

SYNTHETIC GUARANTEED INVESTMENT CONTRACTS MODEL REGULATION

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Section 1. Authority

This rule is issued pursuant to the authority vested in the commissioner of the State of [insert state] under [insert citation for authority].

Section 2. Purpose

- A. The purpose of this regulation is to prescribe:
- (1) The terms and conditions under which life insurance companies may issue group annuity contracts and other agreements that in whole or in part establish the insurer's obligation by reference to a segregated portfolio of assets that is not owned by the insurer;
 - (2)

- M. (1) "Hedging instrument" means:
- (a) An interest rate futures agreement or foreign currency futures agreement, an option to purchase or sell an interest rate futures agreement or foreign currency futures agreement, or any option to purchase or sell a security or foreign currency, used in a bona fide hedging transaction; or
 - (b) A financial agreement or arrangement entered into with a broker, dealer or bank, qualified under applicable federal and state securities or banking law and regulation, in connection with investment in one or more securities in order to reduce the risk of changes in market valuation or to create a synthetic investment that, when added to the portfolio, reduces the risk of changes in market valuation.
- (2) An instrument shall not be considered a hedging instrument or a part of a bona fide hedging transaction if it is purchased in conjunction with another instrument where the effect of the combined transaction is an increase in the portfolio's exposure to market risk.
- N. "Investment guidelines" means a set of written guidelines, established in advance by the person with investment authority over the segregated portfolio, to be followed by the investment manager. The guidelines shall include a description of:
- (1) The segregated portfolio's investment objectives and limitations;
 - (2) The investment manager's degree of discretion;
 - (3) The duration, asset class, quality, diversification, and other requirements of the segregated portfolio; and
 - (4) The manner in which derivative instruments may be used, if at all, in the segregated portfolio.
- O. "Investment manager" means the person (including the contractholder) responsible for managing the assets in the segregated portfolio in accordance with the investment guidelines in a fiduciary capacity to the owner of the assets.
- P. "Market value record" means an accounting record provided by the contract to reflect the fair market value of the segregated portfolio.
- Q. "Permitted custodial institution" means a bank, trust company or other licensed fiduciary services provider.
- Drafting Note:** When adopting this regulation, individual regulators may wish to review their applicable state laws to ensure that this definition hasn't inadvertently authorized an entity to act as a custodial institution that it would not wish to do so.
- R. "Plan of operation" means a written plan meeting the requirements of Section 5B(1) of this regulation.

- S. “Qualified actuary” means an individual who meets the qualification standards set forth in [insert reference to section of the regulations related to actuarial opinions and memoranda].
- T. “Rate period” means the period of time during which the fixed rate of return credited to the contract value record is applicable between crediting rate formula adjustments.
- U. “Segregated portfolio” means:
 - (1) A portfolio or sub-portfolio of assets to which the contract pertains that is held in a custody or trust account by the permitted custodial institution and identified on the records of the permitted custodial institution as special custody assets held for the exclusive benefit of the retirement plans or other entities on whose behalf the contractholder holds the contract; and
 - (2) Any related cash or currency received by the permitted custodial institution for the account of the contractholder and held in a deposit account for the exclusive benefit of the retirement plans or other entities on whose behalf the contractholder holds the contract.
- V. “Spot rate”
 - (1) “Treasury-based spot rate” corresponding to a given time of benefit payment means the yield on a zero-coupon non-callable and non-prepayable United States government obligation maturing at that time, or the zero-coupon yield implied by the price of a representative sampling of coupon-bearing, non-callable and non-prepayable United States government obligations in accordance with a formula set forth in the plan of operation.
 - (2) “Index spot rate” corresponding to a given time of benefit payment means the zero-coupon yield implied by (x) the Barclays Short Term Corporate Index (for a given time of benefit payment under one year) or (y) the zero-coupon yield implied by the Barclays U.S. Corporate Investment Grade Bond Index (for a given time of benefit payment

