

NATIONAL CONFERENCE OF INSURANCE LEGISLATORS
LIFE INSURANCE AND FINANCIAL PLANNING COMMITTEE
INDIANAPOLIS, INDIANA
JULY 17, 2015
DRAFT MINUTES

The National Conference of Insurance Legislators (NCOIL) Life Insurance and Financial Planning Committee met at the Hilton Indianapolis Hotel and Suites in Indianapolis, Indiana, on Friday, July 17, 2015, at 1:30 p.m.

Sen. David O'Connell of North Dakota, Acting Chair of the Committee, presided.

Other members of the Committee present were:

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| Sen. Travis Holdman, IN | Sen. Kevin Bacon, OH |
| Rep. Ron Crimm, KY | Rep. Heather Bishoff, OH |
| Rep. Joe Fischer, KY | Rep. Bob Hackett, OH |
| Rep. Tommy Thompson, KY | Rep. Brian Kennedy, RI |
| Rep. George Kesier, ND | Rep. Bill Botzow, VT |
| Sen. Jerry Klein, ND | |

Other legislators present were:

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| Rep. Deborah Ferguson, AR | Rep. Joe Atkins, MN |
| Rep. Jeff Greer, KY | Rep. Michael Stinziano, OH |
| Rep. Bart Rowland, KY | Sen. John Sparks, OK |
| Sen. Dan "Blade" Morrish, LA | Rep. Mark Pody, TN |
| Rep. Tom Leonard, MI | Sen. Larry Taylor, TX |
| Rep. Lana Theis, MI | Rep. Carlos Tobon, RI |
| Rep. Hank Vaupel, MI | Rep. Kathie Keenan, VT |
| Rep. Michael Webber, MI | Sen. Daniel Hall, WV |

Also in attendance were:

Susan Nolan, Nolan Associates, NCOIL Executive Director
Candace Thorson, Nolan Associates, NCOIL Deputy Executive Director
Molly Dillman, Nolan Associates, NCOIL Director of Legislative Affairs
Andrew Williamson, Nolan Associates, NCOIL Director of Legislative Affairs

MINUTES

Upon a motion made and seconded, the Committee unanimously approved the minutes of its February 28, 2015, meeting in Charleston, South Carolina.

CAPTIVE INSURANCE ISSUES

Commissioner Sharon Clark (KY), Vice President of the NAIC, provided background information on captive insurance issues, explaining that recent attention has been on triple XXX captives and AXXX captives. She said the problem is that captive companies and captive reinsurance companies are operating under a different set of criteria than traditional life insurance companies. She noted that these captive companies are not subject to the same financial solvency laws and regulations as traditional life insurance companies and that this creates an uneven playing field for insurers.

Commissioner Clark stated that the NAIC has developed short-term and long-term responses to captives. She explained that the short-term solution is called AG 48, which refers to an actuarial guideline under which the ceding insurance company in order to create a captive has a responsibility to issue a qualified actuarial opinion on why the regulatory framework guidelines are not needed. She said this short-term solution has been successful thus far.

Commissioner Clark reported that the NAIC long-term solution to captives included principle-based reserving (PBR), which would take effect when states meet the threshold for adoption. She said that PRB would remove the incentive to create captives. She said that the NAIC is also looking into revamping the reinsurance model regulation to incorporate AG 48 requirements and is considering changes to the current financial accreditation requirements. Commissioner Clark acknowledged the difficulty posed by the fact that different states have different regulatory authority. She reported that the NAIC has been addressing this issue for several years, and she noted that captives have caught the attention of Congress and the Internal Revenue Service (IRS).

In response to a question from Rep. Keiser, Commissioner Clark explained the process that will take place for Humana and Aetna to merge. She reported, among other things, that many states require a public hearing and other states may elect to do so. She said states will conduct a detailed analysis to ensure against product monopolies and that some states will analyze the possibility of monopolies within an area of the state. She said that merging the insurers is a very detailed process and that either the Department of Justice (DOJ) or the Federal Trade Commission (FTC) will provide oversight.

Paul Graham of the American Council of Life Insurers (ACLI) reported on captive activity from the industry's perspective. He stated that the industry has been working with the NAIC to develop standards for captives and is working on a framework to address some of the issues associated with captives. He said that captives are not going away nor are they necessarily a bad thing. He noted that the solution to the issues associated with captives is to ensure that standards are the same for captive insurance companies as they are for traditional insurance companies.

