SENATE COMMITTEE ON INSURANCE

Senator Susan Rubio, Chair
2021 - 2022 Regular

Bill No:	SB 927	**Hearing Date:**	April 20, 2022
Author:	Archuleta		
Version:	April 18, 2022		
Urgency:	No	**Fiscal:**	Yes
Consultant:	Erin Ryan		

SUBJECT: Life insurance

DIGEST: Extends the "free look" period for life insurance policies and annuities to at least 30 days; provides that a policy owner, in deciding whether to cancel a life insurance policy or annuity is entitled to rely on any information received regardless of whether the information was received before or after the policy was delivered to the policy owner; allows an insurance agent to receive compensation incentives related to the sale of a life insurance policy or annuity if the amount does not influence the recommendation to the consumer; requires several new disclosures to the consumer regarding agent compensation, potential tax benefits, all fees and charges under the policy, and crediting rates and surrender charges, as specified.

ANALYSIS:

Existing law:

1) Generally speaking, grants the Insurance Commissioner (IC) broad powers to determine if annuities and various types of complex life insurance products are fair to the public.

2) Requires that all annuity and life insurance forms be filed with the IC before being used in the market, but specifies that prior approval by the IC before marketing or use is not required.

3) Requires all individual life insurance policies to include a right to return of not less than 10 days nor more than 30 days, specifies that return of the policy within the "free look" period voids the policy and requires all premiums and fees paid to be refunded; and requires a notice of that right be printed on the policy or attached to it.

4) Generally speaking regards senior citizens a protected class in the sale of life insurance and annuities, and requires every individual life insurance or individual annuity contract issued to a "senior citizen" to include a right of return of no less than 30 days; for this purpose defines a "senior citizen" as a person who is 65 years of age or older when the policy is purchased; and requires a notice explaining the right of return to be printed on the front of the policy jacket or cover page.

5) Requires individual non-variable life insurance policies and non-variable annuity contracts, individual variable life insurance policies and annuity contracts, and immediate annuity contracts issued to senior citizens on or after January 1, 2004 to include a notice on the front of the policy jacket or cover page in 12 point bold print that describes the 30 day right to return and any surrender charges or penalties.

6) Provides that insurers, their officers and agents, and brokers and solicitors shall not issue, circulate or use any statement which is known, or which should have been known to be a misrepresentation of: a. The terms of a policy issued by the insurer or which is being negotiated by the person making or permitting the misrepresentation; b. The benefits or privileges promised thereunder; or c. The future dividends payable there under.

7) Requires insurers to notify the IC whether a policy form is to be marketed with or without and illustration, and if without, any use of an illustration prior to the first policy anniversary is prohibited.

8) Grants the IC broad authority to issue regulations governing modified guarantee annuities and variable life insurance, and the conditions under which such policies may be issued.

9) Defines life insurance policy illustrations and the provisions included therein in great detail with the purpose of ensuring that illustrations do not mislead purchasers of life insurance and to make illustrations more understandable by providing illustration formats, prescribing standards to be followed when illustrations are used, and specifying the disclosures that are required in connection with illustrations.

10) Requires the policy or policy owner to sign and date a statement that specifies that they have received a copy of the illustration and understand that that any nonguaranteed elements illustrated are subject to change and could be either higher or lower.

11) Requires the agent or insurer to sign and date a statement that certifies that the illustration has been presented to the applicant, that they have explained that any nonguaranteed elements are subject to change, and that they have made no statements that are inconsistent with the illustration.

This bill:

1) Requires all individual life insurance policies and annuity contracts to include a “free look” period of at least 30 days.

2) Specifies that in deciding whether to cancel a life insurance policy or annuity contract, a policy owner is entitled to review any illustration, policy, or other disclosure or information of any kind, and may rely on that information regardless of whether it was received before or after the policy was delivered to the policy owner.

3) Specifies that in recommending the sale of a life insurance policy, other than a term life insurance policy with no cash value, or an annuity to a consumer, the producer (agent) may receive compensation or incentives authorized by law and regulation if the amount of the compensation does not influence the recommendation.

