INTERSTATE INSURANCE PRODUCT REGULATION COMMISSION

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MEMORANDUM

TO: **IIPRC Management Committee**

FROM: **Product Standards Committee**

DATE: **February 22, 2010**

SUBJECT: **Termination Provision in Guaranteed Annuity Benefit Feature Standards**

Issue: On January 25, the Management Committee of the Interstate Insurance Product Regulation Commission ("IIPRC") directed the Product Standards Committee ("PSC") to evaluate the comments received regarding the Termination provision of three proposed uniform standards currently under consideration[1] and provide further recommendations regarding options for addressing the concerns highlighted by the comments.

Recommendation: The PSC recommends enhancing consumer disclosure by prescribing specific disclosure language for products with restrictions on transfer of ownership.

Background: The Termination provision in each of the three proposed standards provides an option for the company to terminate the benefit feature upon a change in ownership or assignment of the underlying annuity contract unless:

(1) The new owner or assignee assumes full ownership of the contract and is essentially the same person (e.g. an individual ownership changed to a personal revocable trust, a joint ownership of husband and wife changed to the surviving spouse when one of them dies, a change to the owner's spouse during the owner's lifetime, a change to a court appointed guardian representing the owner during the owner's lifetime, etc.); or

(2) The assignment is for the purposes of effectuating a 1035 exchange of the contract (i.e. the rider may continue during the temporary assignment period and not terminate until the contract is actually surrendered);

The PSC reviewed the written comments received by the Management Committee. There are substantial comments on both sides of the issue, from sources including legislators, regulators, consumer representatives, actuaries, the insurance industry and the life insurance settlement industry. Some comments request the removal of this portion of the Termination provision on the basis that it is overly restrictive of a consumer's ability to "seek outside assistance in the settlement of their annuities if they so choose."[2] Other comments request that the provision remain as drafted because removing the ability to terminate the benefit if the annuity is sold would result in higher pricing for all consumers, regardless of

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[1] The effected standards are the Additional Standards for Guaranteed Living Benefits for Individual Deferred Non-Variable Annuities, the Additional Standards for Guaranteed Living Benefits for Individual Deferred Variable Annuities, and the Additional Standards for Guaranteed Minimum Death Benefits for Individual Deferred Variable Annuities.

[2] Comment Letter from State Representative Robert R. Damron (KY), submitted Dec. 4, 2009.

whether a particular consumer ultimately maintains ownership of the underlying annuity contract. All written comments submitted for the proposed standards are accessible on the IIPRC's online Docket (www.insurancecompact.org). The PSC held a public meeting to receive public comments on this recommendation on February 18, during which the PSC made slight changes to the disclosure statement based on comments from the Industry Advisory Committee.

Analysis: The PSC viewed its assignment as balancing two equally important consumer interests: (1) the unrestricted ability to transfer ownership and (2) the potential for increased cost and reduced availability. The PSC weighed several factors in making its recommendation.

- The provision applies exclusively to termination of the benefit feature, and not to the underlying annuity contract. Assignment or change in ownership of the underlying annuity contract would continue to be viable.
- The provision is permissive, i.e. companies may offer guaranteed benefits that do not restrict transfer of ownership.
- The pricing of annuity products is unregulated, which does not lend itself to overseeing the fair pricing of products with and without the ability to terminate the benefit feature upon assignment or change in ownership.
- Eliminating restrictions on termination could potentially result in significant increases in cost for all consumers of these products, which the PSC did not view as a good alternative.
- Products with guaranteed benefits are on the market today without the benefit of uniformity among the states provided by IIPRC uniform standards.
- Products with no restrictions on termination of the guaranteed benefits upon any transfer of ownership are on the market today. The provision contained in the standard already provides greater consumer protection by specifying certain transfers that cannot trigger termination.

The PSC's recommendation is to retain the Termination provision as originally proposed and to change the Cover Page requirements to mandate a specific, prescribed disclosure about the termination of the guaranteed benefits. The mandatory disclosure would state:

> The purpose of the guaranteed living benefit provided under this annuity contract is to provide security through a stream of monthly income payments to the owner. The guaranteed living benefits will terminate upon assignment or a change in ownership of the contract unless the new assignee or owner meets the qualifications specified in the Termination provision of the guaranteed living benefit.

As originally proposed, the standards required disclosure on the cover page or first specifications page about the potential for termination, but the content of the disclosure was not prescribed. The PSC believes this approach maintains the delicate balance between the consumer interests described above while providing certainty that the potential for termination is disclosed to consumers clearly, concisely and unambiguously. The recommendation applies to each of the guaranteed benefit standards.

Another approach considered but not ultimately recommended by the PSC, is to tie restrictions on transfer of ownership to what IIPRC member states already permit. The PSC prefers retaining the Termination provision as originally proposed and adding a promulgated disclosure notice, thereby maintaining uniformity and certainty in product filing requirements. The PSC concluded that regulatory policy on the secondary sale of these annuity benefit features is still emerging. Points considered regarding this approach include the following:

- Regulation of the secondary market is outside of the IIPRC's authority, as are other areas where uniform standards defer to existing state law such as domestic partnership, civil union and marriage.
- Uniform Standards should be reflective of policy decisions regarding the secondary market already made by state legislatures and implemented by insurance departments.
- Consumers should maintain the same choice to enter the secondary market as they possess today in IIPRC member states.
- The following revision to the Termination provision was considered.

(2) A GLB form that is built in or attached to the contract by rider, endorsement or amendment may include the following conditions for termination of the benefit feature or the rider, endorsement or amendment:

(e) Upon a change in ownership (or assignment) of the contract unless prohibited by applicable law in the state where the policy is delivered or issued for delivery at the time of issue or delivery and unless:

(i) The new owner or assignee assumes full ownership of the contract and is essentially the same person (e.g. an individual ownership changed to a personal revocable trust, a joint ownership of husband and wife changed to the surviving spouse when one of them dies, a change to the owner's spouse during the owner's lifetime, a change to a court appointed guardian representing the owner during the owner's lifetime, etc.); or

(ii) The assignment is for the purposes of effectuating a 1035 exchange of the contract (i.e. the rider may continue during the temporary assignment period and not terminate until the contract is actually surrendered); …

If the Management Committee employs this approach, the PSC would still recommend incorporating the enhanced disclosure requirement.