STATE OF ILLINOIS
DEPARTMENT OF INSURANCE
SPRINGFIELD, ILLINOIS 62767

LIFE, ACCIDENT & HEALTH DIVISION

October 30, 1989

TO: ALL CHIEF LIFE ACTUARIES OF LIFE INSURANCE COMPANIES OPERATING IN ILLINOIS

RE: ANNUITY VALUATION (CB 89-57)

REPLY TO: LARRY GORSKI, LIFE ACTUARY

Recent articles on CD Annuities have prompted me to state the position of the Illinois Insurance Department on the valuation of such contracts. For purposes of this letter, CD Annuities are defined to be single premium deferred annuity contracts marketed to individuals in which the contract guarantees the initial interest rate for a period of time, often in excess of one year, with surrender charges applicable during the same period of time. Contractual provisions which apply at the end of the initial guarantee period are the cause of concern on the part of the Illinois Insurance Department. It should be noted, however, that the important aspect of this letter is the valuation of annuity contracts with specific policy provisions and not contracts with a particular name.

Some contracts provide for a brief window period immediately have the guarantee period during which surrender charges are waived. Other contracts provide for an election of a one year renewal guarantee period during which there are no surrender charges. A third variation, while somewhat different than the type described above, provides for a steep drop in surrender charges immediately followed by a low guaranteed interest rate. In effect, the policyholder has access to the full accumulated value at the end of the initial period with high interest rate guarantees.

The Commissioners Annuity Reserve Valuation method states that the reserves "shall be the greatest of the respective excesses of the present values, at the date of valuation, of the future guaranteed benefits, including guaranteed nonforfeiture benefits, provided for by such contracts at the end of each respective contract year. This language would seem to permit reserves to be based on contractual guaranteed benefits at discrete points in time, namely at the end of the respective contract year. However, Actuarial Guideline VIII adopted by the NAIC in December 1980 clearly indicates that the reserve should be the greatest of any of the discounted values of all guaranteed future benefits including cash surrender values available after the date of valuation.

The Guideline clearly indicates that a narrow interpretation of CARVM is inappropriate and that the reserves for such annuity contracts should be based on guaranteed future benefits not only at discrete points in time but on a continuous basis throughout contract years.

Even without the Guideline, failing to recognize in the statutory valuation process a large increase in guaranteed surrender nonforfeiture benefits experienced over a brief period of time is inconsistent with the conservative nature of statutory valuation and would not be acceptable.

If you have any questions concerning this letter, please call me at (217) 782-1794.

Very truly yours,

Larry M. Gorski

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Life Actuary

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