4) Requires a life insurance agent to provide a prominent and separate disclosure to a prospective policyholder at or before the agent first engages in a substantive discussion about the potential purchase of a life insurance policy other than term life

insurance, or an annuity, that specifies that the agent works for one or more insurance companies, the agent may receive monetary compensation as the result of a policy or annuity sale and that the compensation may be based on the amount of the premiums for the policy or annuity purchased, and that encourages the consumer to ask any questions they may have about such compensation or seek professional advice from an independent insurance professional, tax advisor or attorney about any recommendations from the agent.

5) Requires the consumer to sign the disclosure in 4), which may be electronic, requires the consumer be given a signed copy of the disclosure, and if a policy or annuity is issued requires the insurer to retain a copy until three years after the policy or annuity is no longer in force.

6) Requires a life insurance policy illustration as defined to disclose all fees or charges applicable to the policy in both a narrative form including its method of calculation, and a numerical form that shows all fees and charges for all scenarios depicted in any presentation of nonguaranteed values in an illustration, as specified.

7) Requires the illustration to include a disclosure immediately above the policy signature line stating "Any fee not labeled as 'guaranteed' may be increased by the insurer at any time."

8) Requires, if a prospective policyholder applies for a policy, the policyholder to sign a copy of the policy charges report for any illustration that is of the policy applied for or of the policy as issued, and requires a signed copy be provided to the policyholder and retained by the insurer until three years after the policy is no longer in force.

9) Provides that if an insurer or agent makes a statement about the potential tax benefits of a life insurance policy, the insurer or agent must, the first time such a statement is made, provide the prospective policyholder with a specific disclosure about potential tax benefits, including:
   a) that in most circumstances a policy of life insurance cannot deliver any tax benefits unless the policy is kept in force until the death of the insured, which may be many years in the future;
   b) that the cost of insurance or other charges or fees may increase substantially as the insured ages;
   c) that neither the insurer nor the agent is authorized to provide tax advice; and
   d) that if potential tax advantages are an important reason for buying the policy, the prospective policyholder should consult a tax adviser.

10) Requires the disclosure in 9) to be signed by the prospective policyholder, a signed copy provided to the prospective policyholder, and if a policy is issued the disclosure be retained by the insurer until three years after the policy is no longer in force.

11) Requires specific disclosures if a life insurance policy provides for crediting the account value of the policy in a manner that does not prorate that credit to the date of termination of the policy, and requires it to be understandable to a reasonable consumer, as specified.

12) Provides that the disclosures required in 11 do not apply to nonguaranteed dividends.

13) Provides that if a life insurance policy or illustration references a guaranteed minimum interest rate or other crediting rate that is determined on any basis other than annual, it shall clearly state that it is not an annual guarantee and include a numerical example that a reasonable consumer could understand how the calculation differs from the calculation of an annual guarantee.

Background

According to the author:

> In order for consumers to avoid making costly mistakes buying life insurance policies, consumers need better information about the policies. SB 927 would require a life insurer to make specified disclosures to a prospective policyholder. Life Insurance Investment Plans (LIIP) are life insurance policies (often universal life) touted and sold as investments that can provide tax-free payments for retirement or for medical, dependent care, or other expenses. However, many of these policies will fail because policy fees will ultimately exceed policy credits and the policies will lapse. LIIP policies are extremely complex, and consumers have little chance of assessing for themselves whether a LIIP is a good investment. Consumers must as a practical matter trust the recommendations of the agents selling the policies. Consumers need better protection in these transactions. SB 927 will implement valuable guardrails for consumers when considering these policies.

This bill primarily is concerned with universal life insurance (UL) policies. UL insurance premiums consist of two components: a cost of insurance (COI) amount and a saving component, known as the cash value. As the name implies, the COI is the minimum amount of a premium payment required to keep the policy active. It consists of several items rolled together into one payment. COI includes the charges for mortality (the life insurance), policy administration, and other directly associated expenses to keeping the policy in force. COI will vary by policy based on the policyholder's age, insurability, and the insured risk amount. Collected premiums in excess of the cost of UL insurance accumulate within the cash value portion of the policy. Over time the cost of insurance will increase as the insured ages, however. If sufficient, the accumulated cash value will cover the increases in the COI. Indexed UL policies allow the net value of the policy to be invested in various indexed investment funds with the goal of increasing the policy's value in addition to premiums. But these investments can go both up and down. If returns are less than the COI, the policy loses value, and can cause the policyholder to actually lose funds and possibly the policy itself and all that has been paid into it.

