NATIONAL COUNCIL OF INSURANCE LEGISLATORS
LIFE INSURANCE & FINANCIAL PLANNING COMMITTEE
ALEXANDRIA, VIRGINIA
SEPTEMBER 26, 2020
DRAFT MINUTES

The National Council of Insurance Legislators (NCOIL) Life Insurance & Financial Planning Committee met at the Hilton Alexandria Old Town Hotel on Saturday, September 26, 2020 at 10:00 A.M. (EST)

Representative Joe Fischer of Kentucky, NCOIL Secretary, Acting Chair of the Committee, presided.

Other members of the Committee present were (* indicates virtual attendance via Zoom):

Asm. Ken Cooley (CA)*
Rep. Matt Lehman (IN)
Rep. Jim Gooch (KY)
Rep. Bart Rowland (KY)
Rep. Michael Webber (MI)
Asw. Pam Hunter (NY)
Sen. Bob Hackett (OH)
Rep. Carl Anderson (SC)
Rep. Tom Oliverson, M.D. (TX)

Other legislators present were:

Rep. Peggy Mayfield (IN)*
Rep. Dean Schamore (KY)
Sen. Kirk Talbot (LA)
Rep. Kevin Coleman (MI)
Sen. Paul Utke (MN)
Asm. Kevin Cahill (NY)

Also in attendance were:

Commissioner Tom Considine, NCOIL CEO
Will Melofchik, NCOIL General Counsel

QUORUM

Upon a motion made by Rep. Matt Lehman (IN), NCOIL President, and seconded by Sen. Paul Utke (MN) the Committee waived the quorum requirement without objection by way of a voice vote.

MINUTES

Upon a motion made by Asw. Pam Hunter (NY) and seconded by Rep. Lehman, the Committee voted without objection by way of a voice vote to approve the minutes from the Committee's March 6, 2020 meeting.

PRESENTATION ON LIFE INSURANCE SETTLEMENTS

Wes Bissett, representing the Life Insurance Settlements Association (LISA), stated that life settlements provide life insurance policyholders with a way to sell their policies that are no longer needed or wanted and at a value that typically far exceeds what they would receive for a cash surrender. Life settlements are essentially a way to unlock the market value that exists in a life policy and provide an alternative to lapse and surrender. LISA represents that market and

has been in existence for about 25 years. When LISA was first established, life settlements were somewhat of a new concept and regulation of the market was inconsistent. Much has changed in the last quarter century. The industry has matured significantly and it now has a comprehensive regulatory framework in place and a lot of credit for that goes to NCOIL. NCOIL first adopted a life settlement regulatory Model Act in 2000 and updated it in 2004 and 2007. Many of the state laws that exist today are based on that Model or a very similar National Association of Insurance Commissioners (NAIC) proposal. The goal today is to simply educate. Many often come to conferences saying there is no "ask" but this is one of the rare times when that is true.

The goal is to explain what life settlements are, what the market looks like in 2020 and how life settlements can potentially help seniors and provide much needed resources for seniors dealing with retirement, long term care and healthcare needs. Mr. Bissett then introduced his co-presenter, Michael Freedman. Mr. Freedman used to work at Coventry – the largest life settlement provider in the market. He worked there for 12 years and worked extensively on legislation across the country. He is now the CEO and co-founder of Lighthouse Life Solutions, LLC, a life settlement company that operates outside of Philadelphia. He is also an active LISA member and Chairs LISA's public policy council.

Mr. Freedman stated that this is a great opportunity to share with both those who are and are not familiar with life settlements what has gone on in the last several years and what the state of the market is and why it is particularly relevant and timely considering the aging of America and the healthcare crises that we face. A life settlement is simply the sale of an in-force life insurance policy. When that policy is sold, the policy owner receives in many instances a cash payment. The owner can also receive something called a retained death benefit option or some combination of the two.

Most policies are universal life but it can be for whole life and term life and under certain circumstances guaranteed universal life and other types of life insurance. People who sell their policies receive as a matter of law greater than they would get if they surrendered that policy and that policy had a cash surrender value. It has to exceed that or accelerated death benefits that might be available under the policy. But as a matter of practice, the average life settlement pays multiples more – it is a factor of the age and the health of the insured and the policy itself. So, there are a lot of factors but the average based on national studies is greater than four times more than surrendering the policy and as a practical matter, when somebody lapses their policy they get nothing so it is infinitely greater to sell the policy if facing a lapse and there is a value for it.

