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INSURANCE

DEP ARTMENT OF BANKING AND INSURANCE

OFFICE OF LIFE AND HEALTH

Preferred Mortality Tables for Use in Determining Minimum Reserve Liabilities

Valuation of Life Insurance Policies

Proposed Amendments: N.J.A.C. 11:4-27A.3 and 32.3

Authorized By: Douglas A. Wheeler, Director, Division of Insurance, Department of Banking and Insurance.

Authority: N.J.S.A. 17:1-8.1, 17:1-14, 17:1-15e and 17B:19-8.

Calendar Reference: See Summary below for explanation of exception to calendar requirement.

Proposal Number: PRN 2010-174.

Submit comments by October 15, 2010 to:

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The agency proposal follows:

Summary

The Standard Valuation Law, N.J.S.A. 17B:19-8, sets forth the basis for the annual valuation of the reserve liabilities of life insurance policies. Pursuant to N.J.S.A. 17B:19-8a(i), the Commissioner of Banking and Insurance (Commissioner) may promulgate a mortality table adopted by the National Association of Insurance Commissioners (NAIC) for use in determining the minimum standard valuation. On November 1, 2004, the Commissioner adopted N.J.A.C. 11:4-27 permitting the use of the 2001 Commissioner's Standard Ordinary (CSO) Table. On September 10, 2006, the NAIC approved amendments to the 2001 CSO Mortality Tables as a basis for valuation and non-forfeiture. The amendments created a new 2001 CSO Preferred Class Structure Mortality Table. In 2008, the Department adopted this Table at N.J.A.C. 11:4-27A. In 1999, the Department adopted N.J.A.C. 11:4-32, which provides the general requirements for the valuation of life insurance policies. Both of these rules are based on applicable NAIC models, which recently have been amended. The Department of Banking and Insurance (Department) proposes amendments to N.J.A.C. 11:4-27A.3 and 32.3 to reflect these changes. The amendments are summarized below.

N.J.A.C. 11:4-27A.3(a) is proposed to be amended to provide that, for policies issued on or after January 1, 2005 and prior to January 1, 2007, the applicable 2001 CSO Preferred Class Structure Mortality Table may be substituted with the consent of the Commissioner and subject to the conditions of N.J.A.C. 11:4-27A.4. In determining such consent, the Commissioner may rely on the consent of the commissioner of the insurer's state of domicile. The Department also proposes to amend this rule to add a new subsection (d) to provide that the use of the 2001 CSO Preferred Class Structure Table for the valuation of policies issued prior to January 1, 2007 shall not be permitted in any statutory financial statement in which a company reports, with respect to any policy or portion of a policy coinsured, either of the following:

1. In cases where the mode of payment of the reinsurance premium is less frequent than the mode of payment of the policy premium, a reserve credit that exceeds, by more than the amount specified in the rule designated as “Y,” the gross reserve calculated before reinsurance; or

2. In cases where the mode of payment of the reinsurance premium is more frequent than the mode of payment of the policy premium, a reserve credit that is less than the gross reserve, calculated before reinsurance, by an amount that is less than the amount specified in the rule as “Z.”

Finally, this proposed amendment provides that the reserve for the mean reserve method shall be defined as the mean reserve minus the deferred premium asset, and for the mid-terminal reserve method shall include the unearned premium reserve. The rule provides that a company may estimate and adjust its accounting on an aggregate basis in order to meet the conditions for the use of the 2001 CSO Preferred Class Structure Table.

N.J.A.C. 11:4-32.3(b)3 is proposed to be amended to remove the requirements as currently set forth in the rule at subparagraphs (b)3ii and iii, that so called “X” factors shall not be less than 20 percent and shall not decrease in any successive policy year. Existing subparagraphs (b)3iv through viii are proposed to be recodified as (b)3ii through vi, respectively. In addition, existing N.J.A.C. 11:4-32.3(b)3vii (proposed to be recodified as (b)3v) is proposed to be amended to delete the following language: “… the

X factor does not decrease in any successive policy years as long as it…" to reflect the changes set forth above and the current NAIC model.

Finally, N.J.A.C. 11:4-32.3(b)4 is proposed to be amended to add a new subparagraph (b)4ii to provide that the appointed actuary shall disclose, in the Regulatory Asset Adequacy Issues Summary required pursuant to N.J.A.C. 11:1-21A.5(e), the impact of the insufficiency of assets to support the payment of benefits and expenses in the establishment of statutory reserves during one or more interim periods. In addition, existing subparagraph (b)4ii is proposed to be recodified as (b)4iii.

The proposed amendments are intended to conform the existing rules with the current NAIC Model Regulation Permitting the Recognition of Preferred Mortality Tables for Use in Determining Minimum Reserve Liabilities, and the Valuation of Life Insurance Policies Model Regulation, respectively. Accordingly, the proposed amendments reflect the current national standard for use by insurers in establishing reserves for life insurance policies.

