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INDIVIDUAL INSURANCE

Adoption of 1958 CSO Mortality Table

A. What new features of actuarial interest have companies incorporated in their contracts or basic rate structures in connection with the introduction of the 1958 CSO Table?
B. What problems have companies encountered in the filing of their new policy forms with the state insurance departments?
C. What effect on the incidence of dividends results from using the 1958 CSO Table instead of the 1941 CSO Table? What problems arise involving maintenance of consistency in net cost between old and new business?

MR. ROBERT E. SLATER: The John Hancock introduced the 1958 CSO Table into its premium notice and monthly debit ordinary lines on January 1, 1963. Since 1954 the company has issued two series of premium notice contracts. One series known as the Multiple Protection Series issued up to $5,000 has a waiver of premium and an accidental death and dismemberment benefit included automatically; the other series, which is issued for amounts of $5,000 and over, has the benefits available on an optional basis. All series of ordinary contracts have the same cash values and dividend scale structure with differences adjusted by the differential premium rate. This is done to minimize the material which must be furnished the agency organization.

As of January 1, 1963, John Hancock, which had previously operated on a four-band system of premium discounts, changed to a policy-fee basis for all policies issued above $2,000 in the premium notice line and above $1,000 in monthly debit ordinary. A modified policy fee basis is used for amounts smaller than these. Premium rates on the new Century Series approximate the rates on the previous basis at $5,000 and are generally higher for smaller amounts and at the younger ages, and lower for amounts over $5,000 and at the older ages. It is anticipated that premiums collected would be about the same on the new basis as on the old if the agency organization writes the same kind of business it has in the past.

John Hancock has recognized that collection costs occasioned by more frequent premium payments do not increase proportionately with larger premiums by incorporating a collection fee in the premium conversion table for installment premiums.

Previously, the company charged off excess first-year expense over the first twenty years of the policy so that the cash value became equal to the net level reserve at the end of twenty years. As of January 1, 1963, this was changed so that excess initial expense is written off in the first ten years and the cash value becomes equal to the full reserve at the end of ten years. Extended term insurance is based on the 1958 CET Table. Because of higher cash values between the tenth and twentieth years, settlement dividends, which were previously generally available at the end of ten years, will now become available at the fifteenth year.

Reserves are based on an interest rate of 3 per cent for the first twenty years and $2\frac{1}{2}$ per cent thereafter, assuming level premiums and using continuous functions. This basis produces reserves approximating those on our former 1941 CSO $2\frac{1}{2}$ per cent basis for the most important plans and at the more important durations. It seems reasonable and proper to guarantee a higher level interest over the near term and to drop to a more conservative rate after twenty years in view of the current high level of interest rates.

The John Hancock has moved away from rigidly packaged plans and has introduced additional riders in order to meet more precisely the varying needs of the insuring public. The family policy has been replaced by a family rider which permits variation in the relative amounts of insurance on the husband, wife and children. We have eliminated the necessity for numerous separate waiver of premium rates for riders by including an allowance in the rider premium for automatically providing the waiver benefit if it is provided under the basic policy. Prior to January 1 the company had several plans which were sold to females only. Under the new program female risks will have a reduced premium for all plans issued for $5,000 or more with the same cash values and dividends as for male lives. With regard to riders on female lives, a premium discount will be given if the basic policy is issued with a female discount.

In 1962 the company introduced several new term plans with a three-year modified premium. Under the new program all term plans except the five-year term have a three-year modified premium. Furthermore, the level of term plans has been reduced generally. We have also introduced a new whole life contract with preferred underwriting with a minimum amount of $25,000 and having a three-year modified premium.

The Century Series has a double layer of accidental death coverage in its Multiple Protection Series and as the coverage provides for triple indemnity for common carrier accidents this means the company can be liable for five times the face amount under certain circumstances.

We have introduced more liberal settlement options and have increased the guaranteed rate of interest on funds left on deposit from

2 to $2\frac{1}{2}$ per cent. The guaranteed rate for other settlement options has been increased to $2\frac{3}{4}$ per cent.

Substandard extras for medical impairments and occupational hazards have been reduced significantly. In addition, the John Hancock has provided for risks rated as high as 1,000 per cent of standard.

Dividend scales have been increased on all business in force at the time of the introduction of the Century Series, so that the company experienced no difficulties in net cost comparisons between old and new business.

We experienced no unusual difficulties in getting our contracts approved by the various state insurance departments; in fact, service appeared to be better than usual.

MR. HARRY WALKER: Equitable Life Assurance Society of New York introduced its new series based on the 1958 CSO Table on February 1, 1963. In general, we continued the pattern adopted when we first went to graded premiums on January 1, 1959, except for the addition of one more size band covering policies of $25,000 or more.

A distinctive feature of our graded premium structure has been separate scales of cash values and dividends as between policies for under $10,000 and $10,000 and over. This feature has been continued in the new series, and we note that some other companies are now using this technique also. It is our view that the separation into two broad dividend and nonforfeiture value classes enables the company to follow its experience more closely in dividend apportionments and in establishing cash values than a system involving common dividend and cash value scales for all premium classes.