Mr. Freedman stated that the market is regulated by both having life settlement providers as the buyers of policies be licensed under state laws and by state insurance departments as well as the intermediary life settlement broker who represents the policy owner. The root of the sale of a life insurance policy is the fact that a life insurance policy is a form of property that the Supreme Court recognized over 100 years ago that it should have the same characteristics as ordinary property.

The Supreme Court stated that if you limited who could buy a policy - an asset that you own – and the Court was referring to people who have an insurable interest, then it would be worth less. If you could sell your house only back to the developer; if you could sell your car only back to the car dealership and there was only one buyer in the market, it would be worth less. So, everyone that owns a life insurance policy owns a piece of property that is as valuable an asset that they may own. By way of example, look at a $500,000 life insurance policy. If you lapse

that policy, there is no return back to the policyowner of any value – they get nothing. But if the termination is through a surrender and it is a universal or whole life policy with a cash surrender value, that surrender value is usually low. While it might have grown in prior years, by the time somebody is faced with whether to keep that policy or not, the premiums exceed whatever cash value is in the policy and often times that is the reason for surrendering the policy for whatever is left in the cash surrender value.

A life settlement is a demonstrably more valuable option for somebody who isn't going to keep their life insurance policy faced with a lapse or surrender and they will get on average four times more – in this case, with the $500,000 policy they could get $45,000 versus $7,500 if they surrendered it and $0 if they did nothing. As another brief example, people who are already in need of long term care or have entered long term care, their ability to maintain a life insurance policy is challenged by Medicaid eligibility which is the reality for most people who receive long term care having Medicaid pay for that, and also financial restraints make it hard. So, people who are in long term care or facing it often get rid of their life insurance policies. Selling that policy could generate real resources for somebody who can dedicate those resources towards long term care. As an example, a very average policy of $250,000 for somebody who needed long term care was able to sell their policy for $75,000. That is not going to change their life but it is money that goes towards their care and can help them get into the proper level and type of long term care whether it is nursing home care, assisted living, or skilled nursing. So, it is very good to be able to liquidate an asset rather than having to rely on government benefits all the time.

Mr. Freedman stated that the realty is that very few policies ever pay a death benefit. Based on data from the insurance industry, in 2018 there was $57 billion dollars in death benefits paid on individual life policies but more than $700 billion dollars worth of policies lapsed or surrendered in 2018. 92.5% of all death benefits that were terminated in 2018 were terminated without paying the policyowner anything or very little if there is a cash surrender. Nine times out of ten you are going to outlive your life insurance policy. What we do know based on research data is that seniors who have policies are more likely than the average policyowner to lapse or surrender their policy and that is at a rate of about 75% of term and universal life policies – it is just not affordable to keep the policy. Seniors terminate their policies because of the need for healthcare, specifically long term care, or really just meeting the cost of living in retirement. Most Americans don't have enough savings to cover their entire retirement and they do manage their assets by liquidating them and selling their home and using the equity and a life insurance policy is also capable of being sold and used in that same way.

Regarding the current state of the market, it is important to start with the available and in-force life insurance market. There is roughly $12 trillion dollars of in-force life insurance in the U.S. today of individual life insurance policies. About $700 billion in individual policy face value was lapsed or surrendered in 2018. With regard to life settlement activity, in 2019 there was only 2,800 life settlements done in the U.S. representing about $4.4 billion in death benefits. So, the idea that the life settlement market is a threat to the life insurance industry or to anything really is not really true given those numbers. The market is trending upward primarily because there is a greater focus on smaller face life insurance policies and there is more direct to consumer marketing that is taking place in the life settlement market where people who are in need of resources in retirement are searching the internet or being served ads on social media.

The market is still very much a deep end market as you can see from the 2019 numbers the average transaction for a life settlement at $4 billion dollars in life settlements and 3,000 transactions represents an average of $1.47 million dollars per transaction. Those are people

that have $1.5 million dollars on average so the market is still very much focused on large faced policies because there are still a large number of intermediaries involved – insurance agents and financial advisors versus those who are on their own looking on the internet saying I don't have an agent anymore or a financial advisor so what am I going to do with this life insurance policy. So, the market is starting to change but it is still very much in the large face market.

