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BILL ANALYSIS



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House Bill 5932 (Substitute H-2 as passed by the House)
Sponsor: Representative Peter Lund
House Committee: Insurance
Senate Committee: Insurance

Date Completed: 12-16-14

CONTENT

The bill would amend the Insurance Code to do the following:

- Require the Director of the Department of Insurance and Financial Services annually to value the reserve liabilities of all outstanding life insurance contracts, annuity and pure endowment contracts, accident and health contracts, and deposit-type contracts issued on or after the effective date of the "valuation manual".
- Require every company with outstanding life insurance contracts, accident and health contracts, and deposit-type contracts annually to submit the opinion of an appointed actuary as to certain matters.
- Require the Director to promulgate regulations containing the minimum standards applicable to the valuation of disability plans and contracts issued before the date of the valuation manual.
- Provide that for contracts issued after the operative date of the manual, the standard prescribed in it would be the minimum required standard of valuation.
- Establish minimum valuation standards the manual would have to include, and specify other provisions that would apply to it.
- Require a company that issued life insurance contracts, accident and health insurance contracts, or deposit-type contracts, to establish reserves using a principle-based valuation that met particular conditions for policies or contracts, as specified in the valuation manual.
- Establish certain requirements for a company that used principal-based valuation for one or more policies or contracts.
- Exempt a domestic company from the proposed requirements if it met certain conditions.
- Provide for the confidentiality of certain information.
- Require the valuation manual to provide the Commissioners Standard Mortality Table for use in determining a minimum nonforfeiture standard that could be substituted for certain other tables.

The bill would define "valuation manual" as the manual of valuation instructions adopted by the National Association of Insurance Commissioners as described in the bill. The manual's operative date would depend, in part, on the enactment of the Standard Valuation Law or its equivalent by a certain number of jurisdictions.

Annual Valuation

The bill would require the Department Director annually to value the reserve liabilities (the "reserves") for all outstanding life insurance contracts, annuity and pure endowment

contracts, accident and health contracts, and deposit-type contracts of every company issued on or after the operative date of the valuation manual.

"Life insurance" would mean a contract that incorporates mortality risk, including annuity and pure endowment contracts, and as may be specified in the valuation manual.

"Accident and health" insurance would mean contracts that incorporate morbidity risks and provide protection against economic loss resulting from accident, sickness, or medical conditions, and as may be specified in the valuation manual.

"Deposit-type company" would mean a contract that does not incorporate mortality or morbidity risks and as may be specified in the valuation manual.

Opinion of Appointed Actuary

Under the bill, every company with outstanding life insurance contracts, accident and health insurance contracts, or deposit-type contracts in the State and subject to regulation by the Director annually would have to submit the opinion of the appointed actuary as to whether the reserves and related actuarial items held in support of the policies and contracts were computed appropriately, were based on assumptions that satisfied contractual provisions, were consistent with prior reported amounts, and complied with applicable laws of the State.

("Appointed actuary" would mean a qualified actuary (as defined in the bill) who was appointed in accordance with the valuation manual to prepare the required actuarial opinion.)

Also, except as exempted in the valuation manual, every such company would have to include in the opinion an opinion of the same appointed actuary as to whether the reserves and related actuarial items held in support of the policies and contracts specified in the manual, when considered in light of the assets held by the company with respect to the reserves and related actuarial items, made adequate provisions for the company's obligations under the policies and contracts, including associated benefits and expenses.

The bill sets forth a number of provisions that would apply to an opinion, including a requirement that the opinion be based on standards adopted from time to time by the Actuarial Standards Board.

Minimum Standards of Valuation; Valuation Manual

The bill would require the Director to promulgate regulations containing the minimum standards applicable to the valuation of disability plans and contracts issued before the date of the valuation manual. For accident and health insurance contracts issued on or after the manual's operative date, the standard prescribed in the manual would be the minimum standard of valuation required by the bill (for the Director's annual valuation of contract reserves).

For policies issued on or after the operative date of the valuation manual, the standard prescribed in the manual would be the minimum standard of valuation, except as otherwise provided (e.g., there was not a specific valuation requirement or the Director determined that a specific valuation requirement in the manual did not comply with the bill's requirements). At a company's option, this also would apply for policies or individual blocks of policies acquired by a company through a business acquisition or reinsurance transaction after the bill's effective date.

The operative date of the valuation manual would be January 1 of the first year following the first July as of which all of the following had occurred:

- The National Association of Insurance Commissioners (NAIC) had adopted the manual by a vote of at least 42 members, or three-fourths of the members voting, whichever was greater.
- The Standard Valuation Law, as amended by the NAIC in 2009, or legislation including substantially similar terms and provisions, had been enacted by states representing more than 75% of the direct premiums written as reported in the following annual statements submitted for 2008: life, accident, and health annual statements; health annual statements; or fraternal annual statements.
- The Standard Valuation Law, as amended by the NAIC in 2009, or legislation including substantially similar terms and provisions, had been enacted by at least 42 of the following 55 jurisdictions: the 50 states, American Samoa, the American Virgin Islands, the District of Columbia, Guam, and Puerto Rico.