There are several aspects of Equitable's new program that may be of general actuarial interest, viz.:

1. Classified letter extra premiums terminate automatically on the policy anniversary nearest age 70 or 20 years after issue, if later.
2. Our Joint Ordinary Life policy incorporates a "Survivor's Insurance Option," and a "Survivor's Temporary Insurance Benefit." Under the first option when the policy matures at the first death, the survivor has the option within 90 days to purchase a new policy without evidence of insurability, the insurance to take effect at the end of the 90 days. Under the second benefit if the survivor dies within the 90-day period after the first death, the face amount is payable on account of the survivor's death in addition to the amount that has been payable on the first death. These benefits apply only if the first death occurs before the policy anniversary nearest the older life's 70th birthday. The benefits are not available if either life is rated up at issue.
3. We have a more liberal life income settlement option basis for policies whose

reserves qualify as "pension plan reserves" under section 805(d) of the Internal Revenue Code than for regular policies. There is no difference in the mortality basis, but the guaranteed interest rate is 3 per cent for the qualified pension plan reserve cases and $2\frac{3}{4}$ per cent for regular issues. This recognizes the more favorable income-tax treatment accorded pension-plan reserve cases under the Internal Revenue Code.

4. We included in the new series as a matter of contract our so-called "103 Per Cent Annuity Option" which had been previously available to a limited extent as a matter of practice. Under this option the payee may apply the policy proceeds to secure an annuity in any form issued by the Equitable at time of settlement with income equal to 103 per cent of the income otherwise available at current rates (no commissions being paid to any agent under this option). We expect greater use of this option than heretofore because our immediate annuity rates involve the use of the investment year method of allocating investment income. Currently, for example, a payee under a policy of the new series would find it more advantageous to elect the 103 per cent annuity option rate than the guaranteed rates of the life income option in the policy.
5. The table of nonforfeiture values in the new contracts is completed by EDPM equipment for the particular issue age and for the face amount of the policy. Thus for the first time our policies show cash values and reduced paid-up values for the full face amount rather than per $1,000 of face amount.

MR. ZEHMAN I. MOSESSON: About two years ago the Prudential decided to aim for January 1, 1963, as the introduction date of the 1958 CSO Table, since we believed there were decided advantages in completing the task as soon as possible. Comprehensive studies of our market indicated a need for two series of ordinary policies: one, which we call the "Gibraltar Series," for the moderate-income group (basic amounts of less than $10,000), and the other, which we call the "Estate Series," for higher-income groups (basic amounts of $10,000 or more). The Estate Series cash values reach full reserves at the end of ten years and are higher at the early durations than the Gibraltar Series values. Standard policies of the Gibraltar Series include, without specific extra premium, a waiver of premium benefit, a benefit in event of loss of eyesight or limbs, an accidental death benefit, and a nonoccupational vehicle accident death benefit. Gibraltar Series policies may be sold on a debit basis if the monthly premium does not exceed $20. Policies other than weekly premium previously issued on a debit basis are no longer available.

The new policies are on an age last birthday basis. In general, rates for females are equal to those for males three years younger. We no longer grade insurance benefits for policies issued at age 0. The guaranteed interest rate for settlement options providing an annuity certain has been increased to 3 per cent. Changes in the policy format were made to secure the maximum advantages of electronic issue. Necessary variable information is mechanically printed on a continuous form, which is then assembled with fixed printed pages to complete the policy.

In regard to problems encountered in filing new policy forms with the state insurance departments, our answer is that very few were encountered. The most important reason for this is probably the fact that we developed nonforfeiture factors in such a way that it could be shown without difficulty that they are not greater than the adjusted premiums defined in the Standard Nonforfeiture Law. We enclosed with our submissions a series of memorandums which demonstrated our compliance with the Standard Nonforfeiture Law.

Our nonforfeiture values are based on the 1958 CSO and CET Mortality Tables at $2\frac{1}{2}$ per cent, using age last birthday and with provision for immediate payment of death benefits. We compiled sets of monetary tables on this basis and with the first major submission we sent each department the first volume, which contains basic functions. This enabled the department to check the values and, more important in my opinion, showed graphically how large an undertaking our revision was and how much care had gone into preparation. Later we sent most of the departments the second volume containing net level premiums and terminal reserves.

A second important reason for our relatively smooth sailing was the way we drafted our submission letter. The letter itself was brief, with most of the details in separate exhibits. One exhibit listed the forms to be replaced when the new forms came into use. Another exhibit served as a guide in reviewing the forms. This exhibit compared each new form with the pilot form or some other form of the new series previously or simultaneously submitted rather than referring to the form which it was intended to replace. The insurance departments apparently found this approach quite acceptable. A specific effort was made to tailor submission letters and exhibits to the individual requirements of the departments.

I might say a word about our time table. Our operative date was January 1, 1963. A pilot filing was made in September, 1961. In April, 1962, we submitted slightly revised versions of the pilot forms, together with a large number of other forms. Remaining portions of the new series were submitted in May, June, and August, 1962. By November 1, 1962, we had received approvals or tentative approvals from almost every state, so that final cleaning up was a minor task. As of January 1, 1963, there were only three minor rider forms which were not available for use in all states.