A 60-day comment period is provided for this notice of proposal, and, therefore, pursuant to N.J.A.C. 1:30-3.3(a)5, the proposal is not subject to the provisions of N.J.A.C. 1:30-3.1 and 3.2 governing rulemaking calendars.

Social Impact

The proposed amendments affect minimum reserve liabilities that insurers must establish pursuant to law and may permit insurers to hold lower reserves under a formula than is the case under the current rules. This, in turn, may result in lower costs of doing business to insurers, which savings may be shared with policyholders classified as preferred risks. This should result in a positive social impact. The Department notes that, pursuant to N.J.S.A. 17B:19-10, insurers will continue to be required to submit an opinion by a qualified actuary whether the insurer's reserves and related actuarial items held in support of policies and contracts make adequate provision for the insurer's obligations under the policies and contracts, including benefits thereunder.

Economic Impact

The proposed amendments to N.J.A.C. 11:4-27A.3 generally will permit insurers to lower reserve requirements by electing to use the 2001 CSO Preferred Class Structure Mortality Table, and may also result in lower premiums and charges for those policyholders included in the preferred class or in higher earnings for insurers. This, in turn, should provide a beneficial impact both to insurers and policyholders. In addition, the proposed amendments to N.J.A.C. 11:4-32.3 generally will have a similar impact with respect to policyholders included in the standard class. As noted in the Social Impact above, pursuant to N.J.S.A. 17B:19-10, insurers will continue to be required to submit an opinion by a qualified actuary whether the insurer's reserves and related actuarial items held in support of policies and contracts make adequate provision for the insurer's obligations under the policies and contracts, including benefits thereunder.

Professional services required to comply with the proposed amendments will include actuarial and accounting services. The Department believes that insurers have already developed in-house operations, or contracted with outside entities, for the services needed in order to comply with existing N.J.A.C. 11:4-27A and 32, respectively, and to comply with the proposed amendments.

In addition, appointed actuaries filing the actuarial opinion memorandum required pursuant to N.J.A.C. 11:1-21A must include, to the extent that the “X” factor is less than 100 percent at any duration for any policy, in the Regulatory Asset Adequacy Issues Summary required pursuant to N.J.A.C. 11:1-21A.5(e), the impact of the insufficiency of assets to support the payment of benefits and expenses and the establishment of statutory reserves during one or more interim periods. The Department believes that any additional costs that may be imposed on actuaries or insurers in providing this additional information should be minimal in that such information should be readily available and developed as part of the insurer’s and its in-house or contracted actuary’s analysis of reserves in compliance with N.J.A.C. 11:4-32.

Accordingly, little or no additional costs should be imposed with the benefits set forth above to be achieved.

Federal Standards Statement

A Federal standards analysis is not required because the proposed amendments are not subject to any Federal requirements or standards.

Jobs Impact

The Department does not anticipate that any jobs will be generated or lost as a result of the proposed amendments.

The Department invites commenters to submit any data or studies on the potential jobs impact of the proposed amendments together with their comments on other aspects of the proposal.

Agriculture Industry Impact

The proposed amendments will not have any impact on the agriculture industry in New Jersey.

Regulatory Flexibility Analysis

The proposed amendments may apply to "small businesses," as that term is defined in the Regulatory Flexibility Act, N.J.S.A. 52:14B-16 et seq. To the extent that the proposed amendments apply to small businesses, they will apply to domestic insurers providing life insurance in this State. The Department did not provide any differentiation in compliance requirements based on insurer size. First, the Department believes that the proposed amendments will apply to few, if any, small businesses in that most of the affected insurers do not employ fewer than 100 full-time employees. Moreover, insurers are not required to use the tables under N.J.A.C. 11:4-27A. In addition, the proposed amendments provide more flexibility to insurers by enabling them to reduce required reserves under specified conditions. Moreover, the proposed amendments reflect current NAIC model language which reflects the national standard for these requirements. The costs of compliance and professional services required are set forth in the Economic Impact above. As noted above, the Department does not believe that any additional professional services should be required in order to comply with these proposed amendments. In addition, as is the case with the existing rules, the Department believes that it is necessary to provide a uniform standard under which valuations of life insurance policies are performed to ensure that reserves for such policies are established consistently among all insurers in the market and that such reserves are adequate to pay benefits when they are due.

Smart Growth Impact

The proposed amendments will not have an impact on the achievement of smart growth or the implementation of the State Development and Redevelopment Plan.

Housing Affordability Impact

The proposed amendments will not have an impact on housing affordability in this State in that the proposed amendments relate to the valuation of life insurance policies.

Smart Growth Development Impact

The proposed amendments will not have an impact on smart growth in this State and there is an extreme unlikelihood that the rules would evoke a change in housing production in Planning Areas 1 or 2 or within designated centers under the State Development and Redevelopment Plan in New Jersey in that the proposed amendments relate to the valuation of life insurance policies.

