ATTACHMENT ONE

STATEMENT ON BEHALF OF THE
AMERICAN COUNCIL OF LIFE INSURANCE
TO THE
NAIC (A) COMMITTEE'S
LIFE COST DISCLOSURE TASK FORCE

November 29, 1982

This statement is presented on behalf of the American Council of Life Insurance, whose 555 member companies account for about 95 percent of the life insurance in force in the United States.

At your June meeting, your task force received a draft of a proposed revision of the NAIC Life Insurance Solicitation Model Regulation. The draft was designed to reflecr changes to the model regulation that are supported by the council. It had been prepared by the council staff but had not been reviewed by the appropriate council committees. That review has been completed, and the council now recommends that your task force support NAIC adoption of the revised draft attached to this statement.

The revised draft is substantially the same as the June draft. Some details have been changed, and various refinements and editorial improvements have been made. In addition, a revised Buyer's Guide has been developed and is proposed for adoption as parr of the new model regulation. The revised draft includes annotations indicating the source and background of the changes being proposed to the current model regulation.

This proposal would incorporate the following new features into the model regulation:

1. The concept of a nonguaranteed element to measure the extent to which policy costs can be affected by premiums, benefits, or other items that are subject to change by the company without the consent of the policyholder.

2. A special plans section to accommodate the unique features of nontraditional plans such as universal life insurance.

3. Provision for disclosure of dividend practices to both new and existing policyholders, in accordance with recommendations presented to the NAIC by the Committee on Dividend Principles and Practices of the American Academy of Actuaries.

4. Provision for disclosure to regulators and policyholders of unusual patterns of premiums and benefits, in accordance with recommendations from the NAIC Advisory Committee on Manipulation.

5. Provision for policyholders to request additional information relating to future premiums, benefits, and other items affecting policy costs.

6. Revision of the requirement relating to disclosure of the policy loan interest rate in order to accommodate the features of the NAIC Model Policy Loan Interest Rate Bill.

7. A new Buyer's Guide, with changes designed to take account of recent product developments and to enhance the guide's readability and usefulness.

In connection with item 4 relating to disclosure of unusual discontinuities in yearly prices, we would call your attention to Appendix C of the draft regulation. This appendix is designed to show the numerical values, referred to as "test limits," to be used in testing for these price discontinuities. The Drafting Note in Appendix C indicates that the test limits illustrated apply only to a traditional type of whole life policy and that additional research needs to be done on this subject for other plans and higher issue ages. The council stand as ready to assist your task force and the NAIC in this effort.

Finally, two editorial corrections should be noted in the draft:

1. At the top of page 9 of the annotated draft, the words "Current Dividend Scale or" should be inserted after the word "company's" in the last line of subsection 4(J) (3). This change would make this reference consistent with similar references in other parts of the draft.

2. At the bottom of page 22 of the annotated draft, in subsection 6(A), the following sentence should be inserted after the first sentence and before the sentence "for these policies . . .":

   "The crossover point of an enhanced ordinary life policy is the first policy anniversary at which the sum of the reduced basic amount and paid-up additions equals or exceeds the initial death benefit."

   The addition of this sentence is necessary to enable the reader to understand the instructions that follow.

The council feels strongly that adoption of these proposed revisions to the model regulation would be another clear demonstration of the responsiveness of insurance regulation to the changing needs of the marketplace. This updated and improved model regulation will help to ensure that meaningful and useful information will continue to be provided to the insurance-buying public.

We thank you for your attention and we will be glad to answer any questions you may have.

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ATTACHMENT ONE-A

Bracketing [ ] indicates deletion; <u>underlining</u> indicates new material.

Proposed Revision of
NAIC Life Insurance Solicitation Model Regulation

October 22, 1982

LIFE INSURANCE [SOLICITATION] <u>DISCLOSURE</u> MODEL REGULATION

COMMENT: Since new subsection 5(c) contains requirements applicable to existing policies, the name of the regulation should be revised to indicate that it applies in more situations than just solicitation.

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COMMENT: The changes evident here are discussed in each pertinent annotation.

Section 1. Authority.

This rule is adopted and promulgated by (title of supervisory authority) pursuant to sections (4(1) (a) of the Unfair and Deceptive Acts and Practices in the Business of Insurance Act) of the insurance code.

Section 2. Purpose.

(A) The purpose of this regulation is to require insurers to deliver to purchasers of life insurance[,] information which will improve the buyer's ability to select the most appropriate plan of life insurance for [his] the buyer's needs, improve the buyer understanding of the basic features of the policy which has been purchased or which is under consideration and improve the ability of the buyer to evaluate the relative costs of similar plans of life insurance.

COMMENT: These are editorial changes to improve grammar and delete a sex-specific pronoun.

(B) This regulation does not prohibit the use of additional material which is not in violation of this regulation or any other (state) statute or regulation.

Section 3. Scope.

(A) Except [as hereafter exempted] for the exemptions specified in Section 3(B), this regulation shall apply to any solicitation, negotiation or procurement of life insurance occurring within this state.

COMMENT: The drafters do not intend this revision to be a substantive change in the applicability of this regulation. It is intended merely as a clarification.

Subsection 5(C) only shall apply to any existing nonexempt policy held by a policyowner residing in this state. This regulation shall apply to any issuer of life insurance contracts, including fraternal benefit societies.

COMMENT: Subsection 5(c) is new, and it applies to existing policies.. The purpose of the new sentence in this subsection is to clarify when those requirements apply. For purposes of this regulation, the regulation of the policyowner's domiciliary state would apply notwithstanding the existence or absence of applicable regulations in the state of issue.

(B) Unless [otherwise] specifically included, this regulation shall not apply to:

1. Annuities.
2. Credit life insurance.
3. Group life insurance.
4. Life insurance policies issued in connection with pension and welfare plans as defined by and which are subject to the federal Employee Retirement Income Security Act of 1974 29 U.S.C. §1001 et seq. (ERISA) as amended.

COMMENT: This addition is made merely as clarification.

5. Variable life insurance under which the [death benefits and cash values vary in accordance with unit values of investments held in] amount or duration of the life insurance varies according to the investment experience of a separate account.

SOURCE: Exposure Draft of the NAIC Variable Life Insurance Model Regulation, Art. II, §19. The text of § 19 may be found at page 770 of Volume 3 of the Compilation of Subcommittee and Task Force Reports of the NAIC's June 1982 Meeting.

COMMENT: The purpose of both the deletion and addition in this section is to update the definition of variable life insurance. New product designs include as features of variable or asset-based contracts premiums that are not fixed in amount or timing. Under a flexible premium variable life insurance policy insurance coverage would continue as long as amounts available under the policy are sufficient to support deductions for the cost of insurance and other charges. Thus it may be the duration of insurance coverage, rather than the amount of death benefit, which varies with investment experience. The drafters have revised the definition to include either design.

Section 4. Definitions.

For the purposes of this regulation, the following definitions shall apply:

[(a)] (A) Buyer's Guide. A Buyer's Guide is a document which contains, and is limited to, the language contained in [the] Appendix A to this regulation or language approved by (title supervisory authority).

(B) Cash Dividend. A Cash Dividend is the current illustrated dividend which can be applied toward payment of the gross premium.

(C) Contribution Principle. The Contribution Principle is a basic principle of dividend determination adopted by the American Academy of Actuaries with respect to individual life insurance policies issued by mutual companies. The Academy report, The Recommendations of the Committee on Dividend Principles and Practices (January 1981), describes this principle as the distribution of the aggregate divisible surplus among policies in the same proportion as the policies are considered to have contributed to divisible surplus. In a broad sense the Contribution Principle underlies the essential equity implied by participating business.

SOURCE: II 1981 NAIC PROC. 643-759, 647, 739, 754; American Academy of Actuaries, Report of the Committee on Dividend Principles and Practices (June 1980) (hereinafter cited Academy Report).