MR. LOWELL M. DORN: Under the New York Life's 1958 CSO edition a 3 per cent interest rate is used across the board. We felt the 3 per cent guarantee would emphasize the attractiveness of life insurance from an investment standpoint. The 3 per cent rate applies not only to reserves but also to dividend accumulations and all settlement options. Under our previous (1941 CSO) policy edition reserves were based on $2\frac{1}{2}$ per cent, dividend accumulations were at 2 per cent, interest only settlement options at 2 per cent, and installment and life income options at $2\frac{1}{2}$ per cent.

In the new edition we continue to use fully continuous functions for reserves, and age nearest birthday. Extended insurance values are based on the 1958 CSO Table rather than the 1958 CET Table.

We did not previously have a graded premium program but had a number of special policies subject to $5,000 or higher minimum amounts. In the new edition we adopted a graded premium program based on four amount bands. For most life and endowment plans we developed two policy series, one series covering face amounts under $10,000 and the other covering amounts of $10,000 or more. In the under-$10,000 series premiums are graded in two amount bands—$2,000–$4,999 and $5,000–$9,999. There is a constant differential of $1.75 per $1,000 between these bands for all plans and issue ages. Likewise the $10,000-and-over series is split into two bands, with a dividing line of $25,000 and a constant differential of 50 cents per $1,000.

The differentials between the $5,000–$9,999 and $10,000–$24,999 bands are not constant but vary by plan and issue age. We think this system reflects actual expense differentials more accurately than either a conventional band system or a policy fee system, under which premium differentials for various face amounts are the same for all plans and issue ages.

Policy provisions are identical in both the under-$10,000 and $10,000-and-over series. However, each series has its own dividend scale and nonforfeiture values. Our testing indicated that cash values could equal the full reserve at the end of five years for the larger amount series and at the end of ten years for the smaller amount series.

For term policies (subject to $5,000 minimum) we are now grading premiums by using the three highest amount bands and constant premium differentials. The graded premium concept was extended to supplemental coverages and riders but only two amount bands are used. Premiums for these are graded according to whether the basic policy is under $10,000 or $10,000 or more. This approach is also used for special class extra premiums. Premiums, nonforfeiture values, and dividends for females are based on the 1958 CSO Female Table, which means generally a three-year age setback for females. Waiver of premium charges for women are higher, and accidental death benefit premiums for women are lower than for men, reflecting recent experience.

Our new life insurance premiums are generally moderately lower than previously. In the $10,000-and-over amount range premiums are about 3 per cent lower on whole life and about 6 per cent lower on other plans. In the $5,000–$9,999 range there are reductions of about 5 per cent. In the under-$5,000 range the reductions amount to about 3 per cent. We also reduced premiums generally for term and family plans and for supplemental benefits. Special class extra premiums were reduced about 12 per cent on the average. We introduced a new special class running up to 1,000 per cent. We made a general reduction in occupational flat extras; about 40 per cent of the occupations previously requiring a rating will now be considered standard. The graded premium concept was extended to annual and single premium deferred annuities. We also made some important changes in our single premium immediate annuity program. They are now on a nonparticipating basis, whereas they were previously participating. Their new rate structure reflects our adoption of the investment year allocation method.

MR. CHARLES S. SCHNELLE: Some time ago the New York Life decided to adopt an issue operation based on maximum use of electronic equipment. It was evident that the format of policies electronically produced would differ from any format previously used and that there was a real possibility of questions arising from various Insurance Departments. The issue operation we planned would require designing a face page suitable for every insurance and annuity plan in our portfolio since we visualized this page as a continuous form with no variations in preprinted material. The operation we planned meant, among other things, that the form number and the brief description would have to be printed by the electronic equipment.

We decided to run a test on the acceptability of a format designed for such processing before making final decisions on the content of the 1958 CSO policies. We ran a test on a pilot form containing the same policy provisions and, in general, the same language as were contained in the then current previously approved policy forms. We met with representatives of the New York Insurance Department (and with one other insurance department) after filing. The fundamental point made was that the only new element in the electronic format was the new treatment of form number and brief description, since the only other material inserted in the continuous face page by the electronic printer would be the variable information normally inserted by typewriter. By locking form number and brief description into the machine, we were establishing a process as reliable as printing this information from a plate. The state insurance departments gave us a sympathetic hearing and exhibited a most progressive attitude after we had explained our plans and methods. Approvals were given to our electronic format forms in short order. When we filed the 1958 CSO forms, therefore, we had very few and relatively minor approval problems. It is also of interest to note that, by adopting the electronic format, we were able to reduce the number of policy forms we had to file from more than 300 to only 27.