Existing law requires a life insurance policy illustration, which is a presentation or depiction that includes non-guaranteed elements of a policy of life insurance over a period of years, to include specified requirements to ensure an illustration is understandable and does not mislead consumers. While the statutes are very detailed, or perhaps because they are, the actual illustrations can be very complicated and difficult to decipher. In the case of LIIP often involving universal indexed life insurance policies, the illustrations can run from 40 to more than 70 pages and include tables representing multiple options and calculations reflecting low, medium and high performance returns for assumptions if the policy stays in force for more than 60 years. These documents are full of technical insurance terms such as guaranteed and nonguaranteed minimum interest rates, index credit rates, index caps, weighted index change rate, historical percentiles, and possible investment returns based on the performances of multiple indexes such as the S&P 500, EURO STOXX 50, and the Hang Seng Index. The illustrations contain percentages and formulas, but do not translate these into easily understandable assessments of how the policy will actually perform or whether and how quickly costs and fees associated with the policy can decrease its value.

These policies are also often touted as offering policyholders multiple ways to access funds from the policies tax free prior to any death benefit through loans on the policy, generally up to any accumulated value in the policy, minus policy fees and charges. This is one of the more appealing sales pitches for these policies versus other life insurance products. Ultimately, however, any tax benefits will be determined by the final outcome of the policy. With a few exceptions, if the policy is surrendered or it lapses prior to the death of the policy owner, any funds previously accessed under the policy will become taxable.

All annuity and life insurance forms, policies and illustrations must be submitted to the IC before they can be used or marketed, but do not require prior approval. Variable life policies and forms are subject to greater scrutiny and must be approved before marketing or use by the insurer.

Questions

1. The bill as drafted does not include any delay in implementation despite the many new disclosures and changes to the “free look” period. Should implementation be delayed to January 1, 2024?

2. The bill specifies that agents may receive compensation as allowed by law or regulation, but then qualifies that by stating that it is only true if the compensation does not influence the recommendation to the consumer. How would an agent be able to prove that compensation was not on their mind? Would they have to recommend the product with the lowest agent compensation in order to survive scrutiny? Should the limitation be narrowed to: “if the amount of the compensation or the receipt of an incentive <u>was not the primary reason for the recommendation</u>?

3. Both the disclosure about agent compensation (new Section 10471) and the disclosure about tax benefits (new Section 10473) are required to be provided when the first substantive discussions about the purchase of a life insurance policy. Although the tax disclosure is only triggered the first time taxes are mentioned, that is likely to be very early in the sales process. Both disclosures are allowed to be electronic and have the same signature and retention requirements. Should insurers/agents be able to combine these disclosures into one document?

4. One of the primary complaints about variable life products is that they are so complex that consumers, and often the agents who sell them, do not fully understand the provisions. Should we create a Pre-licensing and Continuing Education requirement for agents who sell variable life insurance as defined by CDI?

Suggested Amendments

1. On Page 4, line__ change “under Section 10129.10” to “under Section 10127.10”

2. On Page 4, line __, Amend Section 10127.9 as follows:

   (f) This section does not apply to:

   (1) An employee pension or welfare benefit plan that is covered by the Employee Retirement and Income Security Act (ERISA).

   (2) A plan described by Internal Revenue Code sections 401(a), 401(k), 403(b), 408(k) or 408(p), as amended.

   (3) A government or church plan defined in Internal Revenue Code section 414, a government or church welfare benefit plan, or a deferred compensation plan of a state or local government or tax exempt organization under Internal Revenue Code section 457.

   (4) A nonqualified deferred compensation arrangement established or maintained by an employer or plan sponsor.

   (5) A settlement or assumption of liabilities associated with personal injury litigation or any dispute or claim resolution process.

   (6) Terminating employee pension plans or to assume liability of certain segments of ongoing plans, such as for terminated vested participants, or existing accrued benefits for currently active participants.

3. On page 4, line __, amend Section 10470 as follows: “The producer may receive compensation or other incentives authorized by law and regulation if the amount of the compensation or the receipt of an incentive ~~does not influence~~ <u>was not material to</u> the recommendation.”

