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LATF 2015 Fall Meeting

Report of the Nonforfeiture Modernization Work Group

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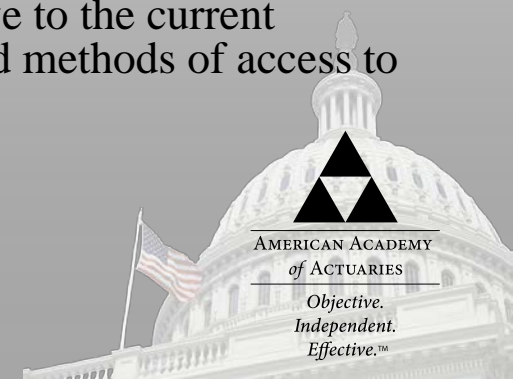
HIGHLIGHTS OF PROPOSED GROSS PREMIUM NONFORFEITURE METHOD (GPNM)

- Under the GPNM Framework:
 - Nonforfeiture (NF) benefits at any time would reflect the funded portion of the risks assumed by the company under the policy with the value of such benefits, where appropriate, determined using actual policy gross premiums paid
 - GPNM is essentially a retrospective approach, however additional elements may be included as needed to support features of some products
 - NF assumptions would be guaranteed, and established such that guaranteed benefits are supported by gross premiums
 - NF law and regulations would provide specific guidance with respect to the NF methodology and general guidance with respect to the establishment of NF assumptions, including “guardrails” on NF factors based on such assumptions
 - The required NF methodology would be consistent for both life insurance and annuity products



HIGHLIGHTS OF PROPOSED GROSS PREMIUM NONFORFEITURE METHOD (GPNM)(Cont'd)

- Under the GPNM Framework:
 - The determination of non-guaranteed elements (including dividends) would not be regulated by NF mandates; however once credited or charged, such amounts would be included in the determination of any required NF benefits
 - NF requirements would incorporate a purposeful and well defined approach to the collection of NF assumption related data by a statistical agency, to monitor results at industry level and indicate any need for adjustments to guardrails
 - Appropriate, timely, and relevant NF basis information would be provided to regulators with product filings to facilitate oversight of the NF methodology at company level
 - In conjunction with revised NF laws and regulations and relative to the current situation, enhanced NF basis and determination information and methods of access to that information would be made available to consumers



ADDITIONAL GPNM CONSIDERATIONS

- Adoption of GPNM may result in the need for product modifications for some existing products to comply with NF requirements (for new business), or exemptions/allowances for those or other existing products to remain available (some product impacts are described below)
- A NF benefit would be made available whenever the amount of prefunding is positive, subject to public policy and regulatory considerations
- The presence of a NF benefit does not imply that a cash surrender value needs to be provided, as providing a cash surrender value is primarily a public policy consideration.
- Any cash surrender value that is provided would be actuarially related to, but not necessarily equal to, the value of the NF benefit



TERMINOLOGY GUIDE

- SNFL – Standard Nonforfeiture Law (current NF requirements)
 - Refers to Life or Annuity as applicable
- SNFL Value – Amount used to determine NF benefits under current NF requirements
- GPNM – Gross Premium Nonforfeiture Method
 - General NF method under consideration
- GNFB – Guaranteed Nonforfeiture Basis
 - Basis of NF factors under GPNM
- RPNA – Required Policy Nonforfeiture Account
 - If applicable, used to determine the amount of NF benefits available under GPNM
 - Analogous to SNFL Value



APPLICATION OF THE GPNM APPROACH TO SELECTED PRODUCTS

- Level Premium Term / Term-Like Products
- Accumulation Universal Life
- Universal Life with Secondary Guarantees
- Traditional Whole Life
- Fixed Deferred Annuity
- Annuity with Guaranteed Living Benefits



LEVEL PREMIUM TERM / TERM-LIKE PRODUCTS

- Level Premium Term products (with Level Death Benefits) are not generally offered in the current marketplace on term insurance policy forms
- Term-Like products are typically structured as Whole Life, with guaranteed premiums increasing after the “term” period ends
- Premiums after the term period are set at a very high level
- Current NF formulas produce no SNFL Values for Term-Like products because of the guaranteed premium payment pattern
- Under GPNM, recognition of prefunding would result in NF benefits during (prior to the end of) the term period
- Including such NF benefits could increase premium rates to consumers during the level premium period



