Washington State
House of Representatives
Office of Program Research

BILL ANALYSIS

Financial Institutions & Insurance Committee

2SSB 5793

Brief Description: Changing on a temporary basis the minimum nonforfeiture amounts applicable to certain contracts of life insurance and annuities.

Sponsors: Senate Committee on Financial Services, Insurance & Housing (originally sponsored by Senators Winsley and Prentice).

Brief Summary of Second Substitute Bill

- Changes the minimum nonforfeiture amounts applicable to annuity contracts.

Hearing Date: 2/24/04

Staff: Carrie Tellefson (786-7127).

Background:

An "annuity" is a type of investment product that an individual may purchase from an insurance company. The typical annuity contract requires the purchaser (annuitant) to pay for the annuity either by a single premium or through installment payments. The insurance company, in turn, pays the annuitant a fixed sum, payable at specific intervals, for a specific period of time or for life. Each of the payments received by the annuitant represents a partial return of the invested capital as well as interest. Most annuity contracts require the annuitant to pay up-front fees and require the annuitant to pay a penalty if he or she decides to take the cash surrender value of the annuity before the annuity payments begin.

The Insurance Commissioner is responsible for the regulation of annuity contracts that are offered by insurance companies. Minimum non-forfeiture amounts are those amounts in an annuity contract that the policy holder does not forfeit even if he or she stops paying premiums. Annuity contracts must contain provisions requiring the insurer to pay a cash surrender benefit to the annuitant if the annuitant decides to "cash out" of the policy before maturity. Insurers are required to use a minimum interest rate of 3 percent per annum in calculating the value of any paid-up annuity, cash surrender, or death benefit.

The National Association of Insurance Commissioners (NAIC) adopts model legislation on various insurance topics. The NAIC developed model legislation regarding minimum nonforfeiture rates in 2003.

Summary of Bill:

Insurers must grant a paid-up annuity benefit either when the annuitant stops making his or her payments under the contract or when the annuitant requests, in writing, a paid-up annuity benefit.

When an annuitant decides to take a cash surrender benefit before annuity payments begin, the insurance company may defer payment of the cash surrender benefit for a period not to exceed six months, after making a written request and receiving written approval from the Commissioner. The request must address the necessity and equitability of the deferral.

The interest rate used to determine the minimum nonforfeiture amount is the lesser of 3 percent per annum or the five year constant maturity treasury rate reduced by 125 basis points where the resulting interest rate is not less than 1 percent. The interest rate is applied to an initial period and may be redetermined for additional periods. The redetermination date, basis, and period must be stated in the annuity contract.

When an annuity contract participates in an equity indexed benefit, it may increase the reduction described above by up to an additional 100 basis points to reflect the value of the equity index benefit. The present value of the additional reduction may not exceed the market value of the benefit. The Commissioner may require an insurer to demonstrate that the present value of the additional reduction does not exceed the market value of the benefit and, if the demonstration is not acceptable to the Commissioner, he may disallow or limit the additional reduction.

The minimum nonforfeiture amount due when an annuitant wants to cash out prior to receiving annuity payments is equal to the accumulation at rates of interest, as described above, decreased by prior withdrawals or partial surrenders (including interest, as described above); an annual contract charge of $50 (including interest, as described above); any premium tax paid by the insurer for the contract (including interest, as described above); and the amount owed on the annuity contract (including interest, as described above).

Before January 1, 2006, an insurer can choose to issue an annuity contract under the old law or the new law on this subject. On or after January 1, 2006, an insurer must issue an annuity contract under the new law.

Appropriation: None.

Fiscal Note: Not requested.

Effective Date: The bill takes effect on July 1, 2004.