COMMENT: The definition was presented to the NAIC in June 1981 as part of the report of the (C3) Task Force on Manipulation, Lapsation, Dividend Practices and Annuity Disclosure. It is used in subsections 5(B)(1) and 5(C)(2) of this proposed regulation. Those provisions impose a duty on insurers to notify both new and existing policyowners if any policy's dividend calculations do not comply with the Contribution Principle. As drafted this definition and those subsections apply to mutual companies only. The Academy's Committee on Dividend Principles and Practices plans to develop orderly transition rules concerning accepted dividend practices for participating policies issued by stock companies.

(D) Current Dividend Scale. The Current Scale is a schedule that exhibits dividends to be distributed if there is no change in the basis of these dividends after the time of illustration.

COMMENT: The Current Dividend Scale is a disclosure item in subsections 4(J)(3), 4(N)(5)(g), 4(N)(8)(b), 5(C)(1), 6(A)(2), 7(D), and 7(H).

(E) Current Rate Schedule. The Current Rate Schedule is a schedule showing the premiums that will be charged or the cash values or death or other benefits that will be available if there is no change in the basis of these items after the time of illustration.

COMMENT: Recent policy designs have incorporated features that the company can change during the contract term. The expense or mortality rates, for example, are in some instances changeable. The Current Rate Schedule appears as a disclosure item in the same subsections as the Current Dividend Scale (above).

(F) Discontinuity Index. The Discontinuity Index is the sum of the backward second differences squared in the Yearly Prices of Death Benefits (per 1,000) for policy years 8 through 23. Examples of calculations appear in Appendix B of this regulation.

SOURCE: II 1981 NAIC PROC. 646-48, 739-40, 754-59. The Discontinuity Index was presented to the NAIC at its June 1981 meeting by the (C3) Task Force on Manipulation, Lapsation, Dividend Practices and Annuity Disclosure.

COMMENT: The purpose of the test is to disclose manipulation, which has been defined as an unrealistically attractive progression of premiums, dividends, and benefits that has no acceptable rationale. II 1980 NAIC PROC. 828-40, 830. Subsection 5(A)(3) imposes the discontinuity test on newly issued policies. The object of the test is to reveal to the regulator and affected policyowner which policies have unusually large changes in year-to-year costs. The test detects irregularities in the otherwise smooth progression of the net result of offsetting the dividends and annual changes in cash value against the annual premium. The test limits used to separate policies with undue irregularities are set out in Appendix C of this regulation. Those limits apply only to traditional types of whole life policies; other test limits should be developed for other plans. Test limits for issue ages over 45 are also necessary.

[(C) Equivalent Level Annual Dividend. The Equivalent Level Annual Dividend is calculated by applying the following steps:

1. Accumulate the annual cash dividends at five percent interest compounded annually to the end of the tenth and twentieth policy years.

2. Divide each accumulation of Step 1. by an interest factor that converts it into one equivalent level annual amount that, if paid at the beginning of each year, would accrue to the values in Step 1. over the respective periods stipulated in Step 1. If the period is ten years, the factor is 13.207 and if the period is twenty years, the factor is 34.719.

3. Divide the results of Step 2. by the number of thousands of the Equivalent Level Death Benefit to arrive at the Equivalent Level Annual Dividend.]

COMMENT: The drafters propose to eliminate this definition because some recent types of contracts have premiums or benefits that the company can change. For those plans the portion of the policy's cost which is not guaranteed can be generated by elements other than just dividends. The concept of the Equivalent Level Annual Dividend (ELAD) is succeeded by that of the Nonguaranteed Element, defined in subsection 4(L). The Nonguaranteed Element is intended to help consumers distinguish between guaranteed and nonguaranteed costs, as was the ELAD.

[(D)] (G) Equivalent Level Death Benefit. The Equivalent Level Death Benefit of a policy or term life insurance rider is an amount calculated as follows:

1. Accumulate the [guaranteed] amount payable upon death, regardless of the cause of death, at the beginning of each policy year for ten and twenty years at five percent interest compounded annually to the end of the tenth and twentieth policy years respectively.

2. Divide each accumulation of step 1. by an interest factor that converts it into one equivalent level annual amount that, if paid at the beginning of each year, would accure to the value in step 1. over the respective periods stipulated in step 1. If the period is ten years, the factor is 13.207 and if the period is twenty years, the factor is 34.719.

COMMENT: The term "guaranteed" has been eliminated to accommodate flexible premium and benefit policies. For all policies the calculation would be done using the stated or assumed death benefit for each year as shown in the Policy Summary (subsection 4(N) (5) (C)).

[(E)] (H) Generic Name. A Generic Name [means] is a short title [which] that is descriptive of the premium and benefit patterns of a policy or a rider.

COMMENT: This is an editorial change to conform this definition with others in this section.

(I) Investment Generation Method. The Investment Generation Method is the method of determining dividends so that dividends for policies issued in specified years or groups of years reflect investment earnings on funds attributable to those policies.

SOURCE: II 1981 NAIC PROC. 646-760, 733, 754, See Academy Report at 9, 13, 24, 29-30.

COMMENT: The actuarial profession has stated formally that either the investment generation method of allocating and illustrating investment income or the portfolio average method is considered generally accepted practices. Academy Report at 24. Their 1980 report recommending certain dividend principles and practices suggested, however, that the existence of different methods of reflecting investment earnings in dividend illustrations should be disclosed to consumers. Academy Report at 12-15. The Academy made several recommendations, many of which were presented to the NAIC in June 1981 and appear in these revisions.

[(F)] (J) [Life Insurance] Cost Comparison Indexes.

1. [Life Insurance] Surrender Cost Comparison Index. The [Life Insurance] Surrender Cost Comparison Index is calculated by applying the following steps:

   a. Determine the [guaranteed] cash surrender value, if any, available at the end of the tenth and twentieth policy years.

   b. For participating policies, add the terminal dividend payable upon surrender, if any, to the accumulation of the annual Cash Dividends at five percent interest compounded annually to the end of the period selected and add this sum to the amount determined in step a.

   c. Divide the result of step b. (step a. for [guaranteed-cost] nonparticipating policies) by an interest factor that converts it into an equivalent level annual amount that, if paid at the beginning of each year, would accrue to the value in step b. (step a. for [guaranteed cost] nonparticipating policies) over the respective periods stipulated in step a. If the period is ten years, the factor is 13.207 and if the period is twenty years, the factor is 34.719.

   d. Determine the equivalent level premium by accumulating each annual premium payable for the basic policy or rider att five percent interest compounded annually to the end of the period stipulated in step a. and dividing the result by the respective factors stated in step c. ([t] This amount is the annual premium payable for a level premium plan).

   e. Subtract the result of step c. from step d.

   f. Divide the result of step e. by the number of thousands of the Equivalent Level Death Benefit to arrive at the [Life Insurance] Surrender Cost Comparison Index.

2. [Life Insurance] Net Payment Cost Comparison Index. The [Life Insurance] Net Payment Cost Comparison Index is calculated in the same manner as the comparable [Life Insurance] Surrender Cost Comparison Index except that the cash surrender value and any terminal dividend are set at zero.

COMMENT: *The revisions in these two subsections are editorial. One set of revisions changes the names of the indexes. The modifier "Life Insurance" has been deleted because it is redundant. The modifier "Comparison" has been added to emphasize that the indexes measure only relative, not absolute, costs. The other set of revisions accommodate flexible premium-flexible benefit policies by replacing the term "guaranteed-cost" with the term "nonparticipating."*

3. In the calculation of Cost Comparison Indexes for policies that have a Nonguaranteed Factor, the amount payable upon death for purposes of Section 4(G)1, the cash surrender value for the purposes of Section 4(J)1.a., and the annual premium for the purposes of Section 4(J)1.d. are calculated on the basis of the company's Current Rate Schedule.