There is a great deal of regulation in this market as opposed to 15 or 20 years ago. 43 of the 50 states have laws on the books regulating the transaction. The regulations include licensing of providers and brokers. Interestingly and importantly, a life insurance agent can be a settlement broker by notifying the state in which they are licensed and they are transacting, if they have reciprocity of that license, that they are transacting as a broker and by doing so what is imposed on them is a fiduciary duty to represent the policyowner in the sale of that policy. They don't represent the buyer; they don't represent the insurance company – they represent the policyowner and that is very unique under insurance laws and regulations, particularly with life insurance.

There are numerous disclosure requirements throughout the transaction that at the outset tell the policyowner about the risk of selling their policy more generally and alternatives to selling their policy and that as the transaction goes on that the life settlement company advises the policyowner of how much they would get if they surrendered the policy, how much they would get for an accelerated death benefit and all sorts of disclosures. The compensation has to get disclosed if there is an intermediary involved. So, the level of disclosure in the transaction and the level of consumer protections in life settlements overall has really made this one of the hallmarks of insurance and financial services regulation. The result is that according to NAIC data in the past several years there has been one or two transactions that have been reported as a problem and one or two consumer complaints filed with the state insurance department in the past five years. Granted, the number of overall transactions is small but this is a senior financial service that doesn't have allegations of fraud or complaints and as a matter of fact there is virtually no legislation pending in the U.S. today for life settlements which is why there is no "ask" today. The fact is that this is a well regulated transaction and consumers are getting value for their life insurance policies and they are doing so with greater transparency and accountability than we find in any other insurance or financial services transaction. That is regulation that NCOIL led the way on.

Mr. Freedman stated that a number of states have adopted either the NCOIL Life Insurance Consumer Disclosure Model or some variation of it. There are disclosure requirements that when somebody is giving up their life insurance policy, in addition to what they can do once they give up the policy, the NCOIL model says that you have to tell them there are options that allow them to keep the policy if they can find a way to do it or if not then they can sell it or they can choose an accelerated death benefit so NCOIL went even further in establishing strong consumer protections by having the Model that has been adopted by several states.

Most important is the individual life insurance policy owner. Somebody who sells their policy does so for a variety of reasons, most often because they need the money in retirement either for healthcare or just cost of living in retirement and other things. A company led study in the life settlement industry found that most use their proceeds for their long term care and their healthcare – buying long term care insurance or a hybrid policy or to pay for direct healthcare, particularly long term care. Some use it just to supplement their income in retirement and that is often very much needed because we are in a time of a retirement crisis. We now have baby boomers turning 75 and we know there is a need for resources in retirement for seniors. We know specifically that there is a healthcare crisis for seniors and the majority of seniors are

defaulting for long term care and moving on to Medicaid to pay for that long term care. The cost of nursing home care and other healthcare are rising and the out of pocket expenses that are not covered by Medicaid or Medicare can be very expensive and can be as much as $500,000 out of pocket for a couple starting at age 65 so it is very dramatic and here is an asset in a life insurance policy that nine times out of ten will be gotten rid of for little or nothing in the form of a lapse of surrender. That life insurance policy in a folder in a drawer can have as much value as the equity in their own home so the ability for them to know about life settlements and the ability to sell the policy and use the money for whatever they need it for is the same as with any other asset owned and that is going back to the Supreme Court decision from over 100 years ago.

In 2017, the NAIC when looking at innovative ways to finance long term care included life settlements as one way for seniors to help finance their long term care needs and reported along with other options not only the value that policyowners can receive with over four times the cash surrender value but also among all the options that were innovative in the NAIC report, the life settlement option was the only one that the senior didn't have to shell out any money to benefit from to have money for long term care. It wasn't the purchase of a long term care insurance policy or the purchase of a health insurance policy with long term care benefits – it wasn't anything other than selling the policy which didn't cost them a penny and only made them some money. It was good to be included among those options to help seniors pay for long term care.