MR. CHARLES M. STERNHELL: In regard to the second part of the question, the first problem was whether to revise dividends for previous policy editions to conform with the new amount and sex classifications adopted in our 1958 CSO edition as described by Mr. Dorn. We decided not to vary dividends on prior editions by sex and amount where no such distinction was made in the premium rates for these prior editions for the following reasons:

1. We believe that dividends should be allocated on the basis of classes established by conditions at time of issue. This is in accordance with the definition of "dividend class" established in the Rhine case.
2. If we started to vary dividends for old policies by amount of insurance or sex where no such distinction existed in the original rates, policyholders could argue that we were changing the rules in the middle of the game.
3. We did not anticipate any serious problem involving replacement of prior issues by our 1958 CSO edition. Although net payments are generally lower under new policies, net costs are generally more favorable under prior editions. In addition, we adopted a new replacement rule to the effect that, when a new policy is classified as a replacement, the first year commission will be equal to the excess of the normal first-year commission over the actual first-year commission paid on the policy being replaced. New York Life's new program was introduced over two months ago, and so far there are no signs of a serious replacement problem.

In regard to maintaining consistency in net cost between old and new issues, we do not feel that it is necessary to introduce artificial factors that will produce approximately the same illustrative cost picture for new issues as for old issues. We feel that basic differences in reserves, cash values, and premium differentials by amount and sex will naturally operate to produce different cost patterns. As we see it, equitable distribution of surplus is obtained when dividends are determined on the basis of asset-share calculations reflecting consistent mortality, lapse, and expense factors for old and new issues.

In regard to the first part of the question there is no general pattern that will describe the relationship between the incidence of dividends in the new and old series. New York Life uses the three-factor dividend formula, with mortality and interest contributions determined in the conventional manner, but with the loading contribution acting as a balancing factor designed to produce the appropriate accumulation of surplus on the basis of asset share calculation. Naturally, the change from a 1941 CSO $2\frac{1}{2}$ per cent reserve basis to a 1958 CSO 3 per cent basis resulted in a significant reduction in the level of mortality and interest contributions. Loading contributions, however, were generally increased for the new series so as to produce reasonably consistent asset-share surplus accumulations for both the new and the old series.

Marketing of Life Insurance

Why are fewer individual life insurance policies being sold than four or five years ago? To what extent is the trend attributable to developments within the business such as graded premiums, family plans, and changes in mass selling techniques? To what degree might it be due to the competition of other media, such as social security benefits and mutual funds? Does this trend raise a question whether insurance companies are adequately covering the needs of the public?

MR. RONALD G. STAGG: An examination of the total sales for all companies as well as the sales records of a group of nineteen ordinary companies indicates clearly that the number of ordinary policies sold each year has leveled off or decreased in the last five years. There are many factors contributing to this decrease, namely:

a) Competition from Social Security and other forms of security provided by the government at the expense of the taxpaying public.

b) Competition from mutual funds and savings and loan companies.

c) Closely related to the rise of mutual funds and other competing media is the fact that life companies have failed to meet the fear of inflation that has been instilled in the minds of many persons.

d) Competition within our own business from group insurance, including the rather recent addition of widows' benefits.

e) The fact that incomes have not kept pace in many instances with rising living costs, leaving less income available for the purchase of life insurance.

f) The effect of rising unemployment.

g) The increased participation in the stock market by the general public.

h) The great and increasing shortage of agency manpower. One estimate is that we shall need to add 35,000 agents (net) in the next ten years in order to *maintain* our present position with respect to our share of the public's dollars. At that, our present position is not a happy one if we remember that the average amount of insurance in force is less than twice the average annual income.

i) The advent of graded premiums has tended to cut down the number of policies written.

j) The fragmentation of an agent's time to the extent that he directs his efforts to the sale of group, accident and sickness, or other related coverages, as well as mutual funds.

k) The increasing use of group annuities instead of pension trust and other individual policies written for pension purposes.

l) The writing of family policies instead of policies on individual members of the family.

m) There is some possibility that irresponsible promotions of new life companies, which are not unheard of, have led to the development of improperly trained and high-pressure agency forces, creating a poor image of life insurance in the minds of the public. It is certainly true that the advent of these new companies has made prospecting, recruiting, and retention of agents more difficult.

n) The attempt of companies and agents to upgrade the latter into what might be called the higher-income market.

In my opinion this last factor is a major cause, possibly the most significant, of the trend we are discussing and justifies elaboration.

It is not possible to quarrel with the desire on the part of the company and agent to write higher average-size policies. This process provides greater income per sale with relatively little increase in effort, better persistency, lower premiums per thousand, and to some extent higher early cash values. Certainly, if an agent aspires to a given level of income, he can, if equipped to do so, more easily attain that level by selling larger policies.

There is even a question, at least in the bigger cities, of whether a successful agent can afford to expend the possibly disproportionate effort and time necessary to write smaller policies. To the extent he goes after larger policies, however, he tends to limit his market to such policies, and gives less attention to the market for smaller ones. If he and all other agents in his agency strive to upgrade, then in effect that agency has abandoned its market for smaller policies.

The tendency of agencies to cover smaller and smaller geographical areas, which obviously springs from a desire to make sales supervision easier and less expensive, may very well lead to spottier geographical coverage by any given company or group of companies. As a matter of fact, the larger companies tend to confine themselves almost entirely to larger cities and in many cases to very limited areas within those cities.