COMMENT: *The purpose of this revision is to state that, for purposes of calculating the Equivalent Level Death Benefit and the Cost Comparison Indexes, the values used should be those currently illustrated for that policy.*

(K) Nonguaranteed Factor. A Nonguaranteed Factor is any premium, benefit, or other item entering into the calculation of the Surrender Cost Comparison Index that can be changed by the company without the consent of the policyowner.

COMMENT: *The policy factors included are the cash surrender value, the terminal dividend payable on surrender, the annual premium, and the amount payable on death.*

(L) Nonguaranteed Element. The Nonguaranteed Element is calculated by subtracting (a) the Surrender Cost Comparison Indexes for ten- and twenty-year periods, calculated as described in (J) above, from (b) the corresponding Surrender Cost Comparison Indexes for ten- and twenty-year periods calculated on the assumption that the company charges the maximum premiums and provides the minimum cash values and death benefits allowed by the policy, and, if the policy is participating, pays no dividends.

SOURCE: I 1982 NAIC PROC. 394-411, 400, 404.

COMMENT: The Nonguaranteed element represents the difference between the surrender cost index determined on the highest-possible-cost basis and the surrender cost index calculated on the currently illustrated basis. The result is a relative indication of how must of a policy's cost is not guaranteed.

(M) Policy Data. The Policy Data is a display or schedule of numerical values, both guaranteed and nonguaranteed, for each policy year for a series of designated policy years, of the following information: illustrated annual, other periodic, and terminal dividends; premiums; death benefits; cash surrender values; and endowment benefits.

SOURCE: II 1981 NAIC Proc. 739-60, 754.

COMMENT: The definition appears in the June 1981 report of the (C3) Task Force on Manipulation, Lapsation, Dividend Practices, and Annuity Disclosure. The purpose of the definition is to provide a shorthand way to refer to those policy values which must be disclosed to any existing or prospective policyholders who request it. Refer to subsections 5(A)(2) and to 5(C)(1).

[G] (N) Policy Summary. [For the purposes of this regulation,] The Policy Summary [means] is a written statement describing the elements of the policy, including, but not limited to:

1. A prominently placed title as follows: STATEMENT OF POLICY COST AND BENEFIT INFORMATION.

2. The name and address of the insurance agent[,] or, if no agent is involved, a statement of the procedure to be followed in order to receive responses to inquiries regarding the Policy Summary.

3. The full name and home office or administrative office address of the company in which the life insurance policy is to be or has been written.

4. The Generic Name of the basic policy and each rider.

5. The following amounts, where applicable, for the first five policy years and representarive policy years thereafter sufficient to clearly illustrate the premium and benefit patterns, including, but not necessarily limited to, the years for which [Life Insurance] Cost Comparison Indexes are displayed and the earlier of at least one age from sixty through sixty-five [or] and policy maturity [whichever is earlier] :

   a. The annual premium for the basic policy.

   b. The annual premium for each oprional rider.

   c. The [Guaranteed] amount payable upon death, at the beginning of the policy year regardless of the cause of death, other than suicide[,] or other specifically enumerated exclusions, which is provided by the basic policy and each optional rider, with benefits provided under the basic policy and each rider shown separately.

   d. The total [guaranteed] cash surrender values at the end of the year with values shown separately for the basic policy and each rider.

   e. The Cash Dividends payable at the end of the year with values shown separately for the basic policy and each rider. (Dividends need not be displayed beyond the twentieth policy year.)

   f. Any [Guaranteed] endowment amounts payable under the policy which are not included under [guaranteed] cash surrender values above.

COMMENT: These are editorial changes to conform the form of this subsection to other usages in this draft.

   g. If the policy has a Nonguaranteed Factor, the maximum premium, minimum amount payable upon death, minimum cash value, and minimum endowment amounts allowed by the policy. These amounts may be shown in addition on the basis of the company's Current Rate Schedule and Current Dividend Scale.

COMMENT: *The amounts that are described just above, in subsections 4(N)(5)(a)-(f), are the illustrated or current amounts payable. This section requires the insurer to show those same amounts, according to the contract's guarantee, so that a consumer has readily available information about the maximum premium and minimum benefits.*

6. The effective policy loan annual percentage interest rate, if the policy contains this provision, specifying whether this rate is applied in advance or in arrears. If the policy loan interest rate is [variable] adjustable, the Policy Summary [includes the maximum annual percentage rate.] shall also indicate that the annual percentage rate will be determined by the company in accordance with the provisions of the policy and the applicable law.

SOURCE: *See I 1981 NAIC PROC. 535-6 (text of the NAIC Model Policy Loan Interest Rate Bill).*

COMMENT: *Changing the term "variable" to "adjustable" conforms this section to the language in the NAIC Model Policy Loan Interest Rate Bill. Under that Model, now adopted in about two-thirds of the states, the maximum rate can be indexed and can change during the period the loan is outstanding. Therefore the phrase requiring the Policy Summary to include the maximum annual percentage rate is obsolete and has been deleted. A provision has been added that would require the Policy Summary to put the policyowner on notice that the rate may change. Section 3(e) of the Model Policy Loan Interest Rate Bill contains further requirements for notifying a borrowing policyholder of the effective rate.*

7. The [Life Insurance] Cost Comparsion Indexes for ten and twenty years but in no case beyond the premium-paying period. Separate indexes [are] shall be displayed for the basic policy and for each optional term life insurance rider. Such indexes need not be included for optional riders which are limited to benefits, such as accidental death benefits, disability waiver of premium, preliminary rerm life insurance coverage of less than [12] twelve months and guaranteed insurability benefits, nor for [the] any basic policies or optional riders covering more than one life.

COMMENT: *These changes are editorial.*

8. [The Equivalent Level Annual Dividend, in the case of participating policies and participating optional term life insurance riders,] If the policy has a Nonguaranteed Factor:

   a. The Nonguaranteed Element under the same circumstances and for the same durations at which the [Life Insurance] Surrender Cost Comparison Indexes are displayed. The Policy Summary may include in addition a Nonguaranteed Element calculated assuming all cash surrender values and terminal dividends to be zero.

[9. A Policy Summary which includes dividends shall also include a sratement that dividends are based on the company's current dividend scale and are not guaranteed in addition to a statement in close proximity to the Equivalent Level Annual Dividend as follows: An explanation of the intended use of the Equivalent Level Annual Dividend is included in the Life Insurance Buyer's Guide.]

   b. A statement indicating which cost factor is not guaranteed and that such factor is based on the company's Current Dividend Scale or Current Rate Schedule.

   c. This statement in close proximity to the Nonguaranteed Element: "An explanation of the intended use of the Nonguaranteed Element is included in the Life Insurance Buyer's Guide."

COMMENT: *The purpose of these changes are to eliminate reference to the Equivalent Level Annual Dividend and to incorporate instead an instruction that its successor, the Nonguaranteed Element, be included on the Policy Summary. Note that the insurer is required also to inform the policyowner on the Policy Summary exactly which factors may be changed without his or her consent.*

[10.] 9. [A] This statement in close proximity to the [Life Insurance] Cost Comparison Indexes [as follows]: "An explanation of the intended use of these indexes is provided in the Life Insurance Buyer's Guide."

[11.] 10. The date on which the Policy Summary is prepared. The Policy Summary must consist of a separate document. All information required to be disclosed must be set out in such a manner as to not minimize or render any portion thereof obscure. Any amounts which remain level for two or more years of the policy may be represented by a single number if it is clearly indicated what amounts are applicable for each policy year. Amounts in item 5 of this section shall be listed in total, not on a per thousand nor per unit basis. If more than one insured is covered under one policy or rider, [guaranteed] death benefits shall be displayed separately for each insured or for each class of insureds if death benefits do not differ within the class. Zero amounts shall be displayed [as zero and shall not be displayed] as a blank space.

