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BULLETIN NO. 11-31

TO: **ALL NEW JERSEY LICENSED LIFE INSURANCE COMPANIES AND FRATERNAL BENEFIT SOCIETIES**

FROM: **THOMAS B. CONSIDINE, COMMISSIONER**

RE: **REVISED STANDARDS FOR EQUITY INDEXED ANNUITY FORMS REVISING BULLETIN NO. 06-18**

N.J.S.A. 17B:25-18.1 requires any life or health insurance policy or contract, annuity, or variable contract delivered or issued for delivery in this State to be filed with the Commissioner of Banking and Insurance ("Commissioner") for approval. N.J.S.A. 17B:25-18.2 requires the Commissioner to adopt rules concerning any actuarial or form requirements for such policies and contracts. On July 24, 2006, the Department of Banking and Insurance ("Department") issued Bulletin No. 06-18, which provided guidance concerning the criteria for Department approval of equity indexed annuity ("EIA") forms.

In light of the continuing evolution of EIA product designs and the current low interest rate environment, the Department has determined that it is necessary to review and update this guidance. The purpose of this Bulletin is to provide revised guidance concerning the current criteria for Department approval of EIA forms. It should still be noted that this Bulletin applies not only to fixed (i.e., non-variable) EIA forms, but also to any Fixed Account option of a variable annuity form where the Fixed Account contains an equity indexed component.

- An EIA is an annuity having contract values that reflect the performance of a specified equity-based index (or indices). In addition, EIAs that are not variable contracts provide guaranteed minimum values that must comply with the Indexed Standard Nonforfeiture Law for Individual Deferred Annuities at N.J.S.A. 17B:25-21 et seq.

- The holder of an EIA receives a guaranteed rate of interest specified in the contract. The holder also receives a portion of the gains of a designated equity index over a period of time. The performance of the equity index is not guaranteed, and the portion of the equity index gain credited to the contract could increase or decrease subject to any limits specified in the contract. The Department believes that it is the right of the purchaser of such an annuity to be advised that gains may not occur, and that it is the

obligation of the insurer to so notify the purchaser. If gains do occur, the Department believes that the purchaser is entitled to a minimum portion of any such gains.

- The amount credited to an EIA contract depends on the following:

The "equity credit", which means the amount credited to the contract at the end of a "term" (as defined below) based upon changes in the index and the application of any applicable participation rate, cap, margin or other design element;

The "term", which means the period of time over which equity credits are determined;

The "method", which means the manner in which the equity credit is determined based on the term and changes in the index over that term (for example, in a "point-to-point" method, the credit is based on the change in the index from the beginning to the end of the term). There are a number of other methods by which the equity credit may be determined, including those that use averaging, the highest value, or combinations of methods. Generally, any method is permitted so long as it is not ambiguous, not so complicated as to be incomprehensible, not misleading, and is consistent with the general intent of crediting increases in the equity index;

The "participation rate", which means the percentage of the change in the index that is credited to the annuity. This rate may be changed prospectively by the insurer, subject to a minimum stated in the contract;

The "threshold rate" or "margin", which means an amount subtracted from the change in the equity index, subject to a maximum stated in the contract;

The "cap", which means a maximum interest rate that can be credited to the contract regardless of how well the equity index performs, subject to any minimum stated in the contract; and

The "floor", which means the minimum interest rate (at least zero percent) to be credited to the contract regardless of the equity performance.

- In addition to providing any required guaranteed minimum values as defined in the Indexed Standard Nonforfeiture Law for Individual Deferred Annuities, an EIA should meet the following requirements:

1. The brief description on the face page must prominently describe the benefits under the product as depending on the performance of an equity index;

2. The contract should define the annuity value used to determine annuity income benefits and state the method for calculating the annuity value, particularly the method by which changes in the equity index will be credited to the annuity value; and

3. The contract should specify the duration of the term(s) for purposes of equity credit calculation, and provide that any equity credit earned during a term will be credited to the annuity value no later than the end of that term.

4. The contract should contain a provision describing the minimum guaranteed cash surrender value in a manner that complies with the Indexed Standard Nonforfeiture Law for Individual Deferred Annuities.

- The specific parameters of the equity credit calculation are subject to the following:

1. If the contract has a cap rate, this rate, net of the threshold rate or margin, should not be less than the interest rate credited to the fixed (interest-based) account, or, in the absence of such an account in the contract, the minimum nonforfeiture interest rate required by N.J.S.A. 17B:25-21 et seq.;

2. If the contract offers a participation rate, this rate should be at least 10%, unless the actuarial documentation filed with the contract provides a demonstration that the cost of providing such minimum participation rate exceeds the cost to provide the cap rate as described in the previous paragraph.

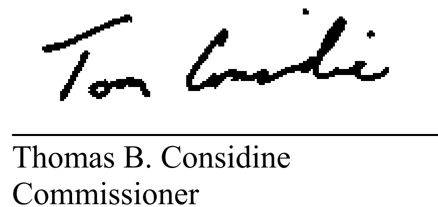
- Parameters should be set so that:

1. The cash and non-forfeiture values should be determinable at all times. It should be clear whether the cash and non-forfeiture values are based on the annuity value, or whether they are calculated independent of the annuity value;

2. The minimum cash and non-forfeiture values satisfy the requirements of N.J.S.A. 17B:25-21 et seq., including the requirement that the cash surrender value on the maturity date, as defined therein, is not less than the annuity value;

3. The cash surrender value should not be defined as the minimum value required by N.J.S.A. 17B: 25-21. If an insurer wishes to use the formula stated in law as the basis for the cash surrender value, then that formula should be stated in the contract; and

4. If a term is greater than one year, the cash surrender value during a term should include an equitable provision for an accrued credit during the term.



December 28, 2011
Date

Thomas B. Considine
Commissioner

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