Mr. Freedman stated that there is a bill pending in Congress that would allow seniors to sell their life insurance policies and take the proceeds from the sale tax free if they were to roll the proceeds into what's called a senior health planning account that would be similar to a health savings account or other flexible spending account (FSAs) where you can defer taxes paid by dedicating the money into that account as long as they are used for qualified medical expenses. If you think about it, every other American and age group is incentivized to invest in healthcare except seniors who are the most expensive group of healthcare recipients in the U.S. So, they don't have any way to invest or plan for or pay for their costs of healthcare in a way that all other Americans can. The bill has bipartisan support and needs further vetting but it is an idea that is consistent with existing public policy at the federal level that allows for people who are dying to sell their policies tax free.

The bill is for people who don't have to be at that stage in life where they are diagnosed as terminally or chronically ill but who can sell their policy but dedicate those resources for long term care and get the tax free benefits of that transaction so it is very consistent with existent public policy. That is a sign that this market is becoming more and more accepted by public policymakers. NCOIL has led the way in this effort to put regulations in place and give the market the structure it needed to the point where now there are potential tax advantages to policy owners that are being considered in Congress on a bi-partisan basis. It is a long journey.

Sen. Bob Hackett (OH) stated that he appreciates all of the work that has been done to put regulations in place and noted that 15-20 years ago there were hundreds of complaints about life settlements in Ohio. Regulation was needed because it was like the Wild West. People needed to realize that the brokers were in between the people buying the policy and the people selling the policy and the commissions made were unbelievably high. There is a principle of follow the money and it was said that there was money there. It was said in Ohio that either the policyowner or investor was going to be disadvantaged until regulations were put in place.

Sen. Hackett stated that one of the problems that the life insurance industry has been experiencing for several years is that when universal life was sold years ago interest rates were

so much higher and these policies are really going to blow up much earlier. Sen. Hackett asked if the life settlement industry is staying away from those policies because they are to expensive to keep in force. Sen. Hackett further stated that a problem is that you cannot really lower the death benefit too much in these policies due to existing regulations.

Mr. Freedman stated that is an interesting question because everything described by Sen. Hackett is why people are dropping their universal life insurance policies at a high rate, especially in older age when their premiums are doubling every year and the cash value is being depleted. Everything described by Sen. Hackett regarding interest rates being historically low is a consumer problem and it is also from a life settlement standpoint an investor in life settlement problem because what carriers are doing to address this in many instances is raising the cost of insurance (COI) which is within the rights of the policy and is contractually provided for but when those COI increases offset the costs inside the policy to the insurer and are passed onto the policyowner that is causing them to terminate their policies it also makes those policies less attractive to the life settlement market. It is a challenge for the life settlement industry in trying to help policyowners get the value if the life insurance company were to raise the premium to recoup their costs over those years and it hurts the consumers by not being able to keep their policy and not being able to sell it.

COVID-19 AND THE INSURANCE INDUSTRY – NOT JUST A P&C ISSUE

Kweilin Ellingrud, Leader of Life and Annuities Practice in North America; Senior Partner at McKinsey & Company, stated that she would like to spend some time discussing the impact of COVID-19 on life insurance and what some of the key trends are in talking to carriers across the country. The presentation will discuss: the impact of COVID-19 on life insurance in terms of broad trends; acceleration in digital and analytics; in such a record low interest rate environment, product innovation and what we can learn from Japan and Germany and elsewhere on capital light product innovation which we are likely to see a lot more of in this market; and in-force actions which we have seen over the years throughout the world but we will probably start to see more in the U.S..

If you index all the way back to the end of 2019 across all industries it is worth noting that insurance in particular has been impacted from an equity markets perspective much more than many other industries. Impacted more than insurance have been the travel and logistics industries as no one is staying at hotels and nobody flying; banking which has equally been hit with low interest rates and likely some of the small business and other failures in the market; and oil and gas which had a record drop in the price of oil globally. Those industries certainly have been hit harder than insurance but insurance overall has been harder than the overall world average and quite a bit harder than technology and pharma which for reasons related to COVID have been doing reasonably well.

There are a number of trends very specific to insurance disruptions that we are seeing. There have been operational disruptions – for the P&C industry there have been questions around what is covered in business interruption – and closer to home in life insurance there have been challenges in reduced appetite for higher value policies certainly in the term life side and for older policyholders. There has been a challenge of in-force blood draws and a highly paper based underwriting and application process. There have also been hundreds of thousands of call center representatives who have went home and we are also seeing much more higher cyber risk exposure than before and a lot more exploration of that area.