The desire on the part of most companies to limit their sales forces to full-time life underwriters is commendable, but it may well have led to still spottier coverage geographically of the whole market, in that many areas in the country have been left to part-timers, who are usually less well trained in life sales techniques as well as in knowledge of their product.

These trends are not limited to the ordinary companies. Debit agents, too, are upgrading their markets and are consistently writing monthly debit ordinary business in place of weekly premium business and regular ordinary business in place of monthly debit ordinary business. This, too, undoubtedly leads to the ignoring by debit agents of prospects at income levels that at one time they specialized in.

For the reasons just stated, it is quite likely that the lower-income groups, even in the big cities, are being so neglected by life salesmen that they are receptive to mutual fund salesmen and other competitors of ours and are building their modest estates through other means than life insurance. There is a real likelihood that we are not reaching them simply because we are not ringing enough doorbells.

I am impressed with the undeniable fact that we are reaching a smaller and smaller proportion of the public through ordinary insurance. With this situation we can hardly be self-complacent. It is not even sufficient to aim at getting a larger share of the public's savings dollars because this may simply result in a higher proportion of higher premium plans with no increase in the number of sales. This, it might be said parenthetically, is one objection to the current trend of the companies in measuring production in terms of premium dollars rather than amounts of insurance. Something more in the way of sales emphasis is needed which will produce more prospects, more calls, and more sales. After all, it is in terms of number of policies and amounts of insurance, rather than premiums, that the ultimate success of our sales effort must be measured; a widow does not care how much her late husband's insurance had cost.

We cannot simply shrug our shoulders and say that this is what the public wants or that our agents are responsible for the trend. Company attitude is a major factor, and company policy has a great deal to do with the apparent shrinking of our market and with our failure to reach all segments of the public.

An LIAMA survey suggests that the majority of our companies are not so concerned about the shrinking number of sales as they might be and not willing to take corrective steps unless assured that those steps will have no adverse effects, such as higher lapse rates, lower average size policies, and higher expenses. This survey was, however, made in 1953 and might possibly bring out a different result if made now.

What is the extent of the collective obligation of our companies to try to reach all insurable prospects without qualifications as to age or earnings? Strictly speaking, I suppose there is no real compulsion to do so other than the social undesirability of doing so—whatever that means! We can, if we choose, always leave it to George to cover the fringe areas —George, in this case, being the government, or our competitors in other fields, such as mutual funds.

Most of us would, however, say that it is not in our best interests or those of the public to permit a blind spot to develop in our coverage of the public. Such a spot would be likely to fester and to grow malignantly to a size which would ultimately embarrass us mightily, and which might lead to the conclusion in the minds of the public that our interests are selfishly linked with the higher-income classes. This is a trap that we should not permit ourselves to fall into. Let us, therefore, examine a few things that might be done to improve this situation.

1. We must convince the public that life insurance is a basic rather than a marginal need and that they should not wait to buy it until after their basic needs have been taken care of by mutual funds, savings plans, Social Security, and group insurance. These other media will simply not take proper care of their basic needs.

2. It may be that, like the automobile industry, which presently offers four hundred or more different models, our prospects and our agents are thoroughly confused by the multiplicity and complexity of our products.

3. It may be that we could improve the packaging of our products. I do not propose to get into an argument with our sales-promotion staffs on this point.

4. Possibly what is needed if we are to reach all our markets is a dual recruiting system within an agency accompanied by a dual training system. One kind of training would be relatively simple, dealing solely with the basic elements of salesmanship, such as prospecting, closing, etc. This kind of training would be administered to agents who would be selected with a view to selling in the lower-income market. More advanced training in estate analysis, etc., would be offered to agents selected for the higher-income market. There seems to be no reason why two kinds of agents could not coexist in the same agency, possibly subject to two kinds of supervision, and why both kinds of agents could not earn competent livings.

5. As someone has said, there ought to be a middle path between a wholly variable-dollar approach and wholly fixed-dollar approach to the problem of providing protection and savings through the medium of life insurance. This suggests the investment of a higher proportion of life company assets in equities.

6. A really promising field for ordinary sales in the next decade should be that of payroll deduction or salary savings. The anticipated development of many small service industries points the way to this; and there are many small businesses not so covered now.

7. Automatic bank-check plans offer some possibilities in the lower-

income field, though many blue-collar and even white-collar workers do not now have checking accounts.

8. One-stop or multiple-line selling, not really tried yet, may turn out to be feasible in the lower-income field, where insurance needs—life, fire, and casualty—are simple.

9. There are, in this country and Canada, minority ethnic groups in considerable numbers. It is probable, because of language problems, that these are not adequately insured, coming as they do largely from countries where life insurance is not so common as it is here.

Your speaker is not so unrealistic as to believe that the problem confronting us is as simple as he has intimated and that we can sell more policies merely by ringing more doorbells, by hiring more and better agents, by giving them better training. There is, however, just enough logic in all these suggested steps to imply that steady progress toward our objective can be made if we keep working away at ways and means of accomplishing these steps.

In essence what we should like to do is to make a good life insurance program, sociologically speaking, a status symbol, to the end that the public will accept the concept that one has not "arrived" unless and until his family is adequately insured.