TERM LIFE EXAMPLE - SNFL

- Term-Like WL policy
 - Coverage: 30-year Level Premium Level Death Benefit Term
 - Insured: Male, Age 35, Standard Non-tobacco
 - Premium: \$2.19 per 1000 (for 30 years ; ART thereafter)

- SNFL Assumptions
 - Interest 4.50%
 - Mortality 100% of 2001 CSO Ultimate, Male Non-Smoker ALB

- SNFL Value Components
 - Net Level Premium = \$8.78
 - Expense Allowance = \$20.97
 - Adjusted Premium = \$1.70

- No required non-forfeiture benefits (SNFL Value <0 at all durations)



TERM LIFE EXAMPLE - GPNM

- Term-Like WL policy
 - Coverage: 30-year Level Premium Level Death Benefit Term
 - Insured: Male, Age 35, Standard Non-tobacco
 - Premium: \$2.19 per 1000 (for 30 years ; ART thereafter)
- GPNM Assumptions (GNFB Factors)
 - Interest 4.50%
 - Mortality (Table rate x Factor)
 - Table: 2001 CSO Ultimate, Male Non-Smoker ALB
 - Factors: (50% years 1-30, 150% years 31+)
 - Expenses
 - % of Premium: 87% in year 1, 7% in years 2+
 - Per \$1000: \$1.15 in year 1, \$0.15 in years 2+
- NF Benefit is Extended Term Insurance (ETI) in this example

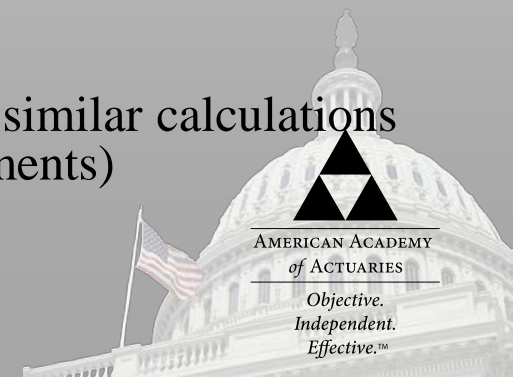


TERM LIFE EXAMPLE – GPNM

Year	Premium	Expense	Mortality	Interest	RPNA	Years of ETI Available
1	2.19	(3.06)	(0.54)	(0.06)	(1.46)	0
2	2.19	(0.30)	(0.56)	(0.01)	(0.14)	0
5	2.19	(0.30)	(0.67)	0.17	3.96	4
10	2.19	(0.30)	(1.05)	0.46	10.79	7
15	2.19	(0.30)	(1.51)	0.72	16.64	7
20	2.19	(0.30)	(2.43)	0.87	20.28	6
25	2.19	(0.30)	(4.00)	0.74	17.08	3
30	2.19	(0.30)	(7.03)	0.00	0.00	0

ACCUMULATION UNIVERSAL LIFE (UL)

- Current NF requirements for flexible premium UL are based on a retrospective accumulation of premiums paid, less withdrawals and charges for benefits and expenses, plus interest, and less any unamortized unused expense allowances
- Result of this calculation is the Minimum Cash Surrender Value (MCSV), which is the SNFL Value
- For typical UL products, a policy will remain in force, with available NF benefits, as long as the cash surrender value is positive i.e., the default NF option is extended term insurance (ETI)
- Minimum NF benefits under current NF requirements are such that the present value of the NF benefits is at least equal to the MCSV on the date elected
- Under GPNM, determination of NF benefits would involve similar calculations as those used for SNFL Values (to meet current NF requirements)



ACCUMULATION UNIVERSAL LIFE (UL) EXAMPLE

■ Universal Life Policy

- Coverage: Universal Life, Level Death Benefit = \$50,000
- Insured: Male, Age 65, Standard Non-tobacco
- Premium: \$57.07 per 1000 (annualized, paid monthly)
 - Level premium amount needed to mature the policy on the guaranteed basis

■ SNFL and GPNM Assumptions (GNFB Factors)