- W. "Synthetic guaranteed investment contract" or "contract" means a group annuity contract or other agreement that establishes the insurer's obligations by reference to a segregated portfolio of assets that is not owned by the insurer. The contract functions as an accounting record for an accumulation fund and the fixed rate of return credited to the fund reflects an amortization of the segregated portfolio's market gains and losses based on the period specified in the crediting formula, subject to any minimum interest rate guarantee.
- X. "Unilateral contract termination event" means an event allowing the insurer to unilaterally and immediately terminate the contract, without future liability or obligation to the contractholder.
- Y. "United States government obligation" means a direct obligation issued, assumed, guaranteed or insured by the United States of America or by an agency or instrumentality of the United States government.
- Z. "Valuation actuary" means the appointed actuary or, alternatively, a qualified actuary designated by the appointed actuary to render the actuarial opinion pursuant to Section 10. Written documentation of any such designation shall be on file at the company and available for review by the commissioner upon request.

Section 5. Financial Requirements and Plan of Operation

A contract may not be delivered or issued for delivery in this state unless the issuing insurer is licensed as a life

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- (b) A statement describing the methods and procedures used to value statutory liabilities for purposes of Section 10;
- (c) A description of the criteria used by the insurer in approving the investment manager for the segregated portfolio of assets associated with a contract in the class, if the investment manager is an entity other than the insurer or its wholly owned subsidiary;
- (d) A description of the insurer's requirement for reports concerning the assets in each segregated portfolio and transactions involving the assets, and a description of how the insurer can use the information in a report to determine that the segregated portfolio is being managed in accordance with its investment guidelines. The insurer shall require that the report be prepared no less frequently than quarterly, and include a complete statement of segregated portfolio holdings and their fair market value;
- (e)

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Drafting Note: The state of filing may request the plan of operation for informational purposes and may take it into account in deciding whether to approve the form. It is not anticipated that the state of filing would review and approve the plan of operation, but may use it in connection with the review of the form of contract.

Drafting Note: In the case that the plan of operation has not been approved, either affirmatively or by deemer, in the state of domicile of the issuing insurer, the state of issue, in issuing contract approvals, may wish to establish requirements to be met by the issuing insurer (e.g., notice requirement if the plan of operation subsequently changes, or requirement that the contract be operated in compliance with the plan of operation) in order to maintain its approval.

Section 7. Investment Management of the Segregated Portfolio

- A. The investment manager must have full responsibility for, and control over, the management of all segregated portfolio assets within the constraints specified in the investment guidelines.

Drafting Note: In the event that the segregated portfolio has multiple managers, all of these managers will be covered by the investment guidelines.

- B. The investment guidelines shall be submitted to the insurer for underwriting review before the contract becomes effective.
- C. If the insurer accepts a proposed change to the investment guidelines or allows the contract to operate in accordance with investment guidelines not meeting the criteria established in Section 5B(1)(g), approval of the non-conforming investment guidelines must be obtained pursuant to Section 5B.

Section 10. Reserves

A. Asset maintenance requirements for segregated portfolios governed by this regulation.

(1) At all times an insurer shall hold minimum reserves in the general account or one or more separate accounts, as appropriate, equal to the excess, if any, of the value of the guaranteed contract liabilities, determined in accordance with Paragraphs (6) and (7) of this subsection, over the market value of the assets in the segregated portfolio less the deductions provided for in Paragraph (2) of this subsection. The reserve requirements of this subsection shall be applied on a contract-by-contract basis.

(2) In determining compliance with the asset maintenance requirement and the reserve for guaranteed contract liabilities specified in Paragraph (1) of this subsection, the insurer shall deduct a percentage of the market value of an asset as follows:

(a) For debt instruments, the percentage shall be the NAIC asset valuation reserve "reserve objective factor," but the factor shall be increased by fifty percent (50%) for the purpose of this calculation if the difference in durations of the assets and liabilities is more(e)2.7 (-1 (i)-0eo224 Tees)-3.4 (er)-1.8 (4 (s)-2.5 (e84(fd[(F.8 (t)