MR. JOHN E. SMITH: The 1 per cent drop in ordinary policies sold from 1957 to 1961 does look serious in the light of the 19 per cent increase in total United States population from 1950 to 1960 and the 18 per cent increase in disposable personal income from 1957 to 1961. However, there are a number of considerations which temper this picture and lead me to believe we may have covered as high a proportion of the population by ordinary policies in 1961 as in 1957.

First, the United States population in the chief insurance buying ages of 25–39 increased only 1 per cent from 1950 to 1960, while the total population was increasing 19 per cent.

Second, the family policy sales increased from 1 per cent to 12 per cent of the market from 1956 to 1961, and this increase of 1,000,000 policies covered 1,000,000 wives and about 2,000,000 children. Had these 3,000,000 been covered by separate policies, the 1 per cent decrease would have been better than a 30 per cent increase. Further evidence of the family policy effect over the 1956–61 period is the decrease in policies sold to females of 10 per cent, a decrease of $3\frac{1}{2}$ per cent in policies sold to children, and a 9 per cent increase in policies sold to males.

The third consideration is the grading of premiums by size, with the tendency to fewer and larger sales. Some idea of the effect of this shift can be seen from consideration of one possibility. From 1956 to 1961 the average size policy increased 20 per cent. If the ultimate amount per individual is to remain unchanged and is to be accomplished by fewer purchases, the number of purchases would be reduced by 17 per cent. Depending on the average frequency of purchase, this effect may become stronger in the next five years as purchases are delayed by larger purchases over the last five years.

Agency Compensation

A. Are the commission limitations of Section 213 realistic under current conditions? Do they inhibit the recruiting and retention of competent salesmen? Would a different distribution between first year and renewal (i.e., more first year, less renewal) be more effective for building and maintaining an agency force?

B. Have the earnings of agents kept up with rising living costs? What is the anticipated impact on agents' earnings of changes in premium levels arising from adoption of the 1958 CSO Table?

C. Are there developments in the business affecting the earnings of agents that suggest that significant modifications of the agency system can be anticipated in future years?

MR. EDWARD A. DOUGHERTY: Neither the commission limitations nor many of the other provisions of Section 213 are realistic under current conditions. Section 213 imposes unrealistic restrictions on *how much* money a life insurance company is allowed to spend, and it imposes unrealistic restrictions on *how* a company may spend what it is allowed.

As to the amounts of the limits themselves, the present formulas fail to recognize two changes that have occurred in our industry in recent years:

1. The cost of living has gone up. It costs more to run an office—whether a home office or a field office—than it used to. It costs an agent, and everybody else, more to live.
2. A higher proportion of term insurance is being sold today than ever before. Term insurance not only has lower premiums than permanent insurance but also has a lower first-year commission *rate* limit under Section 213 than most permanent plans. Thus, in a New York company, that is, one licensed to do business in New York State, whether domiciled there or not, the poor soliciting agent is caught in a two-way commission squeeze. The rate of commission is lower on term insurance than on permanent plans, and the amount of premium against which that rate is applied is lower on term insurance than on permanent plans.

Offsetting the effects of these changes is the fact that people *are* buying more dollars of life insurance than before. They have to if they want to accomplish the same degree of protection in this inflated economy. I question, though, whether this increase in the face amount of insurance being bought has offset the cost-of-living increase, as far as the life insurance company's corporate budget is concerned; and I question whether it has offset the cost-of-living increase *and* the commission squeeze, as far as the soliciting agent's personal budget is concerned.

These are difficult questions, and they cannot be answered completely by statistical averages, for the situation in each company and for each agent is so different.* I personally am convinced that there is a very serious problem to be faced, particularly for our soliciting agents. Is the high rate of turnover among life insurance salesmen related to this problem? Again I can only pose a question. I do have a strong conviction that all three of the expense limits of Section 213 need to be liberalized in the light of current conditions. Certainly, many companies do not need this increase in the limits on how much they can spend, but some companies do. At the Union Central Life, for instance, we need to spend more than most companies of our size to increase our sales; yet we are not permitted, by Section 213, to make an investment which in any other industry would be considered sound business judgment.

The restrictions on how a life insurance company may spend what it is allowed result from the formulas which describe the limits of expense and of commission rates, and from the fact that there are three expense limits rather than just one. Quite aside from how much you may spend, this crazy-quilt law limits the discretion which management can exercise in at least four ways.

1. It limits *what* you may spend your money on. For example, if you save some money on home-office operations, you may not be able to spend it on development and promotion. If you save money on a general agent's expenses, you may not be able to spend it on extra overrides.
2. It limits *where* you may spend your money—as to home office versus field.
3. It limits *when* you may spend your money—
   a) As between policy years. You may not pay extra first-year commissions by reducing renewal commissions.
   b) As between calendar years. You may not carry-over Schedule Q margins; that is, margins achieved in 1962 do not affect your limits in 1963.
4. It limits *to whom* you may pay your money. For example, you may not pay a general agent as much as you may pay a branch manager.

