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DIGEST OF DISCUSSION OF SUBJECTS OF SPECIAL INTEREST

INDIVIDUAL LIFE AND HEALTH INSURANCE

Disability Benefits under Life or Health Insurance Policies

What is the impact of the 1965 changes in OASDI benefits on:

A. Scope of market for private insurance?
B. Underwriting considerations?
C. Policy provisions?

MR. LARRY C. BALLARD: After studying the question, I decided that a little background on disability income insurance might stimulate the discussion. I will, therefore, briefly cover (*a*) the history of disability income insurance, concentrating on the 1920's, 1930's, and 1950's, and (*b*) the present limits of insurance companies with respect to permissible disability income as a percentage of earnings.

I reviewed both the *Records* of the American Institute of Actuaries and the *Transactions* of the Society of Actuaries. My review was concentrated on the twenties, which, I learned as a student, were the "golden" years of disability income; the thirties, which, as I also learned as a student, were the deep, dark years of disability income; and the fifties, which saw the inauguration of social security into the disability income market. I extracted the following representative remarks with respect to each period:

1920 *actuarial comment on disability income* (November, 1927, *Record*, page 309).—"I believe there are a large number of companies charging inadequate rates for Total Disability Benefits."

1930 *actuarial comment on disability income* (November, 1931, *Record*, page 331).—"To quote a previous speaker, I do not know very much about income disability benefits; some day I hope to know less."

1950 *actuarial comment on disability income* (March, 1957, *Transactions*, Society of Actuaries, page 564).—"A challenge to the life insurance business has been created by the entry of the federal government into the field of long-term disability. The small benefits for all except the lowest income groups and the limiting age of 50 for the payment of benefits may stimulate public demand for further coverage."

After reviewing the historical statements of actuaries, I had a change in my preconceived opinion. My original intent in this historical development was to illustrate the optimism of the 1920's, the pessimism of the

1930's, and the cries of anguish of the 1950's. I was unable to illustrate either the optimism of the twenties or the cries of anguish of the fifties. In summary, my historical findings were, in general, that actuaries wear "white hats." I believe that the following points gleaned from my review are pertinent:

1. Most actuaries appeared to see the disaster of the thirties coming.
2. Some actuaries explained the disability debacle of the thirties by saying that disability income was not a life insurance product but rather should be sold only by casualty companies (the logic of this escapes me), and the field force—the bad guys—had forced the companies into the weak disability condition of the late twenties.
3. Certain actuaries heralded the introduction of social security disability income for persons above age 50 as an obvious aid to the expansion by the life insurance industry of the disability income market.
4. After social security disability income was extended to all ages, some actuaries took solace in the fact that the definition of disability was much more stringent than was typical of the disability income products of the insurance industry.
5. My historical review produced the following indictment: Most actuaries exhibited sound judgment but ineffective action.

Next, I investigated the current limitations of disability income to earned income. I made this investigation because I believe this to be the crucial area in which companies should take action in light of the recent social security liberalizations.

Table 1 illustrates what companies considered a safe level of disability

TABLE 1

ILLUSTRATION OF CURRENT INSURANCE COMPANY DISABILITY INCOME MAXIMUMS BASED ON AN UNMARRIED MALE

(Percentage of Gross Earnings Represented by Social Security, Federal Income Tax, and Maximum Disability Income)*

Gross Monthly Earnings	Company A	Company B	Company C
$ 300	116%	67%	116%
450	107	78	113
550	104	82	112
750	96	82	106
1,000	91	84	86
1,700	90	90	87
2,000	92	93	89
3,000	95	99	93

* Social security benefits are included at full 1966 level; federal income tax is computed on the basis of standard deduction.

income. In preparing Table 1, I used the maximum relation between disability income and earnings stated in the *current* ratebooks of three companies.

Table 1 expresses the total disability benefit as a percentage of gross earnings. Disability benefits equal (1) social security; (2) federal income tax, which the disabled life does not pay; and (3) the insurance company maximum disability income benefit.

The footnote to Table 1 indicates the underlying assumptions. The assumption on the social security benefit was that the individual was

TABLE 2

ILLUSTRATION OF CURRENT INSURANCE COMPANY DISABILITY INCOME MAXIMUMS BASED ON A MARRIED MALE WITH A WIFE AND TWO CHILDREN

(Permissible Disability Income, Social Security, and Federal Income Tax as Percentage of Gross Earnings)*

Gross Monthly Earnings	Company A	Company B	Company C
$ 300	149%	100%	149%
450	140	111	146
550	134	112	142
750	117	103	127
1,000	104	97	99
1,700	92	92	89
2,000	90	91	87
3,000	89	93	87

* Social security benefits are included at full 1966 level; federal income tax is computed on the basis of standard deduction.

qualified for the 1966 benefit. This seems to me to be the correct basis for a review of guaranteed renewable or noncancellable maximums.

Table 1 is also based on an unmarried male and shows that (1) among the three companies, Company B is the most conservative, except at the higher income levels, and (2) Companies A and C's current maximum would allow total disability benefits in excess of 100 per cent through annual earnings of $6,600.

Table 2 shows percentages for a family man. For the family situation, all three companies' scales provide far too high a level of benefits below annual earnings of $12,000 per year.

