of Life Insurers (ACLI) stated that the industry does take economic forecasts into account when calculating reserves under a PBR regime. He stated that the new formula is dynamic and that insurers look at relevant factors every year. He commented that the current formula forces insurers to set reserves at very conservative levels.

Mr. Graham stated that PBR will initially decrease reserves because it will take into account actual premiums that consumers are paying. He pointed out that the SVL gives commissioners specific regulatory powers including, he noted, the authority to engage an independent expert to review a company's assumptions and to charge the cost of the review back to the company. He commented that the commissioners have a lot of flexibility to regulate and that PBR does not give free rein to the industry.

Scott Harrison of the Affordable Life Insurance Alliance (ALIA) noted that PBR is already used in other countries, such as the United Kingdom, Canada, and Australia. He commented that on the liability side, PBR is a forward-looking approach to how companies manage risk and that states already have embraced a forward-looking approach on the capital side. Mr. Harrison said under the current regime, regulators and insurers are forced to figure out appropriate reserves amounts up to 50 years down the road based on the past rather than on the future. He argued that PBR would bring transparency to balance sheets.

Birny Birnbaum of the Center for Economic Justice (CEJ) described the current regulatory regime as more of an accounting system. He argued that states will need to make sure that regulators have the additional resources to handle the new formula. He asked legislators to go to their departments and ask if they have the staff to handle PBR regulation and what kind of reliance they will have on NAIC staff. Mr. Birnbaum commented that if New York and California, the states with the largest resources, questioned the ability of states to regulate PBR then legislators need to review their own state resources. He said that regulators would need to be able to evaluate insurers' hedging programs, which are complicated.

Rep. Keiser asked the panel to explain how captives would be affected by PBR. Commissioner McPeak replied that some insurers are placing reserves in captives in lieu of securitizing them in the public market. She stated that companies have found that reserving can be done more cheaply using a captive. She stated, though, that captives were not originally intended for use this way. She stated that one of the goals of the implementation task force is to move insurers away from captives and other workarounds and toward PBR.

Rep. Keiser asked why captives could not be regulated without a new regulatory regime. Commissioner McPeak commented on a lack of transparency in regard to what is approved through the use of captives in various states. Ms. McPeak assured the Committee that the NAIC is looking at addressing the captive issue now because of the uncertainty over the PBR effective date. Mr. Easton agreed that captives could be addressed without introducing PBR, which he said does not entirely address the issue of captives.

Rep. Botzow asked the panel how PBR would affect the volatility of insurers given the economic conditions of the past few years.

Mr. Easton responded that there is a concern that PBR would make things more volatile, and that the reserve "cushion" would be reduced or even cut in half in a lot of instances. He

claimed that reserves would be reduced by tens of billions of dollars over the course of several years under PBR. He cautioned that reserves may be too high now, but that does not mean we need to move to an entirely new system.

Commissioner McPeak stated that reserves would likely go down under a PBR regime but only for certain term life products, while reserves could go up significantly for the more complicated products. Mr. Harrison added that companies would not want to be able to set their own reserves because it would create tax problems. He stressed that he did not want legislators to walk away with the impression that this would be a “wild west scenario.”

Sen. Hall then asked the panel to comment on the level of expertise that regulators have now in regard to PBR. Commissioner McPeak replied that training is one of the charges of the NAIC implementation task force but that the NAIC is not looking to assume the role of state regulators as primary overseers.

Mr. Easton and Ms. Bennett agreed that there would be implementation issues. Mr. Easton noted that there are a large number of state insurance departments that do not have actuaries with expertise in PBR. He described PBR regulation as labor-intensive due to the need to examine each company individually and said that PBR may require a significant change in resources and expertise. Ms. Bennett argued, however, that legislators cannot assume that the current oversight is working.

STATE ACTIVITY ON NCOIL UNCLAIMED BENEFITS MODEL

Bruce Ferguson of ACLI gave an overview of state progress regarding the NCOIL *Model Unclaimed Life Insurance Benefits Act*. Mr. Ferguson pointed to a few issues that had arisen since introduction in the states, including:

- challenges for smaller companies that have not used the Death Master File (DMF) to look for life insurance beneficiaries
- questions as to how the model’s DMF requirement applies to companies with multiple lines of business.

John Camillo of Kemper Home Service Companies stated that there would be a decision on or before March 31 regarding a lawsuit against retroactive provisions of the unclaimed property law in Kentucky. Mr. Camillo asked legislators to wait until then before making any conclusions about how any particular statute should relate to previous transactions.

ADJOURNMENT

There being no other business, the committee adjourned at 9:30 a.m.