

## **New Reserve Requirements for Charities That Issue Gift Annuities in New York**

Approximately two years ago, the New York Insurance Department contacted the American Council on Gift Annuities and certain other individuals who work with charities about collaborating on a revision of the annual state reporting form. Frank Minton and Lindsay Lapole, representing the ACGA, joined others in a meeting with the Department, and the result was a new, simplified, and improved form.

During our conversations about the reporting form, we learned that the Department's actuaries were concerned about the adequacy of reserves being held by charitable organizations in support of gift annuities. To correct this situation, the actuaries proposed that a charity either prepare and file an Actuarial Opinion and Memorandum based on an asset adequacy analysis in accordance with Section 95.8 of Regulation No. 126 (11 NYCRR 95) or that the methodology for determining minimum required reserves be modified to comply with Section 95.11(b) of that Regulation. They suggested that this new methodology entail discounting the value of equity investments, pegging the discount rate to the 10-year Treasury Note at a point in time instead of basing it on the Standard Valuation Law followed by most states, and applying the Annuity 2000 Mortality Tables to all annuities rather than just to the most recent ones.

Lapole and Minton had two additional meetings with the Department. In the course of those meetings, they noted that gift annuities are backed by a charity's entire assets and not merely by those in the segregated account, and they made the point that determination of minimum required reserves should not be complicated, should not require an expensive compliance procedure, and should not discourage the issuance of gift annuities. The Department listened to our concerns and proposed a solution consistent with New York State Regulations that would address their actuaries' concerns about the adequacy of reserves and also accommodate ACGA's concerns to the extent they considered possible.

Following is a summary of that new methodology for determining minimum required reserves:

- The current statutory minimum required assets are 110% of the actuarially-determined reserves based on applicable mortality tables and a discount rate per the Standard Valuation Law.
- A charity shall be required to maintain additional reserves equal to at least 15% of the actuarially-determined reserves mentioned above, which results in minimum required assets equal to 126.5% of such actuarially-determined reserves ( $115\% \times 110\% = 126.5\%$ ). Please note that the 10% surplus requirement has not changed.
- A charity that maintains these additional reserves will not have to file the Actuarial Opinion and Memorandum, though it could do so in lieu of maintaining the additional

reserves. The result is to keep the determination of minimum required reserves quite simple.

- To allow charities time to arrange for the larger reserves they must maintain, the Department will phase in the additional reserve requirement over a three-year period. For the 2008 report (filed in early 2009), total minimum required reserves will be 105% of actuarially-determined reserves. For the 2009 report, total minimum required reserves will be 110% of actuarially-determined reserves, and for 2010 and subsequent years, total minimum required reserves will be 115% of actuarially-determined reserves.

Suppose that in 2008, 2009, and 2010 actuarially-determined reserves were a constant \$1,000,000. The minimum amount of actual assets the charity has to maintain in the segregated account in order to meet the 10% minimum surplus requirement of Section 1110(b) would be \$1,155,000 for 2008, \$1,210,000 for 2009, and \$1,265,000 for 2010. For 2007, the minimum required assets in the segregated account would have been \$1,100,000.

A charity with a relatively new gift annuity program that wants to start issuing gift annuities in New York has two choices. One is to apply immediately for a permit, in which case it will be subject to the above reserve requirements, and it will have to file an annual report. The other possibility, provided its minimum required reserve calculated using the new methodology does not exceed the \$500,000 threshold, is to apply for a certificate of exemption. Once it reaches the threshold, it would apply for the permit. It would not have to file an annual report until it obtains a permit, but it would have to maintain assets that are at least 125% of the higher reserve requirement described above. In view of this, charities may be advised to apply immediately for a permit rather than go through a two-step process.

How will the higher reserve requirement affect charities? Here are some things to keep in mind:

- If a charity follows the ACGA rates, the contribution for a gift annuity will be sufficient to cover even the higher reserve requirement, which means that the charity would not have to move any of its general funds to the segregated account.
- If a charity is accustomed to spending some portion of a contribution up-front, the amount it can spend will be considerably reduced. (The most prudent course is to spend none of the contribution until the obligation terminates at the death of the sole or surviving annuitant.)
- Charities with existing programs, which have been holding in the segregated account just the minimum necessary to meet minimum surplus requirements, may

have to move some general funds into the segregated account, but they will have a three-year period to gradually take whatever action is required.

This solution is not all that we would have wished. Still, in light of what was originally on the table, it appears to be a reasonable compromise, and we have appreciated the Department's willingness to enter into a dialogue with us. That was also the opinion of a number of representatives of New York charities with whom we consulted.

We understand that both the PG Calc and Crescendo programs will calculate both the minimum required reserves as well as the minimum required surplus. Thus, from a practical standpoint, filing your annual report will be no more complicated than before.

The New York Department of Insurance will soon be posting information about the new reserve requirement on its web site, and it also plans to send a notice to gift annuity permit holders.