- Interest 3.00%
- Mortality (Table rate x Factor)
 - Table: 2001 CSO Ultimate, Male Non-Smoker ALB
 - Factor: 100%
- Expenses
 - % of Premium: 13%
 - Monthly Admin: \$14 in year 1, \$9 in years 2+
- Surrender Charge SNFL Expense Allowance remaining

■ $RPNA = SNFL \text{ Value} = \text{Cash Surrender Value}$



ACCUMULATION UNIVERSAL LIFE (UL) EXAMPLE

Year	Annual Premium	Expenses	Mortality	Interest	Account Value	SNFL Value	RPNA	Years ETI
1	2,854	(539)	(759)	25	1,580	-	-	-
2	2,854	(479)	(808)	73	3,220	455	455	<1
5	2,854	(479)	(935)	219	8,172	5,677	5,677	4
10	2,854	(479)	(1,246)	460	16,305	14,264	14,264	7
15	2,854	(479)	(1,627)	685	23,856	22,251	22,251	7
20	2,854	(479)	(2,083)	876	30,221	28,996	28,996	6
25	2,854	(479)	(2,573)	1,023	35,060	34,140	34,140	6
30	2,854	(479)	(2,924)	1,125	38,386	37,732	37,732	5

UNIVERSAL LIFE WITH SECONDARY GUARANTEES (UL-SG)

- Under current NF requirements, UL-SG products are not required to provide additional NF benefits related to the secondary guarantees
- UL-SG products provide for continued coverage if premium payments continue to meet specified requirements, even if the cash surrender value is zero. If premium payments subsequently fail to meet the requirements, the policy lapses without value or NF benefits
- Under GPNM, any prefunding would be recognized with respect to both the basic and the secondary guarantee, and NF benefits would be the greater of the NF benefit for each guarantee
- Some premium requirements used today with UL-SG products are not compatible with GPNM, therefore if GPNM is adopted, product modifications or exemptions would be needed to assure that new sales continue to comply with NF requirements



UNIVERSAL LIFE WITH SECONDARY GUARANTEES (UL-SG) EXAMPLE

- **UL-SG Shadow Fund (secondary guarantee)**
 - Coverage: Universal Life, Level Death Benefit = \$50,000
 - Insured: Male, Age 65, Standard Non-tobacco
 - Premium: \$33.12 per 1000 (annualized, paid monthly)
 - Level premium amount needed to mature the policy on the secondary guarantee basis

- **GPNM Assumptions (GNFB Factors)**
 - Interest 6.00%
 - Mortality (Table rate x Factor)
 - Table: 2001 CSO Select &Ultimate, Male Non-Smoker ALB
 - Factor: 80%
 - Expenses
 - % of Premium: 10%
 - Monthly Admin: \$10 in year 1, \$5 in years 2+

- **RPNA = Shadow Fund (SF) Value**



UNIVERSAL LIFE WITH SECONDARY GUARANTEES (UL-SG) EXAMPLE

Year	Annual Premium	Expenses	Mortality	Interest	SF Value	SNFL Value	RPNA	Years ETI
1	1,656	(286)	(156)	39	1,253	0	1,253	3
2	1,656	(226)	(219)	114	2,578	0	2,578	5
5	1,656	(226)	(410)	349	6,639	0	6,639	8
10	1,656	(226)	(699)	767	13,899	0	13,899	9
15	1,656	(226)	(1,280)	1,188	21,064	0	21,064	9
20	1,656	(226)	(1,812)	1,556	27,328	0	27,328	8
25	1,656	(226)	(2,421)	1,854	32,302	0	32,302	7
30	1,656	(226)	(2,872)	2,064	35,814	0	35,814	6

TRADITIONAL WHOLE LIFE (WL)

- Current NF requirements for traditional WL products are based on net premiums and assumed expense loads rather than gross premiums and actual loads
- Under GPNM, gross premiums and actual loads would be used for NF calculations
- Some traditional WL policies may use the same tabular cash values for various risk classes with different gross premium levels as the basis for NF benefits
- If GPNM is adopted, product modifications and/or exemptions may be needed to assure that new sales continue to comply with NF requirements



TRADITIONAL WHOLE LIFE (WL) EXAMPLE - SNFL

■ Whole Life policy

- Coverage: Whole Life, Level Death Benefit = \$100,000
- Insured: Male, Age 35, Standard Non-tobacco
- Premium: \$9.35 per 1000 (annual)

