

Changes to Smart Builder IUL policies impacted by updates to Section 7702

383NB

Date: November 18, 2021**Effective:** November 22, 2021

Earlier this year, North American shared a field bulletin and FAQ surrounding Section 7702 after the passing of the Consolidation Appropriations Act, which included a change to the rates used in determining whether a policy qualifies as life insurance. These rates are also used to evaluate whether the policy qualifies for preferential tax treatment of distributions from the policy. As a result of changes to Section 7702, life insurers, including North American, are updating rates on impacted products issued on or after January 1, 2021.

What policies will undergo adjustments?

As a result of changes to Section 7702, beginning November 22, 2021, North American will start updating rates on any impacted Smart Builder indexed universal life (IUL) policies issued in between January 1, 2021 – November 21, 2021. Smart Builder policies issued on or after November 22, 2021, will have the new rates incorporated.

Please note, Smart Builder IUL 2 will have the new rates incorporated at product issue.

What impact will these changes have on policies?

North American will retroactively apply the updated rate as of the policy effective date. These changes will affect policies in one of the following ways. Please note, we will not alter face amounts unless we receive a request to do so.

Scenario one: Policy was not a Modified Endowment Contract (MEC) under the previous rules nor will the policy become a MEC under the new rules.

- For policies that qualified as non-MEC, the changes in the law would allow more premium to be paid into the policy without it becoming a MEC.
- If the illustration was run using the Guideline Premium Test, there is a higher Guideline Level Premium (GLP) and Guideline Single Premium (GSP).
- If the illustration was run using the Cash Value Accumulation Test (CVAT), the change in legislation may result in a restatement of client's policy values and could impact long-term illustrated performance.
 - If the policy was already in corridor, the updated CVAT factors will result in a change in the death benefit, thus a change in policy values.
 - If the policy was ever illustrated to be in corridor, then the illustrated performance will change as the corridor factors change.

Field Bulletin

Scenario two: Policy was a MEC under the previous rules but will no longer be a MEC under the new guidelines.

- The changes in law have resulted in the tax status of your client's policy changing to non-MEC life insurance, resulting in more favorable tax treatment of certain distributions.
- If the illustration was run using the CVAT, the change in legislation may result in a restatement of the client's policy values and could impact long-term illustrated performance.
 - If the policy was already in corridor, the updated CVAT factors will result in a change in the death benefit, thus a change in policy values.
 - If the policy was ever illustrated to be in corridor, then the illustrated performance will change as the corridor factors change.

Scenario three: Policy is a MEC under both the previous and new guidelines.

- While the 7-pay limit was updated, the policy still qualifies as a MEC.
- If the policy was issued using the Guideline Premium Test, the change in law may allow for additional premium to be paid into the policy while still qualifying as life insurance.
- If the illustration was run using the CVAT, the change in legislation may result in a restatement of client's policy values and could impact long-term illustrated performance.
 - If the policy was already in corridor, the updated CVAT factors will result in a change in the death benefit, thus a change in policy values.
 - If the policy was ever illustrated to be in corridor, then the illustrated performance will change as the corridor factors change.

Communication to policyowners

Letters to all clients with impacted policies issued on or after January 1, 2021, will be sent beginning in December 2021 and continuing into early 2022 after adjustments have been completed. The letter will direct clients to contact their agent if they have any questions about how their specific policy has been impacted.

Policyowner options

Depending on the type of policy and your client's goal, the following actions may be appropriate:

- Clients can continue their policy without making any changes other than those automatically updated as a result of the new rates.
- Clients can take advantage of updated limits by paying additional premium. If desired, a request for an updated illustration showing the higher premium can be submitted.
- If the policyowner had their death benefit restated as a result of the updated rate, but would prefer to maintain the original death benefit, they may request to increase their policy's face amount up to the prior death benefit amount without undergoing additional underwriting. This request must be made within 90 days of the date of the letter.
- Clients can decrease their face amount to maximize cash value.
- Clients can work with their agent to determine if a different policy would better meet their insurance and financial needs.

FOR AGENT USE ONLY. NOT TO BE USED FOR CONSUMER SOLICITATION PURPOSES.

Field Bulletin

Impact to pending business

For applications that are currently being processed in New Business and Policy Change that have not yet been placed in force, note the following guidelines:

- North American will not require an updated illustration to be run.
- If the policy is to be issued under the Guideline Premium Test, the client's guideline premiums and 7-pay premiums will be updated to the higher limits, but there should not be an impact to illustrated values.
- If the policy is to be issued under the Cash Value Accumulation Test, it may be worthwhile to run an updated illustration as the illustrated cash values may be stronger with the updated CVAT corridor factors, especially for policies slated to enter corridor in early durations.

Availability in Web-Based Illustrations

Web-Based Illustrations will be updated with the new rates for Smart Builder and Smart Builder 2 as of November 20, 2021. Illustrations will not be able to be run under the old rates on Smart Builder as of this date.

Impact of face amount reductions

Policies will still be subject to any applicable surrender or decrease charges. If the policy has insufficient account value to cover the charge, an alternative charge that is proportional to the account value will be applied.

Commissions will be handled in accordance with existing policy guidelines and therefore only result in charge backs if a death benefit decrease is elected on a product with a Waiver of Surrender Charge Option rider.

Impact of internal 1035 exchanges

If the dollar amount of the surrender charge decreases from the old policy to the new policy, that difference will be deducted from the cash value when the policy is rolled over.

Rollover money is not subject to commissions.

Please note, treatment of face amount reductions and internal 1035 exchanges are consistent with North American's current practices. [For more information, view our conversions, internal replacements, and policy change guidelines.](#)

Requesting an inforce illustration

To request an illustration for an inforce policy, use the form located on NorthAmericanCompany.com under Inforce Business Access. A form will need to be submitted for each option illustrated. Illustrations will be delivered through the inforce correspondence section of the website.

For all other questions, please contact your MGA or regional vice president.

Field Bulletin

For most policies, withdrawals are free from federal income tax to the extent of the investment in the contract, and the policy loans are also tax-free so long as the policy does not terminate before the death of the insured. However, if the policy is a Modified Endowment Contract (MEC), a withdrawal or policy loan may be taxable upon receipt. Further, unpaid loan interest on a MEC may be taxable. A MEC is a contract received in exchange for a MEC or for which premiums paid during a seven-year testing period exceed prescribed premium limits (7-pay premiums).

Surrender charges will not be waived if the policy is surrendered under an external 1035 exchange (except in FL). A decrease charge will be assessed if a reduction in the specified amount is requested during the waiver of surrender charge period. However, if a partial withdrawal results in a reduction of the specified amount, the withdrawal charge is waived. There is an additional charge for this rider and it must be applied for at the time of application.

Sammons Financial[®] is the marketing name for Sammons[®] Financial Group, Inc.'s member companies, including North American Company for Life and Health Insurance[®]. Annuities and life insurance are issued by, and product guarantees are solely the responsibility of, North American Company for Life and Health Insurance.

Smart Builder IUL (policy form series LS187) and Smart Builder IUL 2 (policy form series LS187), or state variation, including all applicable riders and endorsements, are issued by North American Company for Life and Health Insurance, Administrative Office, One Sammons Plaza, Sioux Falls, SD 57193. Products, features, riders, endorsements, or issue ages may not be available in all jurisdictions. Limitations or restrictions may apply. North American is not licensed in New York.