COMMENT: *All but one of these changes are editorial. The substantive revision would allow the Policy Summary to exhibit zero amounts as a blank space.*

(O) Portfolio Average Method. The Portfolio Average Method is the method of determining dividends so that, except for the effect of policy loans, dividends reflect investment earnings on funds attributable to all policies whenever issued.

SOURCE: *II 1981 NAIC PROC. 755-56 (text of the Advisory Committee's Report to the (C3) Task Force on Manipulation, Lapsation, Dividend Practices, and Annuity Disclosure); id. at 738 (text of the American Academy of Actuaries' Report on Dividend Principles and Practices to the same (C3) Task Force).*

COMMENT: *This definition should be read together with subsection 4(I), which is the definition of the Investment Generation method of allocating investment income. The operative sections using these definitions are 5(B) (2), 5(B) (3), 5(B) (4), 5(C) (2)(b), and 5(C) (2)(c). These sections apply to existing and newly issued participating policies of a mutual life insurer. They implement the disclosure of dividend practices recommended both by the American Academy of Actuaries and the NAIC's Advisory Committee on Manipulation.*

(P) Yearly Price of Death Benefits. The Yearly Price of Death Benefits per $1,000 is calculated by applying the following formula:

YP = (P-Dv-(CVCv-CVP))/(F(.001)

Where YP = Yearly Price of Death Benefits per $1,000
P = Annual premium
CVP = Sum of the cash value and terminal dividend at the end of the preceding year
CVC = Sum of the cash value and terminal dividend at the end of the current year
D = Annual dividend
F = Face amount
V = 1/(1.05)

SOURCE: *II 1981 NAIC PROC. at 755 (text of the Report of the Advisory Committee on Manipulation to the (C3) Task Force on Manipulation, Lapsation, Dividend Practices, and Annuity Disclosure); II 1980 NAIC PROC. at 831-35, 838 (text of earlier Report of the same Advisory Committee).*

COMMENT: *This definition defines an amount used in the calculation of the Discontinuity Index (see section 4(F) above). The Yearly Price of Death Benefits has no other function in this proposed regulation.*

Section 5. [Disclosure Requirements.] Duties of Insurers.

COMMENT: *This change is intended to make the heading more descriptive of this section's content.*

(A) Requirements Applicable Generally.

[(A)] 1. The insurer shall provide, to all prospective purchasers, a Buyer's Guide and a Policy Summary prior to accepting the applicant's initial premium or premium deposit, provided however that:

a. [unless] If the policy for which application is made or its Policy Summary contains an unconditional refund provision of at least ten days [or unless the Policy Summary contains such an unconditional refund offer in which event], the Buyer's Guide and Policy Summary must be delivered with the policy or prior to delivery of the policy.

COMMENT: *These are editorial changes.*

[(C)] b. [In the case of policies whose] If the Equivalent Level Death Benefit of the policy for which application is made does not exceed $5,000, the requirement for providing a Policy Summary will be satisfied by delivery of a written statement containing the information described in Section 4[(G)] (N), items 2, 3, 4, 5a, 5b, 5c, 6, 7, 8, 9, and 10 [,11].

COMMENT: *The purpose of the change in the first three lines of subsection 5(A)(1)(b) is to clarify that the application of this provision is determined at the time of application. The balance of the changes require that a Nonguaranteed Element, if applicable, appear on the Policy Summary of such a policy and also accommodate the revised section designations.*

[(B) The insurer shall provide a Buyer's Guide and a Policy Summary to any prospective purchaser upon request.]

2. If any prospective purchaser requests a Buyer's Guide, a Policy Summary, or Policy Data, the insurer shall provide the item or material requested. Unless otherwise requested, the Policy Data shall be provided for policy years one through twenty.

SOURCE: *II 1981 NAIC PROC. at 755 (text of the Advisory Committee on Manipulation to the NAIC's (C3) Task Force on Manipulation, Lapsation, Dividend Practices, and Annuity Disclosure).*

COMMENT: *The substantive change in this provision is to require the insurer to provide certain policy data if the prospective insured requests it. That information is defined in subsection 4(M) as the premiums and benefits of the policy, shown on both a guaranteed and illustrated basis. If requested to provide such information, the insurer should provide it for the first twenty years of the contract unless the consumer requests it for a longer or shorter period. Through the Advisory Committee on Manipulation had recommended that the presumption be thirty years instead of twenty, the drafters felt that the administrative benefits of continuing the current presumption outweighed the costs of switching to the longer. Moreover, the provision allows the prospective policyholder to request Policy Data for a period of any duration.*

3. If the Discontinuity Index of any policy exceeds:

a. Any of the test limits for discontinuity set forth in Appendix C herein, the insurer shall, prior to the sale of any such policy, provide to the (title of supervisory authority) a statement identifying as accurately as possible the specific policy premium or benefit causing the policy's Discontinuity Index to exceed the test limits. Upon request of the (title of supervisory authority), the insurer shall also provide to the (title of supervisory authority) the Policy Data for policy years one through thirty, and the Discontinuity Index and its component calculations.

b. The test limit set forth in Appendix C herein for the applicant's issue age, the insurer shall provide:

i. The following statement displayed prominently on the Policy Summary and on all other sales material that show or incorporate the Surrender Cost Comparison Index, the Net Payment Cost Comparison Index, or the Nonguaranteed Element: "This policy has an unusual pattern of premiums or benefits that may make comparison with the cost indexes of other policies unreliable. You should discuss this with your agent or this company. A statement of year-by-year information is available."

ii. If the prospective purchaser requests it, a statement identifying as accurately as possible the specific policy premium or benefit causing the policy's Discontinuity Index to exceed the applicable test limit.

SOURCE: *II 1981 NAIC PROC. at 754 (text of the Report of the Advisory Committee on Manipulation to the NAIC's (C3) Task Force on Manipulation, Lapsation, Dividend Practices, and Annuity Disclosure); II 1980 NAIC PROC. at 831-40 (text of earlier Report of the same Advisory Committee).*

COMMENT: *The object of this provision is to make available to regulators and affected policyowners certain information about policies that seem to have an unrealistically attractive progression of costs or benefits without any acceptable rationale. (Refer to the definition of the term "Discontinuity Index" in subsection 4(F).) If a policy exceeds any of the test limits in Appendix C, the insurer must so inform the regulator before it can issue the policy. At the same time the insurer must tell the regulator in writing which premium or benefit is causing the policy to exceed the test limits. The regulator may request that the insurer also give him or her the Policy Data for policy years 1-30 as well as the Discontinuity Index itself and its component calculations.*

As an additional measure, if a policy as applied for exceeds the test limit for the applicant's particular age, then the company must put a warning on the Policy Summary. That warning must also appear on any sales material that contains any of the cost comparison indexes or the Nonguaranteed Element. If the applicant requests, the insurer must furnish an explanation.

(B) Requirements Applicable to Participating Policies Issued by Mutual Companies.

If a mutual life insurance company illustrates policyowner dividends that are calculated in a manner or on a basis that:

1. Deviates substantially from the Contribution Principle, the Policy summary and all other sales material showing illustrated policyowner dividends must display prominently the following statement: "The illustrated dividends for this policy have not been determined in accordance with the Contribution Principle. Contact this company for further information."

2. Uses the Portfolio Average Method, the Policy Summary and all other sales material showing illustrated policyowner dividends must include the following statement: "Illustrated dividends reflect current investment earnings on funds applicable to all policies and are based on the Current Dividend Scale. Refer to your Buyer's Guide for further information."