■ SNFL Assumptions

- Interest 4.50%
- Mortality 100% of 2001 CSO Ultimate, Male Non-Smoker ALB

■ SNFL Value Components

- Net Level Premium = \$8.90
- Expense Allowance = \$21.13
- Adjusted Premium = \$10.00



TRADITIONAL WHOLE LIFE (WL) EXAMPLE - GPNM

- Whole Life policy
 - Coverage: Whole Life, Level Death Benefit = \$100,000
 - Insured: Male, Age 35, Standard Non-tobacco
 - Premium: \$9.35 per 1000 (annual)
- GPNM Assumptions (GNFB Factors)
 - Interest 4.50%
 - Mortality (Table rate x Factor)
 - Table: 2001 CSO Ultimate, Male Non-Smoker ALB
 - Factor: 65% in years 1-30, 97% in years 31+
 - Expenses
 - % of Premium: 100% in year 1, 5% in years 2+
 - Annual Admin: \$100 in year 1, \$5 in years 2+
- $RPNA = \text{Accumulated Value based on Premium and GNFB Factors}$



TRADITIONAL WHOLE LIFE (WL) EXAMPLE

Year	Annual Premium	Expenses	Mortality	Interest	Accum. Value	SNFL Value	RPNA	Years ETI
1	935	(1,096)	(72)	(7)	(241)	-	-	0
2	935	(62)	(76)	28	584	-	584	6
5	935	(62)	(90)	144	3,263	2,405	3,263	20
10	935	(62)	(133)	369	8,443	7,774	8,443	25
15	935	(62)	(181)	637	14,617	14,040	14,617	26
20	935	(62)	(269)	958	21,975	21,343	21,975	25
25	935	(62)	(396)	1,330	30,494	29,460	30,494	23
30	935	(62)	(593)	1,758	40,229	38,220	40,229	21



FIXED DEFERRED ANNUITY

- Current NF requirements for Fixed Deferred Annuities use different methodologies from SNFL for life insurance
- Basic Annuity SNFL requirement is a retrospective accumulation of premiums, at specified rates and with specified loads, over a specified period
- Cash Surrender Values are not required (although if provided must meet certain requirements)
- In the NAIC model NF requirements, a prospective test also applies if cash values are provided, effectively limiting the pattern of surrender charges
- Under GPNM, the value of non-guaranteed elements (NGEs) would be recognized in NF calculations once the NGEs are credited to the contract



FIXED DEFERRED ANNUITY EXAMPLE 1

- Fixed Deferred Annuity policy (Front Load)

- Annuitant Age 40
- Premium = \$100,000

- SNFL Assumptions

- Interest 1.00% - 3.00% (based on US Treasury rates)
 - Assume 1.50% for Example

- Expenses

- % of Premium: 12.5%
- Admin Expense: \$50

- GPNM Assumptions (GNFB Factors)

- Interest 1.50%
- Expenses
 - % of Premium: 10%
 - Admin Expense: \$120



FIXED DEFERRED ANNUITY EXAMPLE 1

Year	Account Value	SNFL Value	RPNA
1	91,228	88,762	91,228
2	92,475	90,042	92,475
5	96,328	94,001	96,328
10	103,145	101,004	103,145
15	110,489	108,549	110,489
20	118,400	116,676	118,400
25	126,923	125,432	126,923
30	136,105	136,105	136,105



FIXED DEFERRED ANNUITY EXAMPLE 2

- Fixed Deferred Annuity policy (Back Load)

- Annuitant Age 40
- Premium = \$100,000

- SNFL Assumptions

- Interest 1.50%
- Expenses
 - % of Premium: 12.5%
 - Admin Expense: \$50

- GPNM Assumptions (GNFB Factors)

- Interest 1.50%
- Expenses
 - % of Premium: 0%
 - Admin Expense: \$0
 - Surrender Charge: 10% grading down 1% per year