- (a) It is an obligation of
 - (i) A jurisdiction that is rated in one of the two (2) highest rating categories by an independent nationally recognized United States rating agency acceptable to the commissioner;
 - (ii) Any political subdivision or other governmental unit of such a jurisdiction, or any agency or instrumentality of jurisdiction, political subdivision or other governmental unit; or
 - (iii) An institution that is organized under the laws of any such jurisdiction; and
- (b) At all times the principal amount of the obligation and scheduled interest payments on the obligation are hedged against the United States dollar pursuant to contracts or agreements that are:
 - (i) Issued by or traded on a securities exchange or board of trade regulated under the laws of the United States or Canada or a province of Canada;
 - (ii) Entered into with a United States banking institution that has assets in excess of \$5 billion and that has obligations outstanding, or has a parent corporation that has obligations outstanding, that are rated in one of the two (2) highest rating categories by an independent, nationally recognized, United States rating agency, or with a broker-dealer registered with the Securities and Exchange Commission that has net capital in excess of \$250 million; or
 - (iii) Entered into with any other banking institution that has assets in excess of \$5 billion and that has obligations outstanding, or has a parent corporation that has obligations outstanding, that are rated in one of the two (2) highest rating categories by an independent, nationally recognized, United States rating agency and that is organized under the laws of a jurisdiction that is rated in one of the two (2) highest rating categories by an independent, nationally recognized United States rating agency.
- (5) These contracts may provide for the allocation to one or more separate accounts of all or any portion of the amount needed to meet the asset maintenance requirement. If the contract provides that the assets in the separate account shall not be chargeable with liabilities arising out of any other business of the insurer, the insurer shall maintain in a distinct separate account that is so chargeable:
 - (a) That portion of the amount needed to meet the asset maintenance requirement that has been allocated to separate accounts; less
 - (b) The amounts contributed to separate accounts by the contractholder in accordance with the contract and the earnings on the contract.

This single valuation rate shall be used to model future market values of the segregated portfolio of assets. Future credited interest rates shall be modeled

- (e) One or more additional paragraphs may be needed in individual company cases as follows:
 - (i)

- (h) State the amount of account assets maintained in a separate account that are not chargeable with liabilities arising out of any other business of the insurance company;
 - (i) State the amount of reserves and supporting assets as of December 31 and where the reserves are shown in the annual statement;
 - (j) State the amount of any contingency reserve carried as part of surplus;
 - (k) State the market value of the segregated asset portfolio; and
 - (l) Where separate account assets are not chargeable with liabilities arising out of any other business of the insurance company, describe how the level of risk charges payable to the general account provides an appropriate compensation for the risk taken by the general account.
- C. When the insurer issues a synthetic guaranteed investment contract and complies with the asset maintenance requirements of Section 10A, it need not maintain an asset valuation reserve with respect to those account assets.
- D. This section describes the reserve valuation requirements for contracts subject to this regulation.
- (1) Reserves for synthetic investment contracts subject to this regulation shall be an amount equal to the sum of the following:
 - (a) The amounts determined as the minimum reserve as required under Section 10A(l);
 - (b) Any additional amount determined by the insurer's valuation actuary as necessary to make adequate provision for all contract liabilities; and
 - (c) Any additional amount determined as necessary by the commissioner due to the nature of the benefits.
 - (2) The amount of any reserves required by Paragraph (1) of this subsection may be established by either:
 - (a) Allocating sufficient assets to one or more separate accounts; or
 - (b) Setting up the additional reserves in the general account.

Section 11. Severability

If any provision of this regulation or its application to any person or circumstances is judged invalid by a court of competent jurisdiction, the judgment shall not affect or impair the validity of the other provisions of this regulation.

Section 12. Effective Date

This regulation shall take effect [insert date].

Chronological Summary of Actions (all references are to the Proceedings of the NAIC).

1998 Proc. 4th Quarter 16, 17, 609, 638-647 (adopted).

2015 Proc. 3rd Quarter Vol. I 115, 128, 135-138, 182-200, 344 (amended).