3. Uses the Investment General Method, the Policy Summary and all other sales material showing illustrated policyowner dividends must include the following statement: "Illustrated dividends reflect current investment earnings on funds attributable to policies issued since 19 – and are based on the current dividend scale. Refer to your Buyer's Guide for further information." ***Drafting note:** *Insert at * the earliest year of the issue-year grouping used to determine the investment earnings on currently issued policies.*

4. Uses any combination of the Portfolio Average Method and the Investment Generation Method, the Policy Summary and all other sales material showing illustrated policyowner dividends must include an appropriate statement, analagous to the statements required by Sections 5(B) 2 and 5(B) 3, indicating how current investment earnings are reflected in illustrated dividends.

SOURCE: *II 1981 NAIC PROC. at 754-56 (text of the Report of the Advisory Committee on Manipulation to the NAIC's (C3) Task Force on Manipulation, Lapsation, Dividend Practices, and Annuity Disclosure); Academy Report at 12-14; II 1981 NAIC PROC. at 738 (text of the Report of the American Academy of Actuaries Committee on Dividend Principles and Practices to the NAIC's (C3) Task Force on Manipulation, Lapsation, Dividend Practices, and Annuity Disclosure).*

COMMENT: *The requirements in this section apply only to policies newly issued by mutual companies. Parallel requirements for existing policies issued by mutual companies appear in the following subsection. There are currently no principles governing the dividend practices of participating policies issued by stock companies. Consequently these proposed revisions contain no requirements applicable to stocks' participating policies. The American Academy of Actuaries will be completing its work on how dividends should be determined for those policies. Those principles could be incorporated into this regulation at that time.*

Basically this section requires most mutuals to tell prospective policyholders and applicants something about how investment income is allocated. The reason that disclosure is important is that the method of allocating investment income affects the comparability of dividend illustrations. For example, "when recent investment rates exceed portfolio average rates, it would be expected that a lower cost than one using a portfolio average method. The reverse of this cost relationship would occur when recent investment rates are lower than portfolio average rates." Academy Report at 14. Disclosure of the method of investment income allocation is also important because dividends paid on the basis of new money rates are likely to be more volatile than those paid on the basis of an average rate.

The section also requires mutuals to tell prospective policyowners or applicants if their illustrated dividends are not calculated in accordance with the Contribution Principle. If the mutual uses the Contribution Principle, no disclosure of that is required since its use is generally accepted practice. Academy Report at 18. The Principle itself is defined in subsection 4(C).

(C) Requirements Applicable to Existing Policies

1. If a policyowner residing in this state requests it, the insurer shall provide Policy Data for that policy. Unless otherwise requested, the Policy Data shall be provided for twenty consecutive years beginning with the previous policy anniversary. The statement of Policy Data shall include cash dividends according to the Current Dividend Scale, the amount of outstanding policy loans, and the current policy loan interest rate. Policy values shown shall be based on the dividend option in effect at the time of the request. The insurer may charge a reasonable fee, not to exceed $-, for the preparation of the statement.

2. If a mutual life insurance company:

   a. Deviates substantially from the Contribution Principle, it shall annually advise each affected policyowner residing in this state that the dividend paid that year was not determined in accordance with the Contribution Principle and that the policyowner may contact the company for further information.

   b. Is determining dividends, as of the effective date of this regulation, using the Investment Generation Method, it shall, within eighteen months of such date, advise each affected policyowner residing in this state that the dividend for the policy reflects current investment earnings on funds applicable to policies issued from 19* through 19*. This requirement shall not apply to policies for which the amount payable upon death under the basic policy as of the date when advice would otherwise be required does not exceed $5,000. ***Drafting Note:** *Insert at * the applicable years of issue.*

   c. Changes its method of determining dividend scales on existing policies from or to the Investment Generation Method, it shall, no later than when the first dividend is payable on the new basis, advise each affected policyowner residing in this state of this change and of its implication on dividends payable on affected policies. This requirement shall not apply to policies for which the amount payable upon death under the basic policy as of the date when advice would otherwise be required does not exceed $5,000.

SOURCE: II 1981 NAIC PROC. at 756 (text of the Report of the Advisory Committee on Manipulation to the NAIC's (C3) Task Force on Manipulation, Lapsation, Dividend Practices, and Annuity Disclosure).

COMMENT: This section imposes one additional type of disclosure on all insurers. That is to provide current information about his or her policy to any existing insured who asks for it. As in subsection 5(A)(2), the drafters chose to assume, as a matter of administrative practicality, that unless the insured requested otherwise the information would be furnished for a period of 20 years. It is important to note that the Policy Data would be based on the company's then-current assumptions and on the particular options chosen by the insured. Also note that the insurer is allowed to charge a reasonable fee for this service, but this draft does not specify the amount of that fee.

Subsection 5(C)(2), like subsection 5(B), applies only to mutual insurers. First, any mutual that does not comply with the Contribution Principle must so advise each affected policyowner who resides in any state where this regulation is effective. The mutual must do that in each year that the dividend paid did in fact deviate. Second, if a mutual is using the Investment Generation Method to allocate investment income as of the effective date of this proposed regulation, then it must so notify each affected policyowner who resides in any state where this regulation is effective. The mutual has 18 months to provide that notice. Finally, if the mutual changes its method of allocating dividends from or to the Investment Generation Method after the effective date of this regulation, then it must tell those policyowners. It must tell them how the change will affect their dividends to later than when the first dividend is payable on the new basis.

Please note that the last two requirements, subsections 5(C)(2)(b) and (c), which require a mutual to advise its existing policyowners about its method of investment income allocation, do not apply to policies with a face amount of $5,000 or less. The drafters felt such requirements were not cost-effective for such small policies. The provision requiring notification of deviation from the Contribution Principle would, of course, apply.

Section 6. Special Plans. This section modifies the application of this regulation as indicated for certain special plans of life insurance:

COMMENT: Since the NAIC adopted the current regulation in 1976, a number of new types of policies have been designed. Application of the current regulation to those policies has been uncertain and perhaps nonuniform. This section is intended to make that application clear and consistent.

(A) Enhanced Ordinary Life Policies. An Enhanced Ordinary Life Policy is a participating policy which has the following characreristics for all issue ages:

1. The basic policy has a guaranteed death benefit that reduces after an initial period of one or more years to a basic amount; and

2. A special dividend option that provides (a) a combination of immediate paid-up additions and one-year term insurance or (b) deferred paid-up additions, either of which on the basis of the Current Dividend Scale will provide a combined death benefit (reduced basic amount plus paid-up additions plus one-year term insurance) at least equal to the initial face amount.

For these policies:

1. The cash value of benefits purchased by dividends payable on or before the crossover point is included in the cash surrender value for the purpose of Section 4(J) 1.a.

2. The death benefit purchased by dividends payable on or before the crossover point is included in the amount payable upon death for the purpose of Section 4(G) 1.

3. Dividends payable after the crossover point are assumed to be paid in cash for the purpose of Section 4(J) 1.b.

SOURCE: I 1982 NAIC PROC. at 400, 405-06 (text of the Statement of the American Council of Life Insurance to the NAIC's (A) Committee's Task Force on Life Insurance Cost Disclosure).

COMMENT: In calculating the relative cost indexes and the Nonguaranteed Element, dividends credited on or before the crossover point are applied under the dividend option that produces the level death benefit. Thus those indexes are not reduced by dividends due on or before that point, but the cash values and death benefits that the dividends purchased are taken into account.

After the crossover point, the calculations of the relative cost indexes and the Nonguaranteed Element assume that dividends are used to reduce premiums since the level death benefit that this approach produces is usually the basic on which the policy is bought.

(B) Flexible Premium and Benefit Policies. For policies, commonly called "universal life insurance policies," which:

1. Permit the policyowner to vary, independently of each other, the amount or timing of premium payments, or the amount payable on death; and

2. Provide for a cash value that is based on separately identified interest credits and mortality and expense charges made to the policy:

All indexes and other data shall be displayed assuming specific schedules of anticipared premiums and death benefits at issue.

