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BULLETIN NO. 06-18

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

FROM: **STEVEN M. GOLDMAN, COMMISSIONER**

RE: **STANDARDS FOR EQUITY INDEXED ANNUITY FORMS**

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 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 September 21, 1998, the Department proposed regulations establishing standards for the approval of equity indexed annuity (EIA) forms, which were neither adopted nor reproposed. The Department intends to propose new rules in the near future that will permit a wider range of EIA products than would have been permitted under the Department's original proposal. In the meantime, the purpose of this Bulletin is to provide guidance concerning the current criteria for Department approval of EIA forms. It should be noted that this Bulletin applies not only to fixed (i.e., non-variable) equity indexed annuity 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 Standard Non-Forfeiture Law for Individual Deferred Annuities at N.J.S.A. 17B:25-20 or 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 elements:

The "equity credit" 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” means the period of time over which equity credits are determined;

The “method" 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” 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” means an amount subtracted from the change in the equity index, subject to a maximum stated in the contract;

The “cap” 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” 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 applicable Standard Non-Forfeiture Law, an EIA should meet the following requirements:

1. The brief description on the face page should 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.

● The specific parameters of the equity credit calculation should be subject to the following:

1. The participation rate should not be less than 30%;

2. If the contract has a cap rate, this rate, net of the threshold rate or margin, should be greater than 0%.

● 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 should satisfy the requirements of N.J.S.A 17B:25-20 and N.J.S.A. 17B:25-21 et seq., as applicable, 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:25-20 or 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.

Persons having questions regarding this Bulletin may direct them to the Department by phone at 609-292-5427 x50340, or FAX at 609-633-0527, and should specify that the question(s) relates to the Equity Indexed Annuity Bulletin.

This Bulletin, as well as the Department's forthcoming proposed rules establishing standards for EIAs, will appear on the Department's website at www.state.nj.us/dobi/legsregs.htm.

7/24/06
Date

/s/ Steven M. Goldman
Steven M. Goldman
Commissioner

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