

9. A description of all termination events, discontinuance triggers and options, notice requirements, corrective action procedures and all other contractual safeguards, including events that allow the insurer to terminate the contract immediately, and any special termination features of the contract whereby interest rate movements or participant withdrawal activity (or any combinations thereof) might terminate the insurer's contractual obligations;

10. A description of the procedures to be followed when a termination event occurs, but the insurer waives its right to terminate the contract;

11. A statement as to whether the assets in the segregated portfolio may be chargeable with liabilities unrelated to the assets of and services performed under the contract, together with a full explanation of the conditions under which such assets would be so chargeable; and

12. A description of the procedures to be followed in reporting in the Annual Statement for any risk charges.

(b) All data or information submitted to the Department under this section is confidential and shall not be disclosed by the Department to any person.

#### 11:4-46.5 Contract requirements

(a) The contract shall include at least the following:

1. The permissible levels and timing of any new deposits to the segregated portfolio;

2. If the contract does not have a set maturity, settlement options at termination permitting the contractholder to receive the contract value record over time except in the case of unilateral termination;

3. For contracts having a crediting rate formula, the maximum permissible rate period between crediting rate recalculations;

4. A provision that the insurer shall have the right to perform audits and inspections of assets held in the segregated portfolio upon reasonable notice to the custodian;

5. A provision that the insurer shall receive prior notice of any change in custodian, investment manager or investment guidelines;

6. A clear description of the insurer's obligations under the contract, and the contingencies and circumstances under which payments shall be made by the insurer to the contractholder;

7. If a market value adjustment formula is to be used in calculating the effect on the contract value record of certain withdrawals from the segregated portfolio, a clear description of the types of withdrawals subject to market value adjustment;

8. The investment guidelines and any subsequent changes thereto attached to and made a part of the contract;

9. A provision permitting the insurer to unilaterally terminate the contract within 30 business days of the occurrence of any of the following events, except that (a)9i and ii below shall not apply in situations where the investment manager is controlled by the insurer pursuant to N.J.S.A. 17:27A-1:

i. The investment guidelines are changed without the advance consent of the insurer;

ii. The segregated portfolio is invested in a manner that does not comply with the investment guidelines;

iii. Investment discretion over the segregated portfolio is exercised by or granted to anyone other than the investment manager or successor thereof; or

iv. Any act of fraud, misrepresentation of material facts, deceit or any breach of the contract that materially and adversely affects or would have affected the intent, structure or risk profile of the contract;

10. The Department shall permit qualifiers such as "material" or "reasonable" to modify the termination provision referred to in (a)9 above and any other provisions in the contract so long as such qualifiers are adequately quantified in the plan of operation. The adequacy of any such terms shall be within the sole discretion of the Department; and

11. A waiver provision as follows:

No waiver of remedies by the insurer following the breach of any contractual provision or of the investment guidelines, or failure to enforce such provisions or guidelines by the insurer, shall be effective against any insurance commissioner with regulatory jurisdiction over this contract, including the domiciliary insurance commissioner, unless approved in writing by such domiciliary insurance commissioner and any other insurance commissioner with regulatory jurisdiction over this contract.

#### 11:4-46.6 General requirements

(a) The insurer shall monitor the market value record for each contract. Upon each recalculation of the crediting rate, but no less frequently than quarterly, the insurer shall update the market value record to reflect the market value of the segregated portfolio.

(b) No contract shall be delivered or issued for delivery in this State unless the assets which it supports and for which a contract value is established are maintained in a segregated portfolio of a custodian.

(c) The investment guidelines shall be submitted to the insurer for underwriting review prior to the effective date of the contract.

(d) The investment guidelines shall permit investments of the segregated portfolio to be only in instruments for which market values are ascertainable pursuant to N.J.S.A. 17B:28-10.

(e) No contract shall obligate the insurer to purchase any assets at greater than market value or assets that would not be permitted investments pursuant to N.J.S.A. 17B:20-1 et seq.