In addition to all other information required by this regulation, the Policy Summary shall indicate when the policy will expire based on the interest rates and mortality and other charges guaranteed in the policy and the anticipated or assumed annual premiums shown in the Policy Summary.

COMMENT: *The drafters declined to specify the schedules of premiums and benefits to be assumed in calculating relative cost indexes for these policies. They felt that the specific schedule that the applicant desired was a much more appropriate and more useful assumption. These assumptions should, of course, be stated on any display. The nonguaranteed Element would be calculated using that schedule and the policy's guaranteed values. Note that this section also requires that the Policy Summary must indicate when the policy will expire based on those guarantees and the assumed premium schedule.*

(C) Multitrack Policies. For policies which allow a policyowner to change or convert the policy from one plan or amount to another, the Policy Summary:

1. Shall display all indexes and other data assuming that the option is not exercised; and

2. May display all indexes and other data using a stated assumption abour the exercise of the option.

COMMENT: *An example of the type of policy subject to this subsection is adjustable life.*

(D) Policies with Any Rate Subject to Continued Insurability. For policies which allow a policyowner a reduced premium rate if the insured periodically submits evidence of continued insurabiliry, the Policy Summary;

1. Shall display cost indexes and other data assuming that the insured always qualifies for the lowest premium;

2. Shall display cost indexes and other data assuming rhat the company always charges the highest premiums allowable; and

3. Shall indicate the conditions thar must be fulfilled for an insured to qualify periodically for the reduced rate.

SOURCE: *I 1982 NAIC PROC. at 401, 406 (text of the Statement of the American Council of Life Insurance to the NAIC's (A) Committee's Task Force on Life Insurance Cost Disclosure).*

COMMENT: *These are commonly known as revertible term policies. The drafters recommended this approach because the cost is not completely under the insured's control. The cost can be affected by changes in the insured's health and the insurer's underwriting standards. Disclosure of the Nonguaranteed Element would be required if any factor is not guaranteed.*

(E) For all other special plans of life insurance, an insurer shall provide or deliver both a Policy Summary substantially similar to that described in Section 4(N) and a Buyer's Guide. Use of those materials shall be deemed to be substantial compliance with this regulation unless the (title of supervisory authority) makes a finding that such disclosure materials misrepresent a material term or condition of the contract or omit a material fact.

COMMENT: *This subsection makes this proposed regulation able to accommodate new product designs. It requires an insurer selling a policy that meets none of the definitions contained in this regulation to deliver or provide a Policy Summary that is substantially similar to that otherwise required by this regulation. An insurer using such a Policy Summary can assume that it is in substantial compliance with this proposed regulation until the commissioner makes a finding that the Summary misrepresents a material term or condition of the contract or omits a material fact.*

Section 7 [6]. General Rules.

(A) Each insurer shall maintain, at its home office or principal office, a complete file containing one copy of each document authorized and used by the insurer [for use] pursuant to this regulation. Such file shall contain one copy of each authorized form for a period of three years following the date of its last authorized use.

COMMENT: The purpose of this proposed revision is to clarify that the insurer must keep a copy of each document both filed and used.

(B) An agent shall inform the prospective purchaser, prior to commencing a life insurance sales presentation, that he or she is acting as a life insurance agent and inform the prospective purchaser of the full name of the insurance company which [he] the agent is representing to the buyer. In sales situations in which an agent is not involved, the insurer shall identify its full name.

COMMENT: The purpose of this proposed revision is to eliminate a gender-specific reference.

(C) Terms such as financial planner, investment advisor, financial consultant, or financial conseling shall not be used in such a way as to imply that the insurance agent is primarily [generally] engaged in an advisory business in which compensation is unrelated to sales unless such is actually the case.

COMMENT: The purpose of this proposed revision is to clarify what an agent may not do: No agent may imply that his primary business is noncommissioned unless that is true.

(D) Any reference to a [policy] dividend[s] or other Nonguaranteed Factor must include a statement that such item is [dividends are] not guaranteed[.] and is based on the company's Current Dividend Scale or Current Rate Schedule.

COMMENT: The purpose of this proposed revision is to broaden the scope of this provision. All policy cost factors that are not guaranteed must be so designated.

(E) A system or presentation which does not recognize the time value of money through the use of appropriate interest adjustments shall not be used for comparing the cost of two or more life insurance policies. Such a system may be used for the purpose of demonstrating the cash-flow pattern of a policy if such presenration is accompanied by a statement disclosing that the presentation does not recognize that, because of interest, a dollar in the future has less value than a dollar today.

(F) A presentation of costs or benefits, other than rhat required pursuant to this regulation, shall not display guaranteed and nonguaranteed factors [benefits] as a single sum unless they are shown separately in close proximity thereto.

(G) Any statement regarding the use of the [Life Insurance] Cost Comparison Indexes or Nonguaranteed Element shall include an explanation to the effect that the indexes or Nonguaranteed Element are useful only for the comparison of the relative costs of two or more similar policies.

(H) A [Life Insurance] Cost Comparison Index which reflects a Nonguaranteed Element [dividends or an Equivalent Level Annual Dividend] shall be accompanied by a statement that it is based on the company's [c] Current [d] Dividend [s] Scale or Current Rate Schedule and is not guaranteed.

COMMENT: The purpose of the revisions proposed in these subsections are to broaden their effect to conform them to the balance of the material in the proposed regulation.

[(I) For the purposes of this regulation, the annual premium for a basic policy or rider, for which the company reserves the right to change the premiums, shall be the maximum annual premium.]

COMMENT: The drafters propose to eliminate this provision since it is superseded by other provisions in this proposed regulation.

Section [7] 8. Failure to Comply.

Failure of an insurer to provide or deliver a Buyer's Guide, [or] a Policy Summary, or Policy Data as provided in Secrions 5 and 6 shall constitute an omission which misrepresents the benefits, advantages, conditions or terms of an insurance policy.

COMMENT: Subsections 5(A)(3) and 5(C)(1) require an insurer to deliver the Policy Data if an existing or prospective insured requests it. To make that requirement operative the phrase "or Policy Data" is inserted here. Likewise section 6 lists requirements applicable to special plans; that notation is included here to require insurers' compliance.

Section 9. Separability. If any provisions of this rule be held invalid, the remainder shall not be affected.

COMMENT: This is a standard provision usually added to administrative rules to protect nonoffending provisions.

Section [8] 10. Effective Date. This rule shall [apply to all solicitations of life insurance which commence on or after] became effective (insert a date at least six months following adoption by the regulatory authority.)

COMMENT: The drafters recommend that the rule be adopted with an effective date delayed at least six months.

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APPENDIX A

Life Insurance Buyer's Guide

The language in the Buyer's Guide is limited to that contained in the following pages of this Appendix, or to language approved by (title of supervisory authority). However, companies can vary the type style and format and are encouraged to enhance the readability, design, and attractiveness of the Buyer's Guide.

Life Insurance Buyer's Guide

This guide can help you get the most for your money when you shop for life insurance. It can help you answer questions about:

- Buying Life Insurance
- Deciding How Much You Need
- Choosing The Right Kind
- Finding a Low Cost Policy
- Things to Remember

Prepared by
National Association of
Insurance Commissioners

The National Association of Insurance Commissioners is an association of state insurance regulatory officials. This association helps the various Insurance Departments coordinate insurance laws for the benefit of all consumers.

YOU ARE URGED TO USE THIS GUIDE WHEN BUYING LIFE INSURANCE

This Guide Does Not Endorse Any Company or Policy

Reprinted by......

Buying Life Insurance

When you buy life insurance, you want coverage that fits your needs and doesn't cost too much.

First, decide how much you need — and for how long — and what you can afford to pay.

Next, find out what kinds of policies are available to meet your needs and pick the one that best suits you.

