POLICY INSIGHT

A Policy Newsletter on Life and Health Insurance and Financial Security Issues

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Annuities Provide Financial Security

Annuities are popular financial products offered by insurance companies that provide individuals a predictable income stream, most often during their retirement years. Many individuals purchase annuities as protection from the risk of outliving their financial resources. These products have become especially important in the last few years as private pensions have begun disappearing.

Annuities typically involve a contract between an insurance company and an individual. The individual, or purchaser, agrees to make a single premium payment or multiple payments over time. Multiple premium payments can be fixed or flexible, depending on the desires of the purchaser. In return for the payments, the insurance company agrees to provide a single lump sum payment or future payments to the purchaser over a stated period of time. The guaranteed payments can begin within a year (immediate annuity) or at some point in the future (deferred annuity).

There are two phases to an annuity: the accumulation phase and the pay-out phase. During the accumulation phase, the principal value of the annuity will grow based on the interest rate offered by the insurer (fixed annuity) or fluctuate based on the value of the annuity's investment account (variable annuity).

Variable annuities contain funds that function very similarly to mutual funds by allowing purchasers to direct how they want their premiums invested. As with any investment, there is risk, but variable annuities do provide the purchaser the potential of taking advantage of the stock market's performance while also providing protection from inflation that can erode the purchasing power of a fixed return. Some variable annuity contracts provide protection against market declines by guaranteeing that an annuity's value will not fall below the initial investment.

Annuity contracts typically have surrender charge periods of five to ten years, and, while a purchaser may make withdrawals during this period, there may be surrender charges for such withdrawals.

Individuals may use after-tax dollars (non-qualified annuity) or transfer funds from their existing IRA or 401(k) accounts (qualified annuity) in purchasing their annuities. In either case, the investment provides tax-deferral on the value growth until the time of withdrawal. This powerful aspect makes annuities an attractive long-term investment option for individuals wanting to defer tax payments until a later date and a possibly lower tax rate. It should be noted that there may be federal tax penalties for early withdrawals.

In addition to the tax-deferral advantage, annuities offer other attractive features, including the timely passage of benefits to an owner's estate or beneficiaries without the delay and expense of probate. Unlike qualified retirement programs such as IRAs and 401(k) accounts, there are no contribution limits on annuities and no requirement that you begin making withdrawals at the age of 70. Annuities also provide a "free look period" that

(continued on page 2)

In this issue

TALHI
Texas Association of Life & Health Insurers

(continued from page 1)
allows the purchaser to cancel the contract if desired.

Fixed annuities are regulated as insurance, while variable annuities are regulated as both insurance and securities products. Insurers offering variable annuities are required to maintain separate reserves for these products from those maintained for their fixed annuities. The separate reserves are intended to ensure that fluctuating returns from the variable annuity investments do not affect the company's other insurance products.

The financial security that annuities promise places a heightened responsibility upon insurers to ensure that consumers' interests are protected through the annuity sales process and that the integrity of the agents who provide these products remains strong. Insurers have worked closely with the National Association of Insurance Commissioners (NAIC) and, in the case of variable annuities, with the Securities & Exchange Commission (SEC) and the Financial Industry Regulatory Authority (FINRA), to develop regulatory guidelines and laws to achieve these protections.

In 2007, with strong support from the industry, Texas took an important step forward to strengthen consumer protections by adopting the NAIC Suitability in Annuity Transactions Model Regulation. This proposal set high standards to ensure that annuity products purchased are appropriate and suitable to meet the financial needs of the purchaser.

During the 2009 legislative session, insurers advocated for and the legislature adopted new protections for consumers that prevent rogue agents from using misleading agent certifications and designations that do not reflect genuine expertise in annuity and life insurance sales. The legislation also established clear standards for the use of such designations in order to bring uniformity to state enforcement of proper credentialing and designation use.

As more Texans turn to annuities to obtain financial security in their retirement years, they can be comforted in knowing that the commitment shared by both insurers and state regulators to ensuring the promise offered by an annuity is fulfilled. Insurers will continue to work with all stakeholders to guarantee this commitment remains strong.