In short, there are many good ways to conduct a life insurance business, but some of these are not permitted to New York companies. Non-New York companies that want to do business one of these other ways, or that are already deeply committed to one of these other ways, have the New York State market barred to them. In this respect Section 213 has the effect of a tariff barrier.

However, the non-New York companies that wish to do business in some way that is not permitted by Section 213, but that want to get into the great New York State market, have found a way out that is to all intents and purposes denied to a New York company that already

* Milton J. Goldberg concurred.

has a large stake in that market. The non-New York company can form or acquire a wholly owned New York subsidiary. This has been done in several cases. In commenting on this, the president of my company has said: "There seems to me to be something incongruous about this. I have such a profound respect for New York's laws that I assume naturally that this must be eminently fair, but somehow it leaves me with an uncomfortable feeling that something may have been done to the rest of us which if we ever stop long enough and think over may be very disillusioning." Almost no non-New York companies have chosen the alternative of conforming their operations to the Section 213 strait jacket.

Should the New York companies be permitted more first-year commission and less renewals? I read into this, perhaps erroneously, the implication that the present value of commissions would be kept the same but that they would be distributed differently between policy years. Certainly, it would help if the commission limits were defined in terms of the present value of all commissions rather than having the rigid first-year and renewal pattern now specified. Then management could use its own discretion, in this one area at least. But this is not enough. The present value of allowable commissions should be raised above its present level, and the expense limits should be simplified into one over-all limit that is more liberal than the present total expense limit.

MR. MILTON J. GOLDBERG: The Equitable is promoting a philosophy, and it is no secret. We hope you will accept our challenge and try to beat us—and that is to build the superior sales force of the entire life insurance industry, and this means looking at commissions from now on and not volume per se.

We in the Equitable think that through manpower development we will achieve production growth in satisfying measure and that, as long as an agent is able to earn a decent living, he will stay with us and bring us that production.

With respect to the current overemphasis on term insurance—if you want your men to earn a better living, then do not let them sell 70 per cent term insurance. There is a place for term, and permanent and term are not incompatible.

I am opposed to companies introducing special policies that are "special" in that they call for reduced commissions to agents. I could come out with a whole life policy that would pay a 25 per cent first-year commission and corner the entire market. It would be six months before you fellows could get a drop of business, but a year from now all agents would be getting a 25 per cent first-year commission instead of the 50 per cent or 55 per cent to which they are entitled.

MR. ROBERT C. TOOKEY: The limitations of Section 213 are quite unrealistic for the new company. Yet, while they do add to the difficulties of recruiting and retaining competent salesmen, agency-building is just about as tough a job for the unrestricted companies that do not operate in New York.

A different distribution of commissions between first-year and renewal is just one way of attempting to solve the problem of agency development. There has been considerable discussion recently of telescoping commissions so that practically all of the commission payout would be accomplished within the first three or four policy years. While this would certainly help in building an agency force, persistency of the policies of later duration would depend principally on the whims of the policyholders, as there would be little financial incentive for anyone in the agency organization to keep these policies in force.

Generally speaking, the earnings of agents have kept up with rising living costs. The average earnings of salesmen in all fields have increased from $3,000 a year in 1933 to over $10,000 a year today. The LIAMA bulletin of September 17, 1961, compared an agent's potential earnings in 1940 to those in 1960. The agent with the best persistency would have made $11,212 in 1960 compared to $3,890 in 1940. For the agent with the poorest persistency, these figures would be $8,600 and $3,121, respectively. Each agent was assumed to produce fifty-two policies per year, with the average size policy increasing from $3,200 in 1940 to $12,200 in 1960, and the average unit premium declining from $30 per thousand in 1940 to $20.70 per thousand in 1960. Average first-year commission rates were 45 in 1940 and 40 per cent in 1960, with nine renewals of 5 per cent for both periods.

The earnings of the new agent who concentrates in package selling could be affected by the reduced premium levels arising from the adoption of the 1958 CSO Table. However, there would probably be no reduction in the earnings of the more seasoned and sophisticated agent who sells by what they call the "ratebook method." In the ratebook method the agent determines (*a*) what the prospect can afford to pay and (*b*) what plans will have sufficient appeal to the prospect so that he will pay the amount determined in (*a*). When deciding between two plans with equal appeal, the agent will select the one that pays the higher commission.

There will probably be some significant modifications of the agency system in the near and distant future. Because of competition, it is unlikely that many companies can pump money into agency development at a higher rate than they are today. More companies will go after brokerage business, as indeed they are doing today. We may see a change in both the financing of agents and in the agency contracts. The one-stop sale concept will probably continue to gain acceptance. One of the primary advantages of combination selling is the reduction in the number of failures in the insurance business. Many agents who do not have it as life insurance salesmen find that they can make ends meet with commissions earned from sales of fire and casualty insurance. Because of the high overhead in large cities, there will be a shift toward branch-office type operations in these metropolitan areas; the general agency system will continue to work well in towns of 50,000 or less, where overhead is much lower.

