

**TRANSACTIONS OF SOCIETY OF ACTUARIES  
1961 VOL. 13 PT. 2**

D356 DISCUSSION OF SUBJECTS OF SPECIAL INTEREST

*One-Year Term Dividend Option*

- A. What mortality and expense bases are appropriate for the determination of rates for the One-Year Term Dividend Option?
- B. In determining rates for the option from year to year, should consideration be given to the mortality experience under the option itself or of the participating policies as a whole?
- C. What are the arguments for and against making this term insurance convertible?

MR. NORMAN L. CAMPBELL: In the National Life about 85% of financed business carries the term dividend option, with a policy average size of \$65,000. We do not have a high early cash value or special policy. If we can characterize financed insurance as a currently inexpensive type of term insurance in large amounts with poor persistency, it may be argued that new policies with the term dividend option will show poorer mortality than the balance of the Company's new business, which contains only a minor part of financed insurance. It doesn't seem practical to have a separate basic dividend scale for policies with this option, so that any higher mortality of the basic policy combined with the option may have to be charged in total against the option. If such extra mortality exists, it is too early to determine the degree, and some arbitrariness is indicated in the choice of rates; high enough to render unnecessary a change in rates for some time to come, but not so high as to price the option "out of the market."

Low rates for the option will make financed insurance proposals using the option more competitive, and create a bias toward financed insurance sales. If the Company doesn't wish to encourage such sales, higher rates are desirable, and National Life made such a change this year.

With regard to expense charges, we feel that 75 cents per \$1,000 is adequate, because of the high average size policy (\$60,000) employing the option.

MR. HARRY WALKER: Since the term dividend option will be used predominantly for male lives, the mortality basis should be a percentage of the combined male/female experience of the company. Regulation 39 requires that the rate basis be determined annually on a basis consistent with regular dividend scale mortality. The net premium based on dividend mortality should be loaded for the extra mortality arising from the experience being predominantly male, and also for premium taxes.

With electronic data processing, it is probably no more expensive to translate the dividend into one-year term insurance than to pay it in cash. But special promotional materials and illustrations could be a substantial

element of expense that could justifiably be assessed against policies with the option.

If the option is available only at or shortly after issue, or subject to evidence of insurability, there is no reason to expect any worse experience than for policies generally, unless there is a relatively high frequency of cancellation in the later years, indicating that possibly the good lives are dropping out.

**MR. HERBERT W. HICKMAN:** The Prudential will soon offer a one-year term rider on many standard, nonterm policies of \$10,000 or more, both on new issues and on policies issued since 1947. The amount of term insurance will be the amount that can be purchased using the policy's entire dividend, or 30% of the face of the policy, whichever is the lesser. In practically all cases, this will mean the amount of term is 30% of the face, or at least \$3,000 per rider. The rider will terminate no later than attained age 70.

The guaranteed maximum rate for this rider will be the net premium on the policy's valuation basis, which has been 1941 CSO 2½%, since 1947. The actual rates will be based on the mortality assumptions used in determining the regular Ordinary annual dividend scale, with an expense loading of 75 cents per \$1,000 of term. Our expense investigations indicate that this loading will be sufficient because of the efficiencies inherent in having a constant amount of term insurance, namely 30% of face, and in having at least \$3,000 of term per rider.

**MR. ANDREW C. WEBSTER:** The important point is to avoid selection at issue. If you start to add this with scant evidence of insurability after policy issue, you may get a selection against you which might operate quite severely on the option itself.

**MR. CAMPBELL:** Considering section C, the conversion privilege must be exercised at a time when for some years thereafter the term protection would continue to rise, even with relatively adverse changes in future dividends. Good lives would tend to convert, and poor lives would keep the option, which might be considered an additional reason to keep term changes high. Conversion charges should cover the difference between select and ultimate mortality during the select period of the new policy, reduced by usual underwriting costs. We see no real desire to convert on the part of the policyholder, and the privilege would seem to be more important to the agent in selling than to the home office or the policyholder in later years.