ACLI
Financial Security for Life

Talking Points on Deferred Annuity Nonforfeiture Law Changes

The Issue: Generally speaking, the standard Nonforfeiture Law (within the Insurance Code) requires that an individual deferred annuity contract provide the contract holder with a paid-up annuity or cash surrender benefits of a minimum amount if the contract holder surrenders the policy (e.g. stops making payments) during the accumulation period. The nonforfeiture amount is the deferred annuity's accumulated value minus certain charges (such as prior withdrawals and loans), based on interest rate minimums regulated by statute. In recent months, market interest rates have fallen so low as to render unrealistic the old statutory rates that insurance companies were required to use in determining the amount to return to contract holders. The NAIC has determined this threatens the availability of annuity products to consumers.

- The current interest rate environment creates unique challenges on crediting rates. In 2020 the yields for the US 5-year and 10-year Treasuries have been as low as 0.19% and 0.52%.
- The best course of action is to amend the minimum nonforfeiture interest rate in the states' respective Insurance Codes to reflect NAIC action on December 9th, 2020 amending the Model Standard Nonforfeiture Law for Individual Deferred Annuities to reduce the minimum rate from 1% to .15%.
- The .15% floor will only be triggered in low interest rate environments, such as the one we are currently experiencing and will only apply to <u>newly issued contracts</u>.
- While companies can invest in assets with higher yields than US Treasuries, examination of the US Treasuries is appropriate when considering the level of guarantee that a product may support as has been historically by the NAIC.
- <u>Companies are challenged to continue to be able to sell annuities with guarantees in the current environment</u>. Anecdotally, several companies have limited their product offerings while others are considering changes to meet the current economic condition.
- The reduced interest rate is the floor and the current formula will continue to be used to set minimum guarantees at the time of purchase. The floor only comes into play in an historically low interest rate environment such as the one we are currently experiencing.
- Companies will continue to use non-guaranteed crediting rates, bonuses, and other features to maintain market competitiveness and product differentiation.
- When market conditions improve, companies will be pressured to increase both their current and guaranteed crediting rates regardless of the regulatory floor.
- An annuity contract is a long-term commitment and requires that insurers maintain a long-time horizon with respect to managing contract liabilities. Companies invest in long-duration assets to achieve a consistent yield for the duration of the policy. New premiums are invested at current rates which limit both the return and amount available to credit on those assets.

Maximum surrender charges will not increase under the NAIC change, because they are based on a different interest rate ("the interest rate specified in the contract for accumulating the net considerations to determine maturity value").

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