(f) For group annuity contracts that make available to the contractholder the purchase of immediate or deferred annuities for the benefit of individual members of the group, no annuity shall be purchased without the delivery of the agreed consideration to the insurer for allocation to the insurer's general account or separate account as appropriate.

(g) In the case of unilateral termination of a contract pursuant to N.J.A.C. 11:4-46.5(a)9, the insurer shall refund any unearned risk premium or investment management fees, which shall terminate all future liability of the insurer or obligation to provide further benefits.

(h) In the case of an insurer's waiver of its right to terminate a contract when a termination event occurs, the Department shall require the insurer to submit a report describing the corrective action taken by the insurer.

(i) The insurer shall acknowledge in its submission that it shall maintain adequate reserves and collect adequate consideration for the cost of annuities purchased under contract option by transfer from the segregated portfolio.

#### 11:4-46.7 Reserves

(a) Reserves shall be held by the insurer in the general account and shown on Exhibit 10 of the Annual Statement. The assets supporting those reserves, together with the assets in the segregated portfolio, shall be sufficient to mature the liabilities under moderately adverse conditions. Annual asset adequacy analysis shall be performed and reported on by the appointed actuary in the annual actuarial opinion submitted pursuant to the Standard Valuation Law. Asset adequacy analysis must consider the nature of the assets and liabilities, and the anticipated effect on contract value crediting rates of possible future changes in the interest rate environment.

(b) Following is one method of reserve calculation that may be set forth in the plan of operation. The Department shall also consider alternative methods that have been adopted by the NAIC or otherwise supported by detailed actuarial analysis.

1. Project future liability cash flows using the guaranteed rate(s) of interest. For contracts that do not have defined maturity structures (such as "evergreen" or constant duration contracts), use the maturity structure of the assets as a proxy for the maturity structure of the liabilities.

2. Discount the liability cash flows at spot rates of interest that do not exceed 105 percent of Treasury spot yields, and that are adjusted, if necessary, so that the internal rate of return on the liabilities does not exceed the internal rate of return on the assets.

3. Hold reserve equal to the excess, if any, of the sum of the discounted liability cash flows calculated in (b)2 above over the market value of the assets.

4. Hold as additional reserves whether reserves are indicated by asset adequacy analysis in the opinion of the appointed actuary.

#### 11:4-46.8 Severability

If any provision of this subchapter or the application thereof to any person or circumstance is for any reason held to be invalid, the remainder of the subchapter and the application of such provision(s) to other persons or circumstances shall not be affected thereby.

### SUBCHAPTER 47. ACTUARIAL REQUIREMENTS FOR FLEXIBLE-FACTOR POLICY FORMS

#### Authority

N.J.S.A. 17:1-8.1, 17:1C-6(e), 17B:25-18, 17B:25-19, 17B:27-25, 17B:28-5, 17B:30-1 et seq., and P.L. 1995, c.73.

#### Source and Effective Date

R.1996 d.83, effective February 5, 1996.  
See: 27 N.J.R. 3750(a), 28 N.J.R. 1215(a).

#### 11:4-47.1 Purpose and scope

(a) These rules set forth requirements regarding actuarial reports and memorandum which are to be developed in connection with flexible-factor life insurance forms for such forms to be filed by the Commissioner for use and delivery for use in this State pursuant to N.J.S.A. 17B:25-18, 17B:27-25, 17B:28-5 and P.L. 1995, c.73.

(b) These rules shall apply to any insurer seeking to deliver, or issue for delivery, a policy of life insurance under a flexible-factor form in this State.

#### 11:4-47.2 Definitions

The following words and terms, when used in this subchapter, shall have the following meanings, unless the context clearly indicates otherwise.

“Commissioner” means the Commissioner of the New Jersey Department of Insurance.

“Department” means the New Jersey Department of Insurance.

“Flexible-factor form” means any life insurance policy, rider or endorsement, whether participating or nonparticipating, where the insurer reserves the right to modify (upward or downward) premiums, premium factors (interest, mortality, expenses) or benefits (death benefits, cash or loan values) on the basis of future anticipated or emerging experience.