We may see a variety of methods used to get men into the life insurance business without incurring the customary financing cost. A good example would be job moonlighting, wherein the prospective agent works at a rather routine undemanding job during the day (for example, store detective) and tries his luck at selling life insurance at night. By easing into the business in this manner, he develops his techniques and builds his confidence without financial worry. If he makes a go of it, he can later give up his daytime job and devote full time to selling life insurance. If the agent does not succeed, neither he nor his general agent nor the company is out anything. To many, this may seem like a return to the horse-and-buggy days of part-time salesmen, but it does have advantages.

Common reasons for changing a compensation scale include (1) failure of the existing scale to focus on profitable policies; (2) failure of percentage sales costs to decrease as volume goes up; (3) failure to keep from losing the best salesmen to competition; (4) failure to attract the quality of salesmen needed; (5) failure to implement marketing strategy; (6) failure to stimulate salesmen to maximum production; (7) failure to reward salesmen for missionary work done; and (8) failure to provide salesmen with the means of accumulating an estate or to provide pension and other fringe benefits.

To remove some of these flaws, compensation scales will probably be revised to make the commission payout more coincident with activity. Remedial measures include further telescoping of commissions to attract the quality of men needed, relating amount of vesting to years of service to keep from losing the best salesmen to competition, providing greater rewards for persistency, focusing on desirable business and perhaps allowing an actual increase in compensation for a high level of production to stimulate salesmen to maximum production. An example of this last measure would be a production bonus based on the excess of first-year commission income over, say, $3,000 a year. The bonus might be 20 per cent of this excess, so that the productive agent meeting certain persistency requirements actually receives an effective higher commission rate on his business.

We may see a much higher first-year override paid to a general agent on premiums written by agents in their early contract years. This would provide the general agent with a massive incentive both to recruit and to develop new agents, thus also rewarding him for missionary work done. The rich may get richer and the poor may get poorer under such a system, but it will relate the outpay of commissions more closely to the value of service performed and eliminate some of the shortcomings of present-day agency compensation scales.

The life insurance field will continue to be invaded by outside enterprises that will form life company subsidiaries to work a semicaptive market. Many retail organizations are making feasibility studies with this in mind. In most cases, they will not utilize a conventional agency system but will use special merchandising methods, such as mail order. These inroads on the life agent's market may nibble away at the earning potential of the average and below average producer and require periodic review of the agency system. However, any fundamental changes in agency system must await fundamental changes in human nature.

MR. HARRY W. JONES: Recently I was reviewing the Schedule Q returns of six mutual companies operating in New York State under the requirements of Section 213. They reported, for 1961, total ordinary expense of $209.9 million, total field expense of $157.6 million, and total commissions, new and renewal, after elimination of those features of their commission schedules that appeared to be aimed at meeting expenses, of $105.3 million. Differencing these totals and attaching broadly descriptive titles produces the following results:

	Millions	Per Cent
Commissions	$105.3	50
Other field expense	52.3	25
Home-office expense	52.3	25
	$209.9	100

Through long years of life insurance history, the costs of home-office operations have steadily increased by reason of the growth of services to policyholders, taxes, income tax reporting and many other areas. This has been compounded by a steadily increasing scale of compensation paid for manpower. However, these increases in costs have been offset repeatedly through increased use of efficient methods and mechanization. In effect, we have abated the effect of higher pay scales for manpower in our home offices through methods and mechanization which make that manpower more productive and, hence, capable of paying its own way. Bulk or volume provides the basis for this approach to lowering home-office expenses, which presently constitute only 25 per cent of the total ordinary cost.

Field costs, which make up 75 per cent of the total ordinary cost, do not appear to lend themselves easily to this kind of solution. The work of the field force is so largely individual and personal that we have not yet been able to visualize an adequate approach to our market through anything other than manpower. This fact alone means that, in our effort to attract and retain the manpower we need, we are brought face to face with the cost of living and its trend. And the trend in the cost of living has been, and indicates that it will continue to be, steadily upward, not only as measured by the Consumers Price Index, with its heavy, hidden ingredient of taxes, but also through our expanding desire for the nicer things of life beyond the necessities. Thus, for the agent, pressure is exerted for greater take-home pay for personal needs, and on his expenses of doing business before that take-home pay is realized.

Various methods have been tried for making the manpower of our field forces more productive as a means of getting more compensation into their hands. Selling methods and even policy benefits, such as guaranteed insurability and "jumping juvenile," have been designed in an effort to capture the future market. Pricing by size in its various forms has helped many agents toward larger average sales, but, unfortunately, these seem to consume more time and effort; thus the total number of sales made has not held up too well. Fringe benefits in rider form have been attached to basic policies and have helped to expand the premium size of the sale. All these have been somewhat helpful, but none has been notably effective.

It would seem that this area of expense, which, by its nature, yields very little saving in unit cost for large average sales or large volume, must somewhere contain the opportunity for greater ingenuity than we have yet been able to bring to bear. Somehow we will have to find the means of increasing the effectiveness of our manpower so that the resulting profit margins can support the probable increases in compensation, or we may face the need for the "significant modifications of the agency system" which Question C suggests.

It seems to me that these "significant modifications" are to be avoided by all possible effort lest they be found to weaken the agency system, undermine the existence of the business, and thus impair our total value to the public and to our economy.