The valuation manual would have to specify minimum valuation standards for and definitions of the policies and contracts subject to the annual valuation requirement. The minimum standards would be all of the following:

- The Director's reserve valuation method for life insurance contracts, other than annuity contracts.
- The Director's annuity reserve valuation method for annuity contracts.
- Minimum reserves for all other policies or contracts subject to the annual valuation requirement.

The valuation manual also would have to specify the policies or contracts or types of policies or contracts subject to the requirements of a principle-based valuation and the minimum valuation standards consistent with those requirements.

In addition, specific provisions would apply to policies and contracts that were subject to a principle-based valuation, and those that were not.

Principle-Based Valuation

The bill would require a company to establish reserves using a principle-based valuation that did all of the following for policies or contracts as specified in the valuation manual:

- Quantified the benefits and guarantees, and the funding, associated with the contracts and their risks at a level of conservatism that reflected conditions that included unfavorable events with a reasonable probability of occurring during the lifetime of the contracts.
- Incorporated assumptions, risk analysis methods, financial models, and management techniques that were consistent with those used within the company's overall risk assessment process, while recognizing potential differences in financial reporting structures and any prescribed assumptions or methods.
- Incorporated assumptions that were derived in one of the manners set forth in the bill.
- Provided margins for uncertainty, including adverse deviation and estimation error, such that the greater the uncertainty, the larger the margin and resulting reserve.

A company that used principal-based valuation for one or more policies or contracts as specified in the valuation manual would have to do all of the following:

- Establish procedures for corporate governance and oversight of the actuarial valuation function consistent with those described in the manual.

- Provide to the Director and the board of directors an annual certification of the effectiveness of the internal controls with respect to the principal-based valuation.
- Develop, and file with the Director upon request, a principal-based valuation report that complied with standards in the manual.

A company also would have to submit mortality, morbidity, policyholder behavior, or expense experience and other data as prescribed in the manual.

Domestic Company Exemption

A domestic company would be exempt from the requirement described above if the company met both of the following conditions:

- It had less than \$500.0 million of ordinary life premiums and, if the company were a member of a group of life insurers, the group had combined ordinary life premiums of less than \$1.0 billion.
- The domestic company reported total adjusted capital of at least 450% of the authorized control level risk-based capital in the most recent risk-based capital report and the appointed actuary had provided an unqualified opinion of the reserves.

Confidential Information

The bill states that, except as otherwise provided, confidential information (as defined in the bill) would be confidential and privileged, would not be subject to disclosure under the Freedom of Information Act, and would not be subject to discovery or admission in evidence in a private civil action. The Director, however, could use confidential information in furtherance of any regulatory or legal action brought as part of his or her official duties.

Also, except as otherwise provided, the Director could share confidential information with other state, Federal, and international regulatory agencies and with the NAIC, and could share certain confidential information with the Actuarial Board for Counseling and Discipline. The Director could not share confidential information unless the recipient agreed to maintain the confidentiality and privileged status of the information and had verified the legal authority to maintain confidentiality.

The Director also could receive documents, materials, data, or information from regulatory or law enforcement officials of other foreign or domestic jurisdictions, the Actuarial Board for Counseling and Discipline, and the NAIC. The Director would have to maintain as confidential or privileged any documents, materials, or information received with notice or the understanding that it was confidential or privileged under the laws of the jurisdiction that was the source of the information.

In addition, the Director could enter into written agreements governing sharing and use of information.

Mortality Tables; Nonforfeiture

The Act identifies various mortality tables that a company is permitted or required to use. The Act also contains a section that is known as the Standard Nonforfeiture Law for Life Insurance. (Nonforfeiture relates to the cash value of a policy to the policyholder.) This section provides, among other things, that ordinary mortality tables, adopted after 1980 by the NAIC, that are approved by a rule promulgated by the Director for use in determining the minimum nonforfeiture standard may be substituted for certain 1980 tables. Under the bill, this would apply to a policy issued before the operative date of the valuation manual.

For policies issued on or after the manual's operative date, the valuation manual would have to provide the Commissioners Standard Ordinary Mortality Table for use in determining the minimum nonforfeiture standard that could be substituted for the 1980 mortality tables. If the Director approved by regulation any Commissioners Standard Ordinary Mortality Table adopted by the NAIC for use in determining the minimum nonforfeiture standard for policies issued on or after the operative date of the valuation manual, the minimum nonforfeiture standard would supersede the minimum nonforfeiture standard provided by the manual.

Similar provisions would apply with respect to industrial mortality tables.

Currently, the nonforfeiture interest rate per annum for a policy issued in a particular year is equal to 125% of the calendar year statutory valuation interest rate for the policy as defined in the Standard Valuation Law, rounded to the nearest 0.25%. Under the bill, this would apply for a policy issued before the operative date of the valuation manual, and the nonforfeiture interest rate could not be less than 4.0%.

For policies issued on or after the operative date of the manual, the nonforfeiture interest rate per annum for any policy issued in a particular calendar year would be provided by the manual.

MCL 500.102 et al.

Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

The bill would have a minor, but likely negative, fiscal impact on the Department of Insurance and Financial Services, and no fiscal impact on local units of government. The bill would introduce some new administrative costs related to the promulgation of rules. To the extent that, under current statute and rules, the reserve liabilities of accident and health contracts and deposit-type contracts are not reviewed, the bill would introduce some new administrative costs related to those valuations as would be required under the bill.

Fiscal Analyst: Josh Sefton

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.