There have also been pricing, product and balance sheet challenges that insurers have faced. Low interest rates have been at a level that most carriers have never seen, certainly not in the U.S. P&C carriers have seen a lot fewer miles driven but certainly some back and forth in consumer pressure to give back some of those premiums. In the life insurance space we are seeing a lot more pressure on in force blocks and what to do with them as sources of value and revenue and funding are scarce. There are also broader balance sheet challenges as we see a bit more on the credit migration side and a risk of broader instability in the financial markets linked to some of the variable annuity risk which we have seen over the years but is certainly present here as well. So, there have been a lots of operational and product pricing challenges.

In responding to those challenges there are seven broad trends that we have seen insurers react to or accelerate as they try to address some of those challenges. The first three are digital and analytics, innovate the product portfolio, and make in force management a strategic priority. The others include getting serious on cost as life insurers compared to many other industries like telecom have not really improved their cost structure much and when they do it often doesn't stick. Ms. Ellingrud said she is seeing across the industry a much stronger focus on improving expense ratios overall and trying to make some of that stick not necessarily to take it out and keep the cost structure low forever but to invest in digital and analytics efforts and find some of the growth initiatives that they are looking to have. In terms of exploiting strength, a lot of carriers are looking to M&A not just within insurance as there is certainly a bit of a look at smaller carriers with maybe less capital and comfortable carriers in terms of potential acquisitions at pretty attractive multiples. There is also a look at fintechs where they might have been partnering before but now some of them are struggling on both the revenue and funding side to do as well – there are some opportunistic views in the M&A space as well.

There is also an effort to upgrade talent and shift ways of working. Some of that is inevitable as almost all insurance carrier employees have gone home and are working remotely. This is a window of opportunity for carriers to re-think their operating model and how they work. A real thought of how to work in the future and how life claims will be handled how underwriting will be handled and how we avoid shifting employees from one situation and then shifting them again so we can look where the puck is going and shape some of that strategically in where we want it to go and in parallel shift the ways of working and upgrade talent as needed.

There have been a lot of smaller pilots in terms of re-skilling. Some carriers are taking call center representatives and shifting them over time to do very simple entry level IT training. We have also seen some financial reporting folks being trained to do entry level analytics. Most of those re-skilling efforts are on the pretty small scale so far and making that at scale to the hundreds is what we are starting to see carriers plan for as we shift to new ways of working. Finally, we have seen a pretty steady shift from a number of carriers to shifting to more fee-based earnings. We have seen this in Ameriprise over the decades but others as well and we will likely see the continuation of this as capital heavy products get less attractive in this interest rate environment and fee based earnings become a bit more attractive certainly from the valuation and equity markets valuation perspective but more broadly to balance the portfolio.

With regard to acceleration in digital and analytics, there have been three broad shifts. All life insurance executives that Ms. Ellingurd has spoken to have noted the really rapid acceleration of digital and analytics. Some of them have opted into that and really welcomed it in terms of more straight through processing and more online and automated underwriting. Others have felt like they had to jump into it for lack of any alternatives. By and large, the general consensus is that five or more years of progress has been made in the past six months since COVID started. Some of that is because policyholders who might not have opted in to self serve

capabilities before and would have rather met with their agent in person are now forced into new channels and some of that is consumer and policyholder driven, some of that is agent driven and some of that is just the environment but carriers have been able to take advantage of that to further accelerate some of those shifts when they have wanted to.

The accelerated shift to digital is certainly a big trend and in that context we are seeing a lot more advanced analytics as well to identify needs to better match those needs with agents and to do better accelerated underwriting with less data for example. To support that, we have also seen a shift in technology to more services in the cloud and more efficient technology use overall. McKinsey conducted a survey over the past few months with over 600 different agents in the U.S. and they were asked a number of questions. One was "what has been the biggest challenges working with customers during the COVID-19 pandemic?" Over half of them ranked building initial client relationships remotely as their number one challenge; second was generating leads.

Another question was "what portion of your time do you spend on the following activities in a typical week?" Pre-COVID responses were compared to post-COVID responses and by and large it is about equal with a pretty glaring exception of customers facing sales time. About 25% of time before COVID was spent with customers and now it is only about 16% of the time and you can imagine that is a more digital engagement model as some agents are piloting how to do a dinner conference call with a couple to talk through their financial situation and find their life insurance needs. Some are really liking that as they don't have to pay for dinner anymore and it is easier to get their undivided attention and some are finding the new lead generation easier but the vast majority of agents are finding it quite a bit harder.