Full text of the proposal follows (additions indicated in boldface **thus**; deletions indicated in brackets [thus]):

SUBCHAPTER 27A. PREFERRED MORTALITY TABLES FOR USE IN DETERMINING MINIMUM RESERVE LIABILITIES

11:4-27A.3 2001 CSO Preferred Class Structure Mortality Table

(a) At the election of the insurer, for each calendar year of issue, for any one or more specified plans of insurance and subject to satisfying the conditions stated in this subchapter, the 2001 CSO Preferred Class Structure Mortality Table may be substituted in place of the 2001 CSO Smoker or Nonsmoker Mortality Table as the minimum valuation standard for policies issued on or after January 1, 2007. The 2001 CSO Preferred Class Structure Mortality Table is available on the NAIC's website at www.soa.org/research/individual-life/intl-2001-cso-preferred-class-structure-mortality-tables.aspx. The Department shall notify insurers of any changes to the 2001 CSO Preferred Class Structure Mortality Table by Bulletin. **For policies issued on or after January 1, 2005, and prior to January 1, 2007, these tables may be substituted with the consent of the Commissioner and subject to the conditions of N.J.A.C. 11:4-27A.4. In determining such consent, the Commissioner may rely on the consent of the Commissioner of the company's state of domicile.**

(b) – (c) (No change.)

(d) The use of the 2001 CSO Preferred Class Structure Table for the valuation of policies issued prior to January 1, 2007 shall not be permitted in any

statutory financial statement in which a company reports, with respect to any policy or portion of a policy coinsured, either of the following:

1. In cases where the mode of payment of the reinsurance premium is less frequent than the mode of payment of the policy premium, a reserve credit that exceeds, by more than the amount specified in this paragraph as Y, the gross reserve calculated before reinsurance. Y shall be the amount of the gross reinsurance premium that:

i. Provides coverage for the period from the next policy premium due date to the earlier of the end of the policy year and the next reinsurance premium due date; and

ii. Would be refunded to the ceding entity upon the termination of the policy.

2. In cases where the mode of payment of the reinsurance premium is more frequent than the mode of payment of the policy premium, a reserve credit that is less than the gross reserve, calculated before reinsurance, by an amount that is less than the amount specified in this paragraph as Z. Z shall be the amount of the gross reinsurance premium that the ceding entity would need to pay the assuming company to provide reinsurance coverage from the period of the next reinsurance premium due date to the next policy premium due date minus any liability established for the proportionate amount not remitted to the reinsurer.

3. For purposes of this subsection, the reserve for the mean reserve method shall be defined as the mean reserve minus the deferred premium

asset, and for the mid-terminal reserve method shall include the unearned premium reserve. A company may estimate and adjust its accounting on an aggregate basis in order to meet the conditions for the use of the 2001 CSO Preferred Class Structure Table.

SUBCHAPTER 32. VALUATION OF LIFE INSURANCE POLICIES

11:4-32.3 General calculation requirements for basic reserves and premium deficiency reserves

(a) (No change.)

(b) Deficiency reserves, if any, are calculated for each policy as the excess, if greater than zero, of the quantity A over the basic reserve. The quantity A is obtained by recalculating the basic reserve for the policy using guaranteed gross premiums instead of net premiums when the guaranteed gross premiums are less than the corresponding net premiums. At the election of the insurer for any one or more specified plans of insurance, the quantity A and the corresponding net premiums used in the determination of quantity A may be based upon the 1980 CSO valuation tables with select mortality factors (or any other valuation mortality table adopted by the NAIC after January 1, 2000 and promulgated by the Commissioner). If select mortality factors are elected, they may be:

1. – 2. (No change.)

3. For durations in the first segment, X percent of the select mortality factors in the Appendix, subject to the following:

i. (No change.)

[ii. X shall not be less than 20 percent;

iii. X shall not decrease in any successive policy years;]

Recodify existing iv. – vi. as **ii. – iv.** (No change in text.)

[vii.] **v.** The appointed actuary may decrease X at any valuation date as long as X [does not decrease in any successive policy years and as long as it] continues to meet all the requirements of this paragraph and (b)4 below; **and**

[viii.] **vi.** (No change in text.)

4. If X in (b)3 above is less than 100 percent at any duration for any policy, the following requirements shall be met:

i. The appointed actuary shall annually prepare an actuarial opinion and memorandum for the insurer in conformance with the requirements of N.J.A.C. 11:1-21A.6; [and]

ii. The appointed actuary shall disclose, in the Regulatory Asset Adequacy Issues Summary required pursuant to N.J.A.C. 11:1-21A.5(e), the impact of the insufficiency of assets to support the payment of benefits and expenses and the establishment of statutory reserves during one or more interim periods; and

[ii.] **iii.** (No change in text.)

5. (No change.)

(c) – (f) (No change.)