Riva Kinstick of Prudential contributed to this article. ■

Disability and Supplemental Insurance: Questions and Answers

Q: Are there insurance options that provide protection from an extended illness or disability that might prevent an individual from being able to work and pay his bills?

A: Yes, disability and supplemental health plans are insurance products designed to help individuals and families manage such a situation.

Q: How are disability and supplemental plans different from traditional health insurance plans?

A: The biggest difference is that disability insurance provides a cash benefit for lost wages due to a disability that prevents the policyholder from working. Traditional health insurance plans such as

(continued on next page)

Life Insurance: Financial Security for Those Who are Left Behind

Immediate Expenses	Ongoing Expenses	Future Expenses
• Funeral costs • Uncovered medical expenses • Mortgage and other debt • Taxes • Estate settlement costs	• Food • Housing • Utilities • Transportation • Health Care • Clothing • Insurance	• College • Retirement

Source: **LIFE Foundation** – A nonprofit organization dedicated to helping consumers make smart insurance decisions to safeguard their families' financial futures. For more information go to www.lifehappens.org

(continued from previous page)
preferred provider benefit plans (PPBPs) and HMOs provide a medical benefit, where the carrier pays the doctor directly. Disability coverage is often a benefit offered through an employer, and employees may have a choice of short term and long term disability coverage. Disability coverage may also be purchased directly from an insurance company on an individual basis. The cash benefit is typically a percentage of lost wages after an elimination period is met.

Supplemental plans are just like the name implies - insurance products designed to supplement other coverage such as an individual or employee's health benefit plan coverage. Supplemental plans may pay a cash benefit based on a diagnosis or accident or provide coverage for deductibles or coinsurance amounts that are the obligation of the policyholder under his or her health plan.

An obvious example of a supplemental plan is a Medicare supplement policy. Medicare supplement policies provide coverage for Medicare-imposed coinsurance and deductibles and may also cover items not covered by Medicare such as emergency health care services needed while traveling to a foreign country or additional preventive care services.

Examples of supplemental coverage include specified disease and accident only coverage. A specified disease policy will pay a cash benefit, either on a lump sum or daily basis, in the event a policyholder receives a diagnosis of a disease or condition covered under the policy, such as cancer or heart disease. This insurance product is meant to provide the insured with a cash benefit to cover copays or other incidental expenses that arise as a result of being ill. An accident only policy is similar in that it pays a cash benefit in the event of an accidental injury.

Q: How are disability and supplemental plans regulated?

A: The Texas Department of Insurance ("TDI") regulates disability and supplemental plans by requiring all policy forms to be filed with the agency prior to use and by promulgating minimum standards for policies sold directly to individuals. Medicare supplement plans are standardized nationally as a result of federal law and must comply with detailed requirements specified by TDI rule. Medicare supplement plans must be reviewed and approved by TDI prior to use in Texas. Other disability and supplemental products are required to be filed with TDI prior to use under the exempt filing regulations. TDI regularly audits exempt filings to ensure compliance with regulatory requirements. In addition to policy filing requirements, TDI investigates and responds to consumer complaints, if any, about all types of insurance products sold in Texas.

Q: Why don't mandated benefits apply to disability and supplemental plans?

A: Mandated benefits are health benefits that are required to be covered by statute or regulation. Examples of mandated benefits passed during recent legislative sessions include coverage related to autism, acquired brain injury, and routine medical care during clinical trials. Mandated benefit legislation requires an individual or employer-sponsored health benefit plan to provide coverage for a specific mandate. Almost all mandate bills passed by the legislature do not apply to disability or supplemental plans. The rationale for the exemption is that disability and supplemental plans are not designed to serve as an individual's primary health insurance coverage. As described above, disability plans cover lost wages. Supplemental plans (other than Medicare supplement plans) do not pay for services provided by health care providers but instead pay a cash benefit. Supplemental plans are a low cost way to purchase additional coverage to supplement health benefits.