Another question was "what can carriers do to best help you through this crisis?" About one in three said they need carriers to really provide more lead generation support and one in five said they need more digital tools and more self-service capabilities. So, there has been a real acceleration in e-signatures as well as better data to underwrite without in-person blood draws.

McKinsey also conducted a broad survey of over 1,000 companies with more than $1 billion in revenue and looked at those that really captured true at-scale value from analytics. Every company these days is doing analytics in some pocket of the organization but only about one in ten companies are truly capturing full at-scale value from analytics. The survey looked at what those companies are doing disproportionately compared to other companies. Those companies are twice as likely to use agile teams and cross-functional collaboration; 2.5 times more likely to have clear decision making rights and accountabilities; 1.5 times more likely to actually refine that as they put that in place more explicitly; 2.5 times more likely to invest deeply in analytics talent, especially in the analytics translator role which can take a business problem and the analytics science behind that and translate the two to speak the same language on both sides and connect those dots; and 4 times more likely to devote more analytics resources and dollars to last mile conversion. What we often find is that companies are creating really effective models especially with machine learning and other advanced analytics capabilities these days and the real difference in those that capture significant value is that last mile translation – how are you making that black box of analytics insights transparent and clear to the agent so that they can act on the next best conversation to have or next best step to take?

In terms of IT backbone and making IT both more flexible and more efficient we are seeing a number of trends – some of the same trends we have seen in terms of being dynamic, transparent and cross functions structure; more agile teams; a really strong backbone with cloud; and a really clear roadmap which applies to IT and equally to agility and analytics. The

companies that have, for example, a clear analytics roadmap on the use cases that are going to drive the most business value and also where replicating those use cases for a different part of the business is going to give us additional impact. Those roadmaps are much more effective than the bottom up method of a thousand flowers bloom and having each different business unit innovate in its own way.

The second area that is thought to really accelerate, especially in the U.S. with low interest rates, is product innovation. A few overall trends have been seen. We have seen carriers, even if you ignore for a moment the low interest rate environment, in periods of high market volatility there is much more market share gain and loss across the industry than typical. Even in a normal interest rate environment, we would expect a lot more market share shifts right now and over the next couple of years than typical. When you add to that a very low interest rate environment carriers are going to be looking hard under every single rock for potential sources of value. As we look globally for examples, Japan has had a low interest rate for decades and Germany for over a decade – they are innovating with capital light projects with fewer guarantees and that is a trend we are going to see deeply in the U.S. market as well. It is thought that lessons in agile product development can apply there thought in product innovation.

What we have seen in Japan is a very interesting separation of value from the 10 year indexed line and the life insurance index. They have been able to maintain and in some cases grow the value within life insurance despite lower bond yields and lower interest rates. The same thing is seen in Germany and Europe more broadly. A lot of that is driven by Allianz in a particular case in Germany but there are broader European trends as well. In the German market in particular, over the course of five years from 2013-2018, there was a really rapid shift to capital light products and unit linked hybrid products with a different type of guarantee and what we would call as a class capital efficient products. Proportionately, the traditional products have lessened their market share. Disability insurance in particular was growing at about 8% per year in the German market. Allianz has been a market leader in Germany for a long time but they have been really innovating in capital light products.

As we back up and look across carriers, 82% of senior leaders believe that product development is a core competency that they need. 25% of them don't really have a defined product development strategy. 12% of them actually thought that they did have a process that produced strong product innovation. So, it is a critical need and there is a gap more broadly and often times you will see carriers lump in product repricing with real de novo innovation so it might take them 6-9 months to reprice a UL policy while digging into underlying client needs and innovating in this new environment is put into the same team and unfortunately often times repricing of the UL policy will crowd out all of the other activity to do full scale de novo innovation and that is the challenge we are seeing in many of these product innovation teams.