“Insurer” means any person or persons, corporation, partnership, or company authorized or admitted to transact the business of life insurance in this State pursuant to Title 17B of the New Jersey Statutes.

“Minimum guarantee premium” means the minimum premium as established by the insurer to maintain coverage in force and avoid lapse.

“Persistency bonus” means credit either to an explicit or implicit accumulation account which varies by duration in a manner which encourages or rewards persistency.

“Tiered factors” means accumulation account factors (such as interest rates, cost of insurance or mortality charges, and expense charges) which vary by a policy amount (such as accumulation account value, cash surrender value, face value, or net amount at risk), or which differ for various components (tiers) of a policy amount. Factors which vary by policy duration shall not be considered tiered factors, but may be considered persistency bonuses.

“Qualified actuary” means an individual who is a member in good standing of the American Academy of Actuaries and who is qualified to sign statements of actuarial opinion for life and health insurance company annual statements accordance with the American Academy of Actuaries qualification standards and any requirements established by the Commissioner for actuaries signing such statements.

#### 11:4-47.3 General requirements

No form to which this subchapter applies may be delivered or issued for delivery in this State unless submitted to the Commissioner for review and filed by the Commissioner pursuant to all applicable law, including, but not limited to, N.J.A.C. 11:4-40.

#### 11:4-47.4 Pricing assumptions—actuarial certification

(a) Each form submitted for filing shall be accompanied by a certification that the insurer has prepared an actuarial memorandum which specifies the formulas utilized in calculating premiums or flexible factors. The actuarial memorandum shall be available for review by the Department upon request. The actuarial memorandum shall be signed

by a qualified actuary who shall indicate his or her professional qualifications and his or her relationship to the insurer (for example, company officer, consultant, etc.).

1. For purposes of (a) above, “formula” means the methodology used to set the premiums or factors. When asset shares or profit margins are used, the memorandum shall describe the method of calculating profits (that is, the accounting basis) and shall state the internal rate of return or other profit target. If the pricing target varies by pricing cell, the target shall be listed for a representative sample of pricing cells.

2. For policies to which N.J.A.C. 11:4-45 applies, the memorandum shall address the manner in which the cost of coverage is distributed among various factors (interest crediting rates, cost of insurance charges, expense charges, etc.), and the distribution of these factors over age and duration.

(b) The actuarial memorandum shall specify the projected assumptions as to investment earnings, mortality, persistency, and expense on which the initial premium or factor scale is based, together with comparable assumptions for maximum guaranteed premiums or factors set forth in the policy. The assumptions shall be set forth in sufficient detail to permit the Department to determine the profit factors implicit in the initial premium or factor tables. Assumptions that shall be indicated include, but are not limited to, reserve basis, if the pricing method includes profit; required surplus contributions treated as reserves; Federal income tax, if pricing is on an after-tax basis; and premium per unit of insurance, for flexible premium policies (that is, any policy where the policyholder may unilaterally change premium or choose not to pay premium).

1. The expense assumptions shall indicate whether expenses are on a marginal or a fully allocated basis. Expenses should be consistently allocated over the life of the block of business. For purposes of this section, “block of business” means all policies issued on the particular form by the insurer.

2. The profit factor(s) implicit in the initial premium or factor tables also shall be included. The profit factor may be expressed as either a rate of return, a present value of profits, or explicit margins associated within the premium or flexible factors.

(c) The actuarial memorandum shall include tables of all standard and preferred risk premiums or factors on both the initially intended non-guaranteed basis and the guaranteed basis. These tables are not required to include figures for substandard or rated policies.

1. All factors and premiums shall be provided in tabular form on both a current and guaranteed basis. For cost of insurance rates, a formula which reproduces the rates shall be deemed sufficient. Pricing factors (for example, expense charges) which are guaranteed and not subject to change should also be shown. The insurer

shall distinguish between factors which are guaranteed and not subject to change, and factors for which the current value is equal to the guaranteed value but which may be decreased, on a non-guaranteed basis, in the future.

2. The interest rate(s) used at the time of submission shall also be provided. Insurers shall advise the Department of any change in this (or any other factor) prior to the filing of the form by the Commissioner.

