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BILL ANALYSIS

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House Bill 5050 (Substitute H-1 as passed by the House)
Sponsor: Representative David Robertson
House Committee: Insurance
Senate Committee: Banking and Financial Institutions

Date Completed: 10-16-03

CONTENT

The bill would amend the Standard Nonforfeiture Law for Individual Deferred Annuities, within the Insurance Code, to establish new requirements for the minimum nonforfeiture amount available under an annuity contract, beginning on January 1, 2005; and allow insurers to proceed under either the existing or the new regulations until that date. (The current nonforfeiture amount provides for a minimum interest rate of 1.5% until 2005, when it will revert to 3%. The proposed minimum nonforfeiture amount would include an interest rate that could not be less than 1% and would be calculated according to a five-year Treasury rate.) The bill also would require approval of the Commissioner of the Office of Financial and Insurance Services for an insurer to defer the payment of a cash surrender benefit.

Under the Law, the minimum values of any paid-up annuity, cash surrender, or death benefits available under an annuity contract must be based on minimum nonforfeiture amounts described in the Law, depending on whether a contract provides for flexible considerations (amounts paid by the investor), fixed scheduled considerations, or a single consideration. "Minimum nonforfeiture amount" refers to the accumulated value of an annuity contract; that is, accumulated payments, minus certain charges, such as prior withdrawals and loans, subject to the "minimum nonforfeiture rate", which is the minimum interest rate guarantee that an insurer may use to determine the minimum nonforfeiture amount.

Public Act 635 of 2002 amended the Law to lower the minimum nonforfeiture rate for individual deferred annuity contracts providing for flexible considerations, from 3% to 1.5% per year until 2005. Specifically, the minimum nonforfeiture amount, at any time at or before the commencement of annuity payments, must be "equal to an accumulation up to that time at a rate of interest of 1.5% per annum of net considerations...paid before that time", increased by any additional amounts credited by the company to the contract, and decreased by 1) prior withdrawals from or partial surrenders of the contract accumulated at an annual interest of 1.5% and 2) the amount of any indebtedness to the company on the contract. Under the current Law, the annual interest rate will return to 3.0% on January 1, 2005.

Under the bill, beginning on January 1, 2005, the rate of interest used in determining minimum nonforfeiture amounts would have to be "an annual rate of interest determined as the lesser of 3% per annum and the following...:

"(a) The 5-year constant maturity treasury rate reported by the federal reserve as of a date, or average over a period, rounded to the nearest ½0 of 1%, specified in the contract no longer than 15 months before the contract issue date or redetermination date under subdivision (d).
(b) Reduced by 125 basis points.
(c) Where the resulting interest rate is not less than 1%.

(d) The interest rate shall apply for an initial period and may be redetermined for additional periods. The redetermination date, basis, and period, if any, shall be stated in the contract..."

Under this formula, the following amounts, accumulated at rates of interest described above, would have to be deducted:

-- Prior withdrawals from or partial surrenders of the contract.
-- An annual contract charge of $50.
-- Any premium tax paid by the company for the contract.

Until January 1, 2005, insurers could choose to use either the existing or the proposed calculation of the minimum nonforfeiture amount. Beginning on that date, insurers would have to proceed under the new formula.

Under the bill, the "net consideration" for a given contract year used to define the minimum nonforfeiture amount would have to equal 87% of the gross considerations credited to the contract during that year. (Currently, the net consideration may not be less than zero and must equal the corresponding gross considerations credited to the contract during that contract year, less an annual contract charge of $30 and a collection charge of $1.25 per consideration credited to the contract during that year. As a rule, the percentages of net consideration must be 67% for the first contract year and 87.5% for each subsequent year.)

Under the Law, if a contract provides for a lump sum settlement at maturity or at any other time, that the company must pay a cash surrender benefit in place of any paid-up annuity benefit upon surrender of the contract before or when annuity payments begin. The company must reserve the right to defer the payment of the cash surrender benefit for six months after demand for the payment with surrender of the contract. Under the bill, the company would be permitted to reserve the right to defer payment for six months if it made a written request to the Commissioner, showing the necessity and equitability to all policyholders of the deferral, and the Commissioner gave written approval.

Currently, cash surrender benefits available before maturity may not be less than the present value as of the date of surrender of that portion of the maturity value of the paid-up annuity benefit arising from consideration paid before the time of surrender. Under the bill, this amount would be reduced by the amount appropriate to reflect any prior withdrawals from or partial surrenders of the contract. Currently, the present value must be calculated on the basis of an interest rate not more than 1% higher than the interest rate specified in the contract for accumulating the net consideration to determine the maturity value. Under the bill, this amount would be decreased by the amount of any indebtedness to the company on the contract, including interest due and accrued, and increased by any existing additional amounts credited by the company to the contract.

The bill would delete requirements for the calculation of minimum nonforfeiture amounts for contracts providing for fixed scheduled considerations, and for contracts providing for a single consideration.

MCL 500.4072 Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

The bill would have no fiscal impact on State or local government.

Fiscal Analyst: Maria Tyszkiewicz

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