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National Council of Insurance Legislators (NCOIL)

Resolution Identifying Certain Enhanced Cash Surrender Value Endorsements As Violating The Standard Nonforfeiture Law

**Adopted by the NCOIL Life Insurance & Financial Planning Committee on July 15, 2022 and the NCOIL Executive Committee on July 16, 2022.*

**Sponsored by Sen. Travis Holdman (IN); Co-sponsored by Rep. Tom Oliverson, M.D. (TX) – NCOIL Treasurer*

WHEREAS, the Standard Nonforfeiture Law for Life Insurance, based on National Association of Insurance Commissioners (NAIC) Model #808, is a pillar of United States insurance regulation; and

WHEREAS, State legislators have agreed with the public policy in the Standard Nonforfeiture Law and adopted it across the board, a rare example of uniformity not resulting from Federal mandate or NAIC accreditation standards; and

WHEREAS, the Model has been amended from time to time, including a major set of changes in 1980, labeled “extensive and dramatic” by the regulatory actuaries who drafted and recommended them¹; and

WHEREAS, before these amendments, the Standard Nonforfeiture Law required minimum surrender values and methods of calculating them, and the “extensive and dramatic changes” included the imposition of a separate “smoothness” requirement in a new Section 8 titled “Consistency of Progression of Cash Surrender Values with Increasing Policy Duration”; and

WHEREAS, the regulatory actuaries who drafted this new “smoothness” requirement plainly stated that its “underlying purpose is to require a reasonably orderly sequence of increases,” and to correct a prior defect that allowed “sharp increases”; and

WHEREAS, the Society of Actuaries, whose members had to comply with the significant new requirement, described the new “smoothness” requirement as prohibiting “erratic cash values,” “sharp jumps” and “spikes in the nonforfeiture structure,” and making illegal cash surrender “benefits discontinuous in nature...available only during certain windows of time”²; and

¹ 1981 NAIC Proc. Vol. II p. 837

² SOA Record, 1983 Vol. 9 p. 2004; SOA Record 1996 Vol. 22, No. 1, p. 5-6; 1996 NAIC Proc. 1Q p. 888.

WHEREAS, in the last few years, no more than three life insurers, and only one as a regular business practice, have begun offering “enhanced cash surrender value endorsements,” dramatically changing the terms of well-seasoned policies from their issued and approved policy forms, seeking to incentivize consumers to terminate policies and their death benefit protection by means of limited time, enormous increases in cash surrender value, in plain violation of the Standard Nonforfeiture Law standards described above; and

WHEREAS, these endorsements were submitted by companies who self-certified compliance with the insurance code and its Standard Nonforfeiture Law and generally approved by regulators without any evidence of consideration of the Standard Nonforfeiture Law smoothness requirement; and

WHEREAS, in nearly three years of discussion, including more than six months with NCOIL’s active involvement, neither regulators nor the insurers have proffered a plausible explanation of these products’ compliance with the Standard Nonforfeiture Law; and

WHEREAS, these enhanced cash surrender value offers trigger the exact consumer protection concerns identified by regulatory actuaries at NAIC in developing the Standard Nonforfeiture Law smoothness requirement (a consumer who surrenders her contract based on the terms of the issued policy, and its annual statements and illustrations, which never contemplated limited time, spiked offers, ends up receiving a fraction of the benefit for the same premium payments as a similar risk who surrenders a day later after receiving an enhanced cash surrender value offer); and

WHEREAS, arguments have been offered in favor of “enhanced cash surrender value” products, but said arguments pertain to a wholly different product—never asserted to be in violation of the insurance code and thus not objectionable to NCOIL—with the same “enhanced cash surrender value” name, which is a common rider offered at policy issuance, consisting of not a limited time, spiked offer to terminate the policy, but is instead a product designed to support the persistence, rather than the termination, of corporate owned policies due to the tax benefits of treating the surrender value as an asset; and

WHEREAS, limited time, spiked cash surrender value offers carry substantial risks of the same sort as the regulated product they mimic, life settlements, and the carriers who offer them do not follow the consumer protection statutes created by legislators to protect policyholders offered limited time, big cash incentives to give up their policies, such as rescission rights, intermediary fiduciary duty, physician certification of (elderly) consumer competence, and disclosure of competing alternatives; and

WHEREAS, elected legislators perform an essential oversight function over executive branch regulators in ensuring that the laws they pass are enforced as intended, a particularly important function here, where regulators asked legislators to pass “extensive and dramatic” new requirements, and where the licensed entities’ conduct is in blatant violation of the plain language descriptions of the law provided by its regulatory drafters and the actuaries who implemented the law at insurers; and

WHEREAS, State Constitutions definitively vest lawmaking authority in legislators, who by legislation authorize the creation of departments of insurance to serve as statutory regulators, whose authority is limited to the execution of the public policy established by the legislative branch; and

WHEREAS, abdication of enforcement of a central consumer protection law amounts to regulatory nullification of and rewriting of the insurance code and the displacement of the legislative branch's sole lawmaking authority by the executive branch; and

WHEREAS, NOW, THEREFORE, BE IT RESOLVED, that NCOIL, now calls upon state regulators to enforce the same Standard Nonforfeiture Law smoothness requirement that regulators requested legislators to add to the insurance codes, by withholding approval of, and rescinding any previous approval of, any non-compliant "enhanced cash surrender value" endorsements providing limited time, spiked cash surrender value offers incentivizing consumers to terminate their life insurance protection, and calls upon state legislative committees with oversight of insurance to monitor insurance departments' actions with respect to this matter; and

WHEREAS, BE IT FINALLY RESOLVED THAT, that a copy of this Resolution shall be distributed to the American Council of Life Insurers (ACLI); each State's Insurance Commissioner; the National Association of Insurance Commissioners (NAIC); and the Chairs of the Committees of insurance jurisdiction in each Legislative Chamber of each State.