Mr. Graham said another captive issue the industry and NAIC have been addressing is variable annuity captives. He reported that the NAIC created a Variable Annuities Issues (E) Working Group charged with studying the issues involved with selling annuity guarantees and with examining why captives are frequently used by companies selling these products. He noted that these products do not use XXX and AXXX reserves. He said that variable annuities have more to do with accounting treatment of hedged assets, which can create volatility at insurance companies. He stated that the industry is addressing these issues with the NAIC through an open, transparent, and uniform process.

In response to a question from Rep. Keiser, Mr. Graham said the way that captives have historically worked is that the originating company would cede its entire risk to a captive and reduce its liability by the full amount while the captive was divided into half, having an equal amount of hard and soft assets. He said the new framework looks to a PBR calculation, which reduces the amount of hard assets the insurer needs and the amount of soft assets it can use.

UNCLAIMED BENEFITS DEVELOPMENTS

Commissioner James Donelon (LA), on behalf of the NAIC, reported on developments regarding NAIC unclaimed benefits activity. He said a Life Insurance and Annuities Claims Settlement Practices (D) Task Force, or the “lead states,” as he said they are often referred to, continues to actively coordinate investigations of current and past use of the Social Security Death Master File (DMF) or a similar database used by annuity companies and life insurers.

Commissioner Donelon stated that regulators used these multistate examinations to identify any asymmetrical or inappropriate use of the DMF or similar databases and to offer reforms when needed. He reported that the “lead states” have concluded multistate examinations with 17 of the largest life insurance companies that represent 64.4 percent of the national marketplace and have found that all the insurers have used the DMF appropriately. He noted that Mass Mutual and USAA, both of which were included in that group of the 17 largest insurers, used the DMF in a symmetric manner.

Commissioner Donelon said that inquiries were not based on a duty to access the DMF and noted that the courts have consistently held that no such duty exists. He said that only when a company accessed the DMF and then used the information to stop annuity payments have regulators sought to require the insurer to use this knowledge regarding life insurance as well. He said that the “lead states” have not sought to compel any company that has not already used the DMF to do so, nor have they criticized companies that chose not to use the DMF.

Commissioner Donelon stated that the NAIC had not taken a position or recommended corrective action regarding companies that have never used the DMF or similar databases. He reported that last year an NAIC Life Insurance and Annuities (A) Committee established an Unclaimed Life Insurance Benefits Working Group, which was charged with offering recommendations for the consistent handling of unclaimed death benefits. He reported that last fall this newly created Working Group recommended to the NAIC Life Insurance and Annuities (A) Committee that NAIC develop a model law. He stated that the Committee subsequently adopted the Working Group’s request.

Commissioner Donelon said that the Working Group had begun the process of developing the new NAIC model law and recently decided to do so by using a section-by-section approach with a comparison chart of the provisions in the “lead states” model and in the NCOIL *Unclaimed Life Insurance Benefits Model Act*. He noted that while states, industry, and consumer representatives have different views on how to most effectively approach this issue, the NAIC is committed to exploring different avenues in an open and transparent manner.

In response to a question from Sen. O’Connell, Commissioner Donelon said that “fuzzy matches” and retrospective requirements are the most contentious issues.

In response to a question from Rep. Kennedy, Commissioner Donelon said it is the responsibility of the NAIC to set standards and, while he personally commends NCOIL for having such a long-standing model, the NAIC feels a need to create its own.

In response to a question from Rep. Botzow, Commissioner Donelon said the focus of the NAIC Working Group is on insurance claims, whereas state treasuries handle unclaimed property.

John Gerni of the American Council of Life Insurers (ACLI) provided background information on the NCOIL *Unclaimed Life Insurance Benefits Model Act*. He stated that NCOIL passed this model law in 2011 and has continued to update it, most recently at the NCOIL Annual Meeting in the Fall of 2014. He said the model requires life insurers to utilize a DMF periodically to find beneficiaries. He reported that 18 states have adopted some variation of the NCOIL model and that of those 18 states, ten (10) of them have been retroactive and eight (8) prospective. Mr. Gerni noted that in Kentucky, a court had ruled the retroactive language unconstitutional, so until the conclusion of the appeals process, Kentucky is considered to be a prospective state.

Mr. Gerni stated that when a legislator introduces an NCOIL-based bill, the ACLI will work with the legislator regarding potential amendments and that these amendments largely deal with two things. He said the first are “fuzzy match” requirements, which the ACLI originally supported. He said the second issue is whether the DMF should be used in a prospective or retrospective manner. He advised that the ACLI does not favor a position either way and advises that this is best left to the will of individual states.