3. Minimum guarantee premiums for policies to which N.J.A.C. 11:4-45 applies, or critical values for tiered factors, persistency bonuses, or similar information shall be included.

4. Surrender charges shall be included if they are a flexible factor (subject to change) or if they are not included in conjunction with the memorandum required pursuant to N.J.A.C. 11:4-47.5.

(d) The insurer shall provide the Department with a statement of the intended conditions under which premiums or factors may be adjusted and the method by which these adjustments will be accomplished. This statement shall be construed as a statement of intention rather than a "guarantee" as to the insurer's future actions.

(e) All premium and factor formulas shall be approved by the insurer's board of directors, executive committee of the board, or an officer duly authorized by the board.

(f) The insurer shall indicate in its form submission that pricing assumptions for in-force policies will be reviewed whenever the premiums or factors for comparable new issues are changed, but in no event more often than once every policy year nor less often than once every five policy years. This review shall not be required during any period that premiums or factors are subject to an initial guarantee period.

(g) The actuarial memorandum shall contain a certification from the actuary that the assumptions are reasonable, and in the actuary's judgment, self-supporting and that the assumptions do not unfairly discriminate between new issues and in-force policies.

(h) In the case of non-participating policies, the insurer shall certify in the submission that future adjustments in premiums or factors will not be such as to distribute prior profits or to recoup past losses and that the changes will be based solely on future expectations as to investment earnings, mortality, persistency, and expenses.

(i) In the case of participating policies, the insurer shall certify in the submission that future adjustment in premiums or factors, other than dividends, will not be such as to distribute prior profit or to recoup past losses, and that the changes will be based on future expectations as to investment earnings, mortality, persistency, and expenses.

(j) Any adjustments in flexible factors or premiums made after the filing of the form, including changes in a non-guaranteed interest, shall be filed with the Department at least 60 days prior to implementation. The insurer may utilize the new premiums or factors provided the Commissioner has not disapproved such changes within the 60 day period.

1. The Commissioner shall waive the prior notice requirement set forth in (j) above in the case of interest rates when the insurer demonstrates to the Commissioner that credited rates are determined by a formula subject to (l) below.

2. For purposes of (j) above, "flexible factor" includes all factors which are redetermined on the basis of future experience (that is, current costs of insurance rates, interest rates and expenses charges for forms to which N.J.A.C. 11:4-45 applies, and current premiums for indeterminate premium forms).

3. Notification to the Department of any factor or premium change shall include the following information, without limitation:

i. An identifying form number(s) and filing date(s) of the form(s) to which the flexible factor change applies;

ii. An indication of the factor(s) which is being changed and the implementation date of such change, which shall be no sooner than 60 days after the notification of the change is filed with the Department;

iii. A specification of the categories (for example, face amount, date of issue, etc.) of new and in-force business to which the revised factors will apply. If the change is applicable only to new or only to in-force business, the submission should so indicate and include an explanation of the reasons for limited application of the change;

iv. The differences between the new factors and the last previously submitted factors for representative plans, ages and durations, and an indication whether the change represents an increase, decrease or no change from the prior filing, as well as a specification of the relative magnitude of any such change;

v. The rationale for the change, describing changes in experience or expectations leading to that change;

vi. A certification that an actuarial memorandum has been prepared, and is available for review by the Department upon request, which shall include: a certification by qualified actuary that the change does not increase the profit factor or, if changed, includes an explanation of the manner and reasons by which the profit factor is changed; specifies that the change does not unfairly discriminate between existing policies and new issues; and which otherwise satisfies the requirements set forth in (k) below; and

vii. A statement that the board of directors, executive committee, or officer duly authorized by the board has approved a flexible factor change as required by (e) above.

(k) The actuarial memorandum required pursuant to (j)3vi above shall contain a certification from the qualified actuary who prepared it that adjustments are such to retain or reduce the profit factor that was inherent in the rate formulas at issue. If, in the actuary's judgment, the profit factor for in-force policies should be increased, the actuarial memorandum shall provide all justifications for that increase.