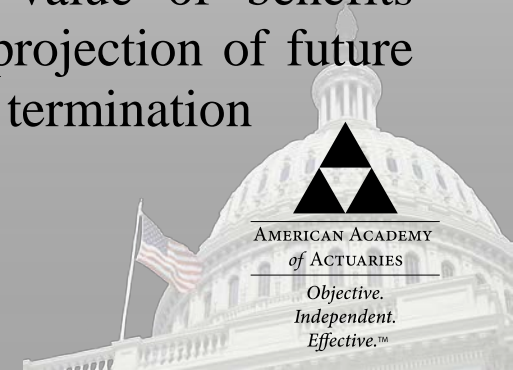
FIXED DEFERRED ANNUITY EXAMPLE 2

Year	Account Value	Surrender Value	SNFL Value	RPNA
1	101,500	91,350	88,762	91,350
2	103,023	93,750	90,042	93,750
5	107,728	101,265	94,001	101,265
10	116,054	114,894	101,004	114,894
15	125,023	125,023	108,549	125,023
20	134,686	134,686	122,108	134,686
25	145,095	145,095	138,154	145,095
30	156,308	156,308	156,308	156,308



ANNUITY WITH GUARANTEED LIVING BENEFITS

- Guaranteed Living Benefits (GLB) are offered in conjunction with a variety of deferred annuity types (fixed, variable, indexed, contingent)
- GLB are typically provided by rider, which may be optional or included, or may be standalone, e.g., Contingent Deferred Annuity (CDA)
- Charges to the policyholder for benefit costs may be explicit or implicit
- Current NF requirements do not recognize the value of these benefits or the cost to the policyholder
- If the annuity is surrendered or the GLB is terminated, there is generally no consideration of the value of charges deducted to that point for GLB
- Under GPNM, prefunding, expressed as the current value of benefits associated with charges deducted for GLB, based on a projection of future benefits, would be recognized at policy surrender or GLB termination



ANNUITY WITH GUARANTEED LIVING BENEFITS EXAMPLE

- Annuity Guaranteed Withdrawal Benefit
 - Fixed Deferred Annuity with Account Value (AV)
 - Annuitant Age 40
 - Premium = \$100,000
 - GLB Base = Rollup of Premium @ 4%, capped at 2X Premium
 - GLB Percentages vary by age at first withdrawal (4% to 7%)
 - GLB Withdrawal Amount = GLB % of GLB Base at time of first withdrawal
 - GLB Charge = 0.50% of GLB Base, annually
 - Earliest Exercise @ Age 60
- SNFL Assumptions (not applicable)
- GPNM Assumptions (GNFB Factors)
 - Interest growth (for projecting assumed future AV) 1.50%
 - Interest discount (for determining PV of Rider Benefits) 1.50%
- Other assumptions
 - Interest credited to AV prior to NF event 3.00%



ANNUITY WITH GUARANTEED LIVING BENEFITS EXAMPLE

- GPNM retrospective approach is modified for this coverage
 - RPNA is not calculated
 - NF Benefit is calculated directly, upon NF event (cancellation of policy or rider coverage) by projecting AV to determine benefits and charges that would otherwise apply (if no cancellation)
 - NF Benefit is a percentage of the projected GLB Withdrawal Amount that would otherwise be payable, assuming Withdrawals begin at the earliest possible date
 - Percentage of projected GLB Withdrawal Amount is the ratio of
 - 1) the present value of rider charges deducted before the NF event to
 - 2) the present value of total rider charges (including deducted and projected charges)
 - NF Benefits begin at the date benefits would otherwise begin, based on the projection (i.e., when the policy account value is projected to be depleted by assumed withdrawals)



ANNUITY WITH GUARANTEED LIVING BENEFITS EXAMPLE

Age at Termination	GLB WD Age	GLB WD %	GLB WD Benefit	% of Charges Paid	NF Benefit	NF Start Age
45	60	4.0%	8,000	12%	980	75
50	60	4.0%	8,000	25%	2,028	77
55	60	4.0%	8,000	40%	3,188	79
60	60	4.0%	8,000	54%	4,320	80
65	65	5.0%	10,000	65%	6,472	83
70	70	6.0%	12,000	72%	8,664	87



POTENTIAL NEXT STEPS

- Consider availability of & conditions for cash values
- Provide additional comparison examples for existing products
- Develop recommendations regarding existing products
- Analysis of Variable and/or Indexed products
- Examples of treatment of non-guaranteed elements



THANK YOU!

QUESTIONS?