Mr. Gerni noted that as the NAIC began the review process of various models, it largely deferred to the NCOIL language. He noted that the Uniform Law Commission (ULC) was in the process of updating its unclaimed property model for the first time since 1995. He said that while the ULC had incorporated the NCOIL model into the first reading of its draft, it had incorporated these provisions into the unclaimed property code as opposed to the life insurance code, as was the original intent. He reported that of the 18 states that have adopted the NCOIL model, 17 adopted it under their state’s life insurance code, and Vermont was the only state to apply it to its unclaimed property code.

Mr. Gerni reported that the ULC has received written requests by ten (10) state insurance commissioners emphasizing that they are responsible for insurance regulation and not the ULC. He said that the ULC has responded to these concerns by agreeing to meet with interested parties, including the ACLI. He said this will be the start of several meetings between now and the ULC Annual Meeting in the Summer of 2016.

Rep. Keiser commented that Mr. Gerni raised an important issue and reinforced the NCOIL model’s commitment to addressing unclaimed benefits through insurance law. He said that unclaimed property belongs to different departments in various states and that in North Dakota, for example, it is housed under the Treasury Department. He encouraged states that are in the process of examining unclaimed property legislation to review all other codes outside of insurance to ensure they are consistent with the intent of the legislation.

PRINCIPLE-BASED RESERVING (PBR) ACTIVITY

Commissioner Clark, on behalf of the NAIC, provided background on PBR and noted that it was first proposed in 2009. She defined PBR as a new method discussed as a substitute to the current formulaic approach to determining policy reserves. She said that current life insurance products on the market are complex and reserving requirements are much different than they were 20 years ago and that PBR is an attempt to adapt to such changes.

Commissioner Clark reported on the most recent changes regarding PBR. She said that in 2015 the NAIC included a small-company exemption in response to concerns from smaller companies. She reported that 31 states have enacted PBR legislation and that the requirement is 42 states

representing 75 percent of the total U.S. premium. She advised that eight other states have introduced PBR and said the NAIC is hopeful that the legislation will pass in this year's session. She said that with the passage of PBR in those states, the NAIC anticipates that it will meet the 42 states/75 percent threshold in 2017. She said that after states meet that threshold, PBR will be phased-in over three years.

Commissioner Clark said the NAIC is working to assist states in the transition to PBR and acknowledged that it is a new type of financial analysis. She said the NAIC is developing a regulatory review system to foster the consistent implementation of PBR. She reported that the NAIC has hired three life actuaries to help establish the review process for the states and also plans to provide training for companies.

In response to a question from Rep. Keiser, Commissioner Clark said the NAIC continues to discuss the fact that due to cost and/or lack of personnel, some states will have difficulty implementing PBR. She said the NAIC is trying to bring those capabilities to those states that need them.

Mr. Graham of ACLI reported that the NAIC is working on developing tools to help states understand the content of reserves so that the necessary level of expertise will be available when PBR is implemented. He said that 36 states have adopted PBR if you include states where the bill has passed in the House and Senate but the Governor has not yet signed it. He stated that it appears PBR will become official on January 1, 2017, followed by a three-year phase-in that will allow companies to choose the products for which they want to use PBR.

Mr. Graham reported that the industry is currently working with the federal government, specifically the U.S. Treasury and Internal Revenue Service (IRS), to understand how PBR will be taxed. He noted that the current U.S. Tax Code mentions the NAIC method as a basis for taxing reserves. He noted that a second issue involves the definition of life insurance, as the current definition uses reasonable mortality tables while with PBR, new mortality tables will be needed.

Nancy Bennett of the American Academy of Actuaries (AAA) reported on the Academy's PBR activity. She said the Academy has been helping with implementation, including providing information as to what insurers will need to report. She said that in addition the Academy has been working with the NAIC and a centralized group of actuaries to help them develop a toolkit for insurance departments that may not have the capability to handle PBR on their own. She said the Academy is examining the PBR requirements and basic reserve framework. She said that it next will focus attention on capital requirements and how to integrate them into the framework. She reported that the Academy also met with the Office of Financial Research, which is part of the Treasury, to aid its understanding of PBR.

Governor Jim Hodges of the National Alliance of Life Companies (NALC) stated that NALC represents small life insurers across the country and expressed concern that PBR might represent considerable cost with little benefit for smaller companies. He said that over time NALC has agreed to the small-company exemption and now has concern regarding recent conversations about revisiting the exemption. He said that NALC has met with ACLI and has encouraged states that have yet to adopt PBR legislation to include the small-company exemption language in the bill.

ADJOURNMENT

There being no further business, the Committee adjourned at 2:30 p.m.

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