1. The Commissioner shall disapprove changes in premiums or other factors which increase the profit factor for in-force business if he or she determines that the actuarial assumptions on which such change is based are unreasonable, not self-supporting, discriminate unfairly between new issues and in-force business, or are otherwise contrary to law.

2. Adjustments in premiums or factors which increase profits (before consideration of dividends) shall be acceptable if the Commissioner determines that future dividends will also be adjusted so that profit to the insurer, after dividends, is the same as was inherent in the rate formulas and anticipated dividends at issue.

(l) The Commissioner shall waive the requirement that the insurer provide 60 days' advance notice of changes in interest rates as set forth in (j) above, provided that the insurer include as part of its initial submission a statement of methodology for deriving the rate. The insurer shall provide 60 days' advance notice when the methodology is changed. The methodology shall tie the credited rate to a market (index) rate or earned rate on all or a segment of the insurer's portfolio, and the spread between this rate and the credited rate shall be fixed with a variation of no more than 25 basis points from the formula rate. Any interest rate methodology submitted pursuant to this subsection shall include, but not be limited to, the following:

1. The formula used to determine the credited rate;
2. If the formula involves the insurer's "earned rate," the following information:
  - i. The earned rate shall be identified as that earned by the general portfolio or by a specific block of assets. In the case of the latter, the specific assets shall be identified, either by listing each asset or by providing a summary which includes the amount and percentage of assets by issuer, duration to maturity, credit quality, payment structure, and call provisions;
  - ii. A description of the earnings of the assets used in determining the earned rate, including an indication of the manner by which capital gains (both realized and unrealized) and the earnings of subsidiaries are used in the calculation;

iii. An indication of whether the earned rate is net or gross of investment expenses, as well as a description of any provision for investment expenses implicit in the earned rate;

iv. The formula used to calculate the earned rate from investment earnings and asset values;

3. The frequency with which the credited rate is recalculated and redeclared; and

4. The frequency of compounding of the credited rate, and the earned or external index rate. Any implicit interest margin resulting from an inconsistency between the frequency of compounding of the earned or external rate and the credited rate shall be indicated.

(m) Any insurer seeking to utilize the alternative procedure set forth in (l) above shall provide to the Department the history of its interest rates upon request.

#### 11:4-47.5 Nonforfeiture benefits—actuarial memorandum

(a) Each form submitted for filing shall be accompanied by a certification, signed by a qualified actuary or company officer, that the nonforfeiture benefits provided under the form are in compliance with N.J.S.A. 17B:25-19, and that an actuarial memorandum has been prepared and signed by a qualified actuary which demonstrates that such benefits are provided in compliance with N.J.S.A. 17B:25-19. The actuarial memorandum shall be available for review by the Department upon request.

(b) For forms where the principal variable is the insurer's right to change (either increase or decrease) premiums subject to a maximum premium amount, policy provisions relating to nonforfeiture shall satisfy the requirements set forth in N.J.S.A. 17B:25-19. For purposes of determining compliance with this statute, "premiums specified in the policy" shall mean the initial scale, rather than the maximum scale, of guaranteed premiums, unless the latter would produce larger cash values. In this case, the minimum nonforfeiture benefits shall be based on the assumption that guaranteed maximum premiums shall apply wherever possible.

(c) For policies where cash values are determined retrospectively as an accumulation of gross premiums less expense charges, with interest increments and mortality decrements, the excess of expense charges in the first policy year over renewal expense charges may not be greater than the maximum initial expense allowance as set forth in N.J.S.A. 17B:25-19h(i). For purposes of determining the maximum initial expense allowance, the plan of insurance may be considered to be either that which would result from an indefinite continuation of initial interest, mortality, and expense factors (that is, the apparent plan), or by the assumption that maximum guaranteed interest, mortality, and expense factors will apply at all durations (that is, the guaranteed plan). In each instance, it shall be assumed that the premiums will continue to be paid at the initial level and

the amount of death benefit will continue unchanged from the initial amount. The resulting plan of insurance shall be either an endowment to the age at which the cash value equals the initial insurance amount or term insurance at which the cash value is exhausted. The maximum initial expense allowance shall be the smaller of the amounts so calculated for the apparent or the guaranteed plan of insurance.