4. Amend Section 10473 as follows: ADD new subsection (c) The disclosure required by this section may be provided in one document with the disclosure required by Section 10471.

5. ADD a new Insurance Code Section 1749.81:

   (a) Every life agent who sells life insurance other than term life with no cash value shall satisfactorily complete four hours of training prior to soliciting individual consumers in order to sell non-term life insurance.

(b) Every life agent who sells variable life insurance shall satisfactorily complete two hours of training prior to each license renewal. Completion of the four-hour annuity training required by Section 1749.8 does not satisfy the training required by this section. For resident licensees, this requirement shall count toward the licensee's continuing education requirement but may still result in completing more than the minimum number of continuing education hours set for in this section.

(c) The training required by this section shall be approved by the commissioner and shall consist of topics related to variable life insurance, and California Law, regulations, and requirements related to variable life insurance, prohibited sales practices and unfair trade practices. Subject matter determined by the commissioner to be primarily intended to promote the sale or marketing of variable life insurance shall not qualify for credit toward the training requirement. Any course or seminar that is disapproved under the provisions of this section shall be presumed invalid for credit for credit toward the training requirement of this section unless it is approved in writing by the commissioner.

(d) The training requirements set forth in this section shall not apply to nonresident agents representing an insurer that is a direct response provider. For purposes of this section, "direct response provider" means an insurer that meets each of the following criteria:

(i) The insurer does not initiate telephone contact with insureds or prospective insureds.

(ii) Agents of the insurer speak with insureds or prospective insureds only by telephone and at the request of the insured or prospective insured.

(iii) Agents of the insurer are assigned to speak with insureds or prospective insureds on a random basis, when contacted.

(iv) Agents of the insurer are salaried and do not receive commissions for sales or referrals.

(e) This section shall become operative on January 1, 2024.

6. Amend to delay implementation of the bill to January 1, 2024

ARGUMENTS IN SUPPORT:

According to the Life Insurance Consumer Advocacy center, too often the consumer's trust is misplaced in the purchase of LIIPs because the agent's financial interests conflict with the consumer's interests. The agent works for the insurance company and has no obligation under current law to consider the interests of the consumer, and agents often stand to make very large commissions if they persuade the consumer to purchase the policy. The bill would require that agents selling LIIP policies or annuities disclose the nature of their compensation and the potential for conflicts of interest at the beginning of substantive discussions about a policy or annuity available for purchase. Given the lure of the supposed tax advantages that motivates many LIIP sales , the bill would require that if an insurer or agent makes any statement about the potential tax benefits or advantages of a life insurance policy, then the consumer must be given a specific disclosure about the potential difficulty of actually realizing any such benefits or advantages.

The Consumer Federation of California supports the bill because it would create and enhance important common sense consumer protections for the rapidly growing, and increasingly opaque and complex, LIIP subset of the insurance industry. Far too many of these policies are lapsing due to obtuse rules, confusing and rapidly growing fees and 40+ page "illustrations" of policy benefits that even those selling the policies do not fully understand.

ARGUMENTS IN OPPOSITION:

The Association of California Life and Health Insurers (ACLHIC) opposes the bill because of significant concerns about the requirements it places on agents, and the workability of many of its disclosures. They believe the language regarding agent compensation would create considerable uncertainty and could be used as a litigation trap because agents would never be able to prove that compensation was or was not considered when working with a prospective policyholder. They also have significant concerns with the provision for fee and charge illustrations. The mandate in the bill will simply create a long and confusing disclosure with little real value to the prospective policyholder. It also requires insurers to disclose the method of calculation of their fees, which is proprietary. Regarding tax disclosures, they believe it places insurance carriers in danger of exceeding the scope of their license.

SUPPORT:

California Advocates for Nursing Home Reform
Consumer Federation of California (Sponsor)
Life Insurance Consumer Advocacy Center (Sponsor)
United Policyholders

OPPOSITION:

American Council of Life Insurers
Association of California Life and Health Insurance Companies
Finseca
Independent Insurance Agents and Brokers of California
Insured Retirement Institute
National Association of Insurance and Financial Advisors of California

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