Then, find out what different companies charge for that kind of policy — for the amount of insurance you want. You can find important cost differences between life insurance policies by using *cost comparison indexes* as described in this guide.

It makes good sense to ask a life insurance agent or company to help you. An agent can be particularly useful in reviewing your insurance needs and in giving you information about the kinds of policies that are available. If one kind doesn't seem to fit your needs, ask about others.

This guide provides only basic information. You can get more facts from a life insurance agent or company or at your public library.

What About Your Present Policy? Think twice before dropping a life insurance policy you already have to buy a new one.

- It can be costly because much of what you paid in the early years of the policy you now have was used for the company's expense of selling and issuing the policy. This expense will be incurred again for a new policy.
- If you are older or your health has changed, premiums for the new policy will often be higher.

- You may have valuable rights and benefits in your present policy that are not in the new one.

- You might be able to change your present policy or even add to it to get the coverage or benefits you now want.

Check with the agent or company that issued your present policy — get both sides of the story. In any case, don't give up your present policy until you are covered by a new one.

How Much Do You Need?

To decide how much life insurance you need, figure out what your dependents would have if you were to die now, and what they would actually need. Your new policy should come as close to making up the difference as you can afford.

In figuring what you have, count your present insurance - including any group insurance where you work, social security or veteran's insurance. Add other assets you have - savings, investments, real estate, and personal property.

In figuring what you need, think ~~of income for~~ your dependents - for family living expenses, educational costs and any other future needs. Think also of cash needs - for the expenses of a final illness and for paying taxes, mortgages or other debts.

What Is The Right Kind?

All life insurance policies agree to pay an amount of money when you die. But all policies are not the same. Some provide permanent coverage and others temporary coverage. Some build up cash values and others do not. Some policies combine different kinds of insurance,

and others let you change from one kind of insurance to another. Your choice should be based on your needs and what you can afford.

A wide variety of plans is being offered today. Here is a brief description of two basic kinds - term and whole life - and some combinations and variations. You can get detailed information from a life insurance agent or company.

Term Insurance covers you for a *term* of one or more years. It pays a death benefit only if you die in that term. Term insurance generally provides the largest immediate death protection for your premium dollar.

Most term insurance policies are *renewable* for one or more additional terms, even if your health has changed. Each time you renew the policy for a new term, premiums will be higher. Check the premiums at older ages and how long the policy can be continued.

Many term insurance policies can be traded before the end of a *conversion period* for a whole life policy - even if you are not in good health. Premiums for the new policy will be higher than you have been paying for the term insurance.

Whole Life Insurance covers you for as long as you live. The most common type is called *straight life* or *ordinary life* insurance - you pay the same premiums for as long as you live. These premiums can be several times higher than you would pay at first for the same amount of term insurance. But they are smaller than the premiums you would eventually pay if you were to keep renewing a term policy until your later years.

Some whole life policies let you pay premiums for a shorter period such as 20 years, or until age 65. Premiums for these policies are higher than for ordinary life insurance since the premium payments are squeezed into a shorter period.

Whole life policies develop cash values. If you stop paying premiums, you can take the cash — or you can use the cash value to buy continuing insurance protection for a limited time or a reduced amount. (Some term policies that provide coverage for a long period also have cash values.)

You may borrow against the cash values by taking a policy loan. Any loan and interest on the loan that you do not pay back will be deducted from the benefits if you die, or from the cash value if you stop paying premiums.

Combinations and Variations. You can combine different kinds of insurance. For example, you can buy whole life insurance for lifetime coverage and add term insurance for the period of your greatest insurance need. Usually the term insurance is on your life - but it can also be bought for your spouse or children.

Endowment insurance policies pay a sum or income to you if you live to a certain age. If you die before then, the death benefit is paid to the person you named as beneficiary.

Other policies may have special features which allow flexibility as to premiums and coverage. Some let you choose the death benefit you want and the premium amount you can pay. The kind of insurance and coverage period are determined by these choices.

One kind of flexible premium policy, often called *universal life*, lets you vary your premium payments every year, and even skip a payment if you wish. The premiums you pay (less expense charges) go into a policy account that earns

interest, and charges for the insurance are deducted from the account. Here, insurance continues as long as there is enough money in the account to pay the insurance charges.

Finding a Low Cost Policy

After you have decided which kind of life insurance is best for you, compare similar policies from different companies to find which one is likely to give you the best value for your money. A simple comparison of the premiums is not enough. There are other things to consider. For example:

- Do premiums or benefits vary from year to year?
- How much cash value builds up under the policy?
- What part of the premiums or benefits is not guaranteed?
- What is the effect of interest on money paid and received at different times on the policy?

Cost Comparison Index numbers, which you get from life insurance agents or companies, take these sorts of items into account and can point the way to better buys.

Cost Comparison Indexes. There are two types of cost comparison index numbers. Both assume you will live and pay premiums for the next 10 or 20 years.

1. The *Surrender Cost Comparison Index* helps you compare costs over a 10 or 20 year period assuming you give up (surrender) the policy and take its cash value at the end of the period. It is useful if you consider the

level of cash values to be of special importance to you.

2. The *Net Payment Cost Comparison Index* helps you compare costs over a 10 or 20 year period assuming you will continue to pay premiums on your policy and do not take its cash value. It is useful if your main concern is the benefits that are to be paid at your death.

The two index numbers are the same for a policy without cash values.

Nonguaranteed Element. Many policies have a *nonguaranteed element* — some because they pay dividends and others because the company has the right to change premiums or benefits from time to time. In these cases, the index numbers are based on the company's current scale of dividends, premiums or benefits. These scales can be changed after the policy is issued, so that the actual dividends, premiums or benefits over the years can be higher or lower than those assumed in the indexes. The *nonguaranteed element* tells you how much higher the *Surrender Cost Comparison Index* would be if it were calculated using only guaranteed numbers.

Some policies do not have a *nonguaranteed element* at all. They are called *guaranteed cost* or *fixed cost* policies. This means that the premiums and benefits are fixed at the time you buy the policy and will not change.

Using Cost Comparison Indexes. The most important thing to remember is that a policy with smaller index numbers is generally a better buy than a similar policy with larger index numbers.

Compare index numbers only for similar policies - those which provide essentially the same benefits, with premiums payable for the same length of time. Make sure they are for your age,

and for the kind of policy and amount you intend to buy. Remember that no one company offers the lowest cost at all ages for all kinds and amounts of insurance.

Small differences in index numbers should be disregarded, particularly where there is a *nonguaranteed element*. Also, small differences could easily be offset by other policy features, or differences in the quality of service from the agent or company. When you find small differences in the indexes, your choice should be based on something other than cost.

Finally, keep in mind that index numbers cannot tell you the whole story. You should also consider:

- The pattern of policy benefits. Some policies have low cash values in the early years that build rapidly later on. Other policies have a more level cash value build-up. A year-by-year display of values and benefits can be very helpful. (The agent or company will give you a Policy Summary that will show benefits and premiums for selected years.)

- Any special policy features that may be particularly suited to your needs.

- The methods by which nonguaranteed values are calculated. For example, interest rates are an important factor in determining policy dividends. In some companies dividends reflect the average interest earnings on all policies whenever issued. In others, the dividends for policies issued in a recent year, or a group of years, reflect the interest earnings on those policies; in this case, dividends are likely to change more rapidly when interest rates change.

Things to Remember

- Review your particular insurance needs and circumstances. Choose the kind of policy with benefits that most closely fit your needs: Ask an agent or company to help you.

- Be sure that the premiums are within your ability to pay. Don't look only at the initial premium, but take account of any later premium increase.

- Ask about cost comparison index numbers and check several companies which offer similar policies. Remember, smaller index numbers generally represent a better buy.

- Don't buy life insurance unless you intend to stick with it. It can be very costly if you quit during the early years of the policy.