New legislation passed in 2009, SB 1479 by Sen. Carona, amended the insurance code to create a standard list of exemptions to mandated benefits. The list includes supplemental and disability insurance policies along with other products that are generally not meant to serve as health benefit coverage, such as workers compensation insurance and dental and vision coverage.

Written by Pati McCandless of Greenberg Traurig LLC. ■

Financial Security Reality Check

√ How long could you be out of work before paying the monthly bills would be a problem?

√ If you were to die tomorrow, would your family members have enough money to maintain their lifestyles or would they have to begin making financial sacrifices almost immediately?

√ How much of your take-home pay is earmarked for savings?

√ Do you feel like you're on track to save enough money for your kids' college education?

√ When is the last time you reviewed the investments in your 401(k) plan?

√ Is the balance on your credit card statement growing or shrinking?

Source: LIFE Foundation – A nonprofit organization dedicated to helping consumers make smart insurance decisions to safeguard their families' financial futures. For more information go to www.lifehappens.org

Wellness and Prevention Programs Can Be Valuable Tool in Fight To Improve Health and Lower Costs

According to the Wellness Council of America (WELCOA), obesity-related diseases resulting from sedentary living cost the nation about $150 billion a year in healthcare costs. In fact, according to WELCOA, illnesses resulting from obesity and smoking represent 65 percent to 70 percent of all healthcare expenditures. Workplace wellness and disease prevention programs can help reverse these trends.

A 2008 PricewaterhouseCoopers study estimates that wasteful spending in the U.S. healthcare system is around $1.2 trillion of the $2.2 trillion total - more than half. About one-third of that waste is linked to behaviors that can be changed.

According to WELCOA, of the top ten causes of death in the U.S., which represent 70 percent of all deaths, four of them (including the top three - heart disease, cancer, and stroke) are directly related to diet – a subject that virtually all wellness programs address. In addition, stress reduction programs have been shown to reduce a host of physical complaints that send countless employees to healthcare providers for treatment.

A study in the *American Journal of Health Promotion* found that 25 percent of all health plan claims for 44,000 employees over six years were related to seven major health risks, all of which tend to be addressed as core components of wellness programs.

In addition to improved health, financial savings are almost always a result of well-managed programs. According to WELCOA, within 18 months to three years, most employers can expect a return on investment (ROI) of 3-to-1. In other words, employers that spend $100 to $150 per employee per year on wellness initiatives can expect to save a minimum of $300 to $450 per year with some experiencing an ROI as high as 6-to-1.

While it can be difficult to accurately determine financial savings, clinical results are much easier to measure, and are just as important. According to WELCOA, participants in wellness programs tend to see a range of tangible and measurable health benefits, such as reductions in cholesterol, blood pressure, and weight.

WELCOA also notes that over 400 individual medical studies have provided concrete evidence that worksite wellness programs do, in fact, affect behavior and risks. In fact, some wellness programs show almost immediate benefits. For example, the blood vessels of employees who quit smoking begin to dilate back to normal within 12 to 24 hours, which can reduce blood pressure within three to six months.

Private businesses are equally interested in wellness. About 80 percent of the member companies of the Dallas-Fort Worth Business Group on Health, a coalition of 126 of the largest employers in North Texas, are now offering some type of wellness or disease management program to their employees. In addition, according to an August 19, 2009 article in the *Dallas Business Journal*, "(M)ost are not cutting back on these programs, despite the recession." ■

ABOUT TALHI: Texas Association of Life and Health Insurers

TALHI is the trade association for life and health insurers doing business in Texas. It was formed when Texas Life Insurance Association and the Texas Legal Reserve Officials Association merged in 1997.

Now representing the majority of insurers doing business in the state, TALHI has emerged as a leading voice for life and health insurers on legislative and regulatory matters.

TALHI is an open-door trade association boasting some of the most progressive life and health insurance company officials throughout the country. We are united for the mutual benefit and development of a healthy and competitive insurance market.

The work that TALHI does in the public policy arena is intended to strengthen the insurance market by enhancing insurers' ability to provide Texans financial security for their future.

We welcome the opportunity to work with you.

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