The last trend to discuss is in force. Such blocks have been looked at for awhile partially as a potential source of a large reserve release but we have seen in the U.S. much less action than in the UK where there has been a lot of migration of closed blocks. There is typically on average simpler policies in many other markets but in the U.S. there hasn't been as much movement as expected over the last five to ten years on in force management. There are a lot of reasons why and one of them is that nobody typically owns it as much as they own the channel and the business and the growth side of things and the cross functional collaboration required to pull it off can be quite challenging. There is also a risk of backlash from customers so while many are closed blocks where you are not actively selling those policies, if they feel they are dealing with a different company that could be a frustrating customer policyholder experience. There is a lot to sort through and it can be highly technical so it is not necessarily

the first thing carriers want to do dive into and terms and conditions can be set 50 years ago when the policies were first sold on that block so there are some really legal and other constraints that are important to keep in mind.

As we look at this, there are three broad buckets of levers that we have seen some cutting edge carries use as they look at in force management. The first would be transactional levers – do I want to change my reinsurance on this block? Do I want to sell this set of closed blocks completely? Above and beyond the deal value that you might get on a transactional lever, technical levels are an additional 20% of value and operational levers can actually be another 30-40% of that value. Technical levers would be things like capital and tax management, reinsurance optimization, hedging, and better pricing. Operational levers would be expensive optimization, understanding the full life cycle of those customers, outsourcing certain pockets, data driven claims management, segmented service models and optimizing commissions. Overall, that can collectively add another 40-50% on the overall transaction lever. Typically, you would do this block by block as you look across the in force management blocks you are looking to optimize.

Ms. Ellingrud then discussed a map that some carriers have used to determine where they want to shift each block. On the X axis, operationally, you have keep as-is in the middle and options include wanting to insource more of the work and do it more yourself or outsource it. On the Y axis there is your balance sheet exposure and the appetite from a balance sheet perspective. Keeping as-is would be more of a operational light owner but you could also increase balance sheet exposure as a consolidation consortium for example or you could reduce it if you wanted to fully exit or insource and be more of a broad service provider. So, there are different actions or movements to take and you wouldn't have to do it across the entire portfolio – you could choose block by block and depending on the runoff, capital usage and profile of the block different decisions could be made.

Sen. Hackett stated that Mr. Freedman spoke about the in force business of universal life and the ability now that some Commissioners are taking to allow increases in COI. Sen. Hackett asked Ms. Ellingurd her thoughts on that. Ms. Ellingrud stated that she would separate the in force and often times closed blocks that are no longer being sold with how you are pricing new insurance and new business. Across the new business continuum there is term insurance on the one side and permanent insurance of which universal life and whole life and variable universal life are all different types of it. If you want the most cost competitive coverage, term insurance is certainly the way to go. Many are actually selling that at a below profit level. Life insurance as a whole really is not making much money at all and in fact it barely makes its cost of capital from year to year. So if you step back from the industry, overall pricing is about as low as it can go on some of those products. On universal life that may not be the case but on other product categories term life is a highly transparent and cost competitive market.

Sen. Hackett asked if that is the result of historically low interest rates. Ms. Ellingrud replied yes and stated it is a real challenge. As you look at life insurers contrasted with P&C insurers, they are holding policies on books for decades and they have to make that guarantee over that long period of time but if 10 years treasuries are at record lows you don't have the ability to do that and so where do you look for a lower risk return? It is a real challenge and that is why many carriers now are looking to lower capital usage products as discussed earlier and looking to cut costs wherever they can whether that is better managing in force books or selling closed books or reducing costs structure overall but it is a really challenging time as you look ahead with low interest rates and a lot of long duration commitments to policyholders. Interestingly, it is a challenging time during what was already a challenging industry. Even if you rewind a couple of

years, the long term profitability over the cost of capital in life insurance was already about 0-1% and now you add to that really low interest rates and it is even more challenging so it is a particularly tough time for life carriers.

Rep. Fischer asked if an example could be provided of the movement from capital inefficient products to capital efficient products. Ms. Ellingurd stated that capital heavy products are traditional life insurance products with a guarantee where you have to keep a lot of that capital to be able to pay out the death benefit whenever that might happen. Term life, whole life, and universal life are all examples of capital heavy products. A capital light product would be some of the products for example in Japan – very targeted insurance like cancer insurance and pet insurance. There are other policies that are capital light and also there has been a broader shift towards fee-based products. More on the wealth and investment side you start to see a lot of fee-based revenue there and there you don't have to hold any capital against somebody's investment portfolio and that is very capital light and capital efficient.

ADJOURNMENT

Upon a Motion made by Asm. Cooley and seconded by Rep. Lehman, the Committee adjourned at 11:00 a.m.