1. The standards set forth in (c) above limit the excess first year expenses to an amount equal to the lesser of the maximum initial expense allowance for the apparent plan and the maximum initial expense allowance for the guaranteed plan.

2. For the apparent plan and the guaranteed plan, insurers shall assume that the initial premium and initial death benefit continue unchanged.

3. For front end loaded policies without surrender charges, in order to satisfy the requirements set forth in (c) above, insurers may be required to express the front end load as a percentage of premium rather than as a flat amount. In the alternative, the insurer may be required to set forth a minimum first year premium which is sufficient to mature the policy.

(d) All policy forms may incorporate surrender charges of specified amounts at specified durations, provided that the resulting cash values are at least as large as those developed under (c) above assuming a maximum initial expense allowance and no surrender charges. For purposes of this subsection, "specified" surrender charges means that the policyholder can determine at issue the exact amount of surrender charge applicable at any future time. Surrender charges provided by a table included in the policy or surrender charges as a percentage of initial premiums or death benefits shall be specified, but surrender charges as a percentage of variable future premiums, values or benefits are not specified.

1. The scale of surrender charges shall be such as to satisfy the tests regarding detection and avoidance of discontinuities in life insurance policies set forth in Exhibit 1 in the Appendix to this subchapter, incorporated herein by reference. The actuarial memorandum prepared pursuant to (a) above shall include a certification from a qualified actuary that surrender charges, if any, are in compliance with these tests for representative issue ages and premium/benefit arrangements on an "apparent plan" basis or, in the alternative, provide justification for instances where the tests may not be satisfied.

2. The insurer may satisfy the requirements set forth in (d) above by demonstrating that surrender charges are less than the unamortized unused initial first year expense allowance. The initial expense allowance shall be derived pursuant to (c) above. Further, the expense allowance shall be amortized over the period for which coverage was purchased.

(e) In order to demonstrate compliance with the requirements set forth in (c) and (d) above, the actuarial memorandum prepared pursuant to (a) above shall contain the following:

1. A description of the calculation of the maximum initial expense allowance, including a specific reference to the guaranteed plan purchased by the initial premium;

2. A demonstration, either algebraically or by comparing the maximum initial expense allowance to the excess first year expenses for all ages and classes, that the requirements set forth in (c) are satisfied; and

3. If there are surrender charges, a comparison, either tabular or by algebraic formula, of surrender charges to unused unamortized expense allowance at all durations.

(f) In addition to surrender charges as permitted pursuant to (d) above, a policy may contain provision for surrender charges in the form of withholding portions of credited excess interest or similarly calculated percentages of accumulated amounts. This type of surrender charge shall be considered a protection against possible asset liquidation loss at time of cash value payment, and the insurer shall state in the actuarial memorandum prepared pursuant to (a) above the circumstances under which such a surrender charge would be imposed. If the charge is to be imposed unconditionally, the minimum value test required pursuant to (d) above shall include the unspecified surrender charge in all calculations, and the insurer, in policy summaries and sales illustrations, may not display any accumulation amounts greater than the cash values assuming imposition of all surrender charges.

(g) Any insurer asserting that the form submitted for filing is not subject to N.J.S.A. 17B:25-19 shall file a memorandum signed by a company officer or qualified actuary with the form submission which sets forth in detail the basis upon which the insurer determined that the particular form is not subject to N.J.S.A. 17B:25-19.

#### **11:4-47.6 Recordkeeping**

Any actuarial memorandum prepared as required by this subchapter shall be retained by the insurer, and submitted to the Department upon request, until such time as the policy form is no longer being issued or delivered to persons residing in this State.

#### **11:4-47.7 Penalties**

Failure to comply with this subchapter shall result in the disapproval of any flexible-factor form for delivery in this State, as well as imposition of any other penalties as may be authorized by law.