- Read your policy carefully. Ask your agent or company about anything that is not clear to you.

- Review your life insurance program with your agent or company every few years to keep up with changes in your income and your needs.

APPENDIX B

Examples of Calculations of the Discontinuity Index

Example 1

The first example is a participating whole life policy issued to a male aged 35. The calculation is made on a per $1,000 basis:

		Illustrated		
Policy Year	Guaranteed Cash Value	Annual Dividend	Terminal Dividend	Premium
1	0.0	0.0	0.00	21.40
2	8.77	2.40	0.00	21.40
3	31.27	2.65	0.00	21.40
4	54.28	2.90	0.00	21.40
5	77.82	3.16	0.00	21.40
6	94.24	3.16	0.00	21.40
7	110.93	3.16	0.00	21.40
8	127.88	3.41	0.00	21.40
9	145.09	3.41	0.00	21.40
10	162.54	3.66	8.00	21.40
11	180.22	4.16	8.00	21.40
12	198.11	4.67	8.00	21.40
13	216.20	5.17	8.00	21.40
14	234.46	5.68	8.00	21.40
15	252.88	6.18	8.00	21.40
16	271.43	6.69	8.00	21.40
17	290.10	7.19	8.00	21.40
18	308.87	7.95	8.00	21.40
19	327.73	8.46	8.00	21.40
20	346.65	9.47	25.00	21.40
21	365.62	10.48	25.00	21.40
22	384.60	11.49	25.00	21.40
23	403.57	12.50	25.00	21.40
24	422.50	13.51	25.00	21.40
25	441.37	14.52	25.00	21.40
26	460.14	15.53	25.00	21.40
27	478.78	16.54	25.00	21.40
28	497.28	17.55	25.00	21.40
29	515.60	18.56	25.00	21.40
30	533.70	19.57	25.00	21.40

The yearly prices, (backward) second differences in yearly prices, and their squares for this policy are:

Policy Year	(1) Yearly Price	(2) Second Difference in Yearly Price	(3) Second Difference Squared
1	21.40	–	NA
2	10.76	–	NA
3	-2.13	-2.25	NA
4	-1.79	13.23	NA
5	-1.44	.01	NA
6	6.46	7.55	NA
7	6.98	-7.38	NA
8	7.29	-.21	.0441
9	7.85	.25	.0625
10	.59	-7.82	61.1524
11	8.72	15.39	236.8521
12	8.88	-7.97	63.5209
13	9.06	.02	.0004
14	9.28	.04	.0016
15	9.52	.02	.0004
16	9.78	.02	.0004
17	10.08	.04	.0016
18	10.15	-.23	.0529
19	10.47	.25	.0625
20	-5.84	-16.63	276.5569
21	11.05	33.20	1,102.2400
22	10.98	-16.96	287.6416
23	10.93	.02	.0004
24	10.91	.03	NA
25	10.91	.02	NA
26	10.94	.03	NA
27	11.00	.03	NA
28	11.06	.00	NA
29	11.15	.03	NA
30	11.27	.03	NA

The column (1) yearly prices are the values of the Yearly Price of Death Benefits per (1000).

Column (2) is calculated by subtracting the change observed in the yearly price in year c-1 from rhe change observed in the yearly price in year t. For example, the second difference of -16.63 in year 10 is calculated:

$$-16.63 = (-5.84-10.47) - (10.47-10.15)$$

$$= -16.31-.32$$

$$= -16.63$$

Column (3), second difference spuared, is the square of the figure in column (2). The sum of the squared second differences between years 8 and 23 is 2028. This sum exceeds by 1528 the test limit for issue age 35 of 500.

The second example is a guaranteed cost policy issued to a male age 25. It has a six percent policy loan rate. The calculation is made on a per $1,000 basis.

Example 2

Policy Year	Guaranteed Cash Value	Illustrated Annual Dividend	Illustrated Terminal Dividend	Premium
1	0.0	0.0	0.0	11.34
2	0.0	0.0	0.0	11.34
3	0.02	0.0	0.0	11.34
4	9.77	0.0	0.0	11.34
5	19.84	0.0	0.0	11.34
6	30.23	0.0	0.0	11.34
7	40.95	0.0	0.0	11.34
8	52.01	0.0	0.0	11.34
9	63.41	0.0	0.0	11.34
10	75.17	0.0	0.0	11.34
11	87.27	0.0	0.0	11.34
12	99.71	0.0	0.0	11.34
13	112.48	0.0	0.0	11.34
14	125.54	0.0	0.0	11.34
15	138.90	0.0	0.0	11.34
16	152.53	0.0	0.0	11.34
17	166.43	0.0	0.0	11.34
18	180.59	0.0	0.0	11.34
19	195.03	0.0	0.0	11.34
20	224.12	0.0	0.0	11.34
21	230.80	0.0	0.0	11.34
22	253.71	0.0	0.0	11.34
23	268.85	0.0	0.0	11.34
24	284.20	0.0	0.0	11.34
25	299.73	0.0	0.0	11.34
26	315.43	0.0	0.0	11.34
27	331.29	0.0	0.0	11.34
28	347.29	0.0	0.0	11.34
29	363.43	0.0	0.0	11.34
30	379.67	0.0	0.0	11.34

Policy Year	(1) Yearly Price	(2) Second Difference in Yearly Price	(3) Second Difference Squared
1	11.34	–	NA
2	11.34	–	NA
3	11.32	-.02	NA
4	2.06	-9.24	NA
5	2.21	9.41	NA
6	2.33	.03	NA
7	2.57	.00	NA
8	2.76	.01	.0001
9	2.96	.01	.0001
10	3.16	.00	.0000
11	3.40	.04	.0016
12	3.65	.01	.0001
13	3.93	.03	.0009
14	4.26	.05	.0025
15	4.59	.00	.0000
16	4.97	.05	.0025
17	5.37	.02	.0004
18	5.78	.01	.0001
19	6.19	.00	.0000
20	-7.08	-17.68	187.1424
21	15.65	36.00	1,296.0000
22	.51	-37.87	1,434.1369
23	9.00	23.63	558.3769
24	9.52	-7.97	NA
25	10.08	.04	NA
26	10.66	.02	NA
27	11.26	.02	NA
28	11.88	.02	NA
29	12.51	.01	NA
30	13.18	.04	NA

The sum of the squared second differences between years 8 and 23 for example two is 3476. It exceeds by 3176 the test limit for issue age 25 of 300.

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APPENDIX C

Test Limits for Discontinuity

Drafting Note: *The test limits for discontinuity contained in this Appendix were developed by the NAIC Advisory Committee on Manipulation to be applicable to the traditional type of whole life policy. Corresponding test limits need to be developed for other plans. Also, further refinement in the test limits for issue ages over 45 appears necessary.*

Issue Age	Test Limit	Issue Age	Test Limit
25 and under	300	36	515
26	325	37	528
27	348	38	541
28	371	39	552
29	392	40	563
30	413	41	572
31	432	42	581
32	451	43	588
33	468	44	595
34	485	45 and over	600
35	500		

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ATTACHMENT ONE-B

Suggested Revisions to Buyers Guide (ACLD Redraft)

R. Seiler
Allstate Life

What Is Cost?

"Cost" is the difference between what you pay and what you get back. If you pay premium for life insurance and get nothing back, your cost for the death protection is the premium. If you pay a premium and get something back later on, such as a cash value, your cost is smaller than the premium.

For some policies all of the cost elements are guaranteed. These are called "guaranteed cost" or "fixed cost" policies. For many policies there is a nonguaranteed cost element. See the paragraph entitled "Non-guaranteed Element" for a description of this element and its effect on "cost."

Notes: Insert above on p. 6 of revised guide just above the paragraph entitled "Cost Comparison Indexes."

Delete the last paragraph of the section "Non-Guaranteed Element" on p. 7 of the revised guide.

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