

An Explanation of the Operation of a Legal Reserve Life Insurance Company, Underwriters of Annuities.

Through devastating world wars, financial recessions and depressions, sweeping epidemics, earthquakes and fires, inflation and deflation, the life insurance industry has protected people to a degree unmatched by any type of financial institution in the history of the world.

Today the life insurance industry provides more than a trillion dollars of death protection to American consumers.

The financial reliability of the life insurance industry, even in times of financial panic, was demonstrated convincingly during the Great Depression of 1929-38 when some 9,000 banks suspended operations while 99% of all life insurance in force continued unaffected. Reinsurance, acquisitions, and mergers protected virtually all policyowners in the affected companies against personal loss.

Unlike most industries where size is a major measure of financial stability, life insurance's unique series of safeguards can make even the smallest company a tower of strength. In 1949 Mr. Leroy A. Lincoln, then president of the world's biggest life insurance company, Metropolitan Life of New York, stated: "You're as safe, as well protected and the cost is just as cheap if you buy from a small insurance company as from the largest."

The State Insurance Department

The State Insurance Department is a most vital department in each of our fifty states. Acting on its own state's insurance laws and regulations, it supervises all aspects of an insurance company's operation within that state. In addition, the State Insurance Department licenses all companies and agents to sell insurance within its boundaries. It must also approve all policy forms and in some cases, sales materials before they can be offered to the public. The Departments review complaints from consumers and mergers of companies which do business within its boundaries.

Required Reserves Ensure Payment of Policyholder Benefits

A large percentage of each premium dollar calculated by actuaries for each company goes into the policyowner's reserve fund. This policy reserve (Legal Reserve) fund is a liability to the life insurance company. The fund is established as a way of determining or measuring the assets the company must maintain in order to be able to meet its future commitments under the policies it has issued.

The reserve liabilities are established as financial safeguards to ensure the company will have sufficient assets to pay its claims and other commitments when they fall due. These assets are kept intact for payment of living and death benefits to the insureds. Life companies that comply with the legal reserve requirements established by the state insurance laws are known as legal reserve life insurance companies.

Risk-Based Capital

In addition to the required reserves, every insurance company is measured using formulas derived under Risk-Based Capital Requirements under the NAIC models. In a nutshell, the RBC measures the amount of capital required to meet different elements of risk, including asset, interest rate, insurance and business risk(s). A company reporting total adjusted capital of 200% or more is considered within acceptable levels. RBC ratios of 300-350% are common in the industry. Companies who RBC ratios fall below 200% fall under regulatory controls by the state insurance departments.

Periodic Company Examinations

Every year all legal reserve life insurance companies submit annual statements to the insurance departments of each state in which they are licensed to do business. The format and contents of the forms used are prescribed by the State Insurance Commissioners and they are a detailed report of an insurance company's financial status that is important in evaluating the company's solvency and compliance with the insurance laws. Every few years, depending on a company's home state law, all companies operating in more than one state undergo a detailed home office zone examination of its financial position. This audit is conducted by a team of State Insurance Department Examiners representing the various zones in which the company is licensed to do business. Companies licensed in only one state are subject only to an annual home office examination by their State Insurance Department.

Additional Security Safeguards

1. Reinsurance: Nearly every legal reserve life insurance company further protects its policyholders by reinsuring part of the coverage with a life reinsurance company. This is done when the company will not or cannot undertake a risk alone. Reinsurance prevents relatively sizable claims from depleting a company's policy holder reserves. The amount reinsured depends on many factors such as the size of the individual claim and the number of claims a company can expect.

2. Surplus: The surplus is the amount by which a company's assets exceed its liabilities. The surplus protects the policyholders and third parties against any deficiency in the insurer's provisions for meeting its obligations. The determination of the optimum amount of surplus that a company will retain must be based on experience, current conditions, and an awareness of the primary goal of maintaining a strong company that is always able to pay claims as they arise.

Mergers

In the unlikely event that a company's annual statement or its own examination reveals possible financial weakness, one of several avenues is open to the company: (1) Produce additional operating capital; (2) Sell its business to another life company; (3) Merger into another financially stable life company. A legal reserve life insurance company simply does not close its doors and go out of business declaring that all policies are null and void. Legal reserve life policyholders enjoy personal security safeguards unknown by other types of business.

Yours for Life

Another unique advantage of legal reserve life insurance is that if one company is purchased or merged into another, there is no change whatsoever in the policy benefits or premiums. Legal reserve life insurance companies have established a public responsibility to respect both the letter and the spirit of laws and regulation so the interest of their policyholders are always protected.

Policyholders Protection Comes First

Today, as has been the case for many years, it is unlikely for the policyowner of legal reserve life insurance companies to lose their policy benefits. Through strict state insurance department regulations, the establishment of many state insurance guaranty associations and because of the insurance industry's history of financial stability and public responsibility to operate in a manner not detrimental to the welfare of the community, your policy is secured by industry safeguards.