Table 3 shows percentages for the composite of all insurance applicants. It indicates that the current rules produce too much disability income for annual earnings of $9,000 and below.

Definitely, the current disability income maximums are set at a very

high level relative to earnings. It does not appear that the current maximums represent a reasonable compromise of sales and actuarial judgment.

With the liberalization of the social security disability definition, we can no longer take solace in the strict administration of a stringent disability definition. Now is the time to revise our disability income–salary relationships or suffer the consequences in the future.

TABLE 3

ILLUSTRATION OF CURRENT INSURANCE COMPANY DISABILITY INCOME MAXIMUMS BASED ON AVERAGE (WITH RESPECT TO FAMILY) INSURANCE PROSPECT

(Permissible Disability Income, Social Security, and Federal Income Tax as Percentage of Gross Earnings)*

Gross Monthly Earnings	Company A	Company B	Company C
$ 300	135%	86%	135%
450	124	95	130
550	120	98	128
750	107	93	117
1,000	97	90	92
1,700	88	88	85
2,000	87	88	84
3,000	87	91	85

* Social security benefits are included at full 1966 level; federal income tax is computed on the basis of standard deduction.

TABLE 4

Gross Monthly Income	Maximum Ideal Disability Income as a Percentage of Gross Income*
Less than $400	17%
$400 but less than $500	22
$500 but less than $600	24
$600 but less than $700	29
$700 but less than $800	35
$800 but less than $1,100	43
$1,200 and above	50

* Subject to an over-all maximum of $1,000 per month.

In the light of what I consider to be unrealistically high disability income–salary relationships, I worked up my own limits. These limits are given in Table 4, which shows a comparison of the present limitations of the insurance industry and the ideal limitations. The ideal maximums are aimed at the longer-benefit-period accident and sickness plans. For benefit periods of one or two years, the "ideals" could be liberalized.

By Table 5 you will see that the "ideals" appear to solve the problem of overinsurance at the lower annual earnings; and, in my opinion, they do not destroy the sales appeal of the product.

I hope that this background will aid us in arriving at the proper solution to the questions posed.

TABLE 5

ILLUSTRATION OF CURRENT INSURANCE COMPANY DISABILITY INCOME MAXIMUMS BASED ON AVERAGE (WITH RESPECT TO FAMILY) INSURANCE PROSPECT

(Permissible Disability Income, Social Security, and Federal Income Tax as Percentage of Gross Earnings)*

Gross Monthly Earnings	Company A	Company B	Company C	Ideal
$ 300	135%	86%	135%	85%
450	124	95	130	85
550	120	98	128	85
750	107	93	117	85
1,000	97	90	92	85
1,700	88	88	85	85
2,000	87	88	84	85

* Social security benefits are included at full 1966 level; federal income tax is computed on the basis of standard deduction.

MR. NORMAN E. HILL: At the Bankers Life and Casualty Company in Chicago, disability income coverage is not a major percentage of our total business, but we do have a large enough volume in force so that we are interested in the effect of the new social security law that liberalizes the definition of disability and increases the potential amount of social security disability income to each person. Since it will be easier to qualify for federal disability income and since there will be a greater frequency of overinsurance, we in the insurance industry must decide whether we can write a substantial volume of disability income on a profitable basis in the face of this competition. I feel that it is not necessary to withdraw from the disability income market or to increase premium scales to the point of unattractiveness. Instead, I feel that reasonably conservative issue and participation limits are the answer.

With the change in legislation, we are considering making our issue limits a function of the number of dependents. It would work in the following way:

1. For short-term disability, continue the current rule of 50 per cent of earned income plus $50 and retain the current issue and participation limits.

Here, a short-term disability policy is defined as having the maximum benefit period for *both* sickness and accident total disability equal to two years or less.

2. For long-term disability, 50 per cent of earned income less $50 for each dependent *including* the insured, up to four dependents including the insured. Here, a long-term disability policy is defined as having the maximum benefit period for either accident or sickness total disability equal to more than two years.

In addition, the issue and participation limits for long-term disability would be increased, as shown in the accompanying tabulation, which uses the Conference Occupational Classes.

OLD LIMITS

1. Guaranteed renewable accident and sickness and accident only policies—participation limit $600.

ISSUE LIMITS

Occupational Class	Male	Female
AAA-AA	$600 per month	$300 per month
A	500 per month	250 per month
B	400 per month	....
C	300 per month	....

2. Optionally renewable accident and sickness and accident only policies—issue and participation limits: $400 per month, for males and females, Classes AAA to C.

NEW LIMITS

1. Guaranteed renewable accident and sickness and accident only policies—participation limit $1,000.

ISSUE LIMITS

Occupational Class	Male	Female
AAA-AA	$1,000 per month	$500 per month
A	900 per month	450 per month
B	750 per month	....
C	600 per month	....

2. Optionally renewable accident and sickness and accident only policies—issue and participation limits: $750 per month, for males and females, Classes AAA to C.

There are a number of reasons for maintaining the current limits on short-term disability. The first is that our experience to date has been quite good. The second is that our average policy size is around $150 monthly indemnity and gives no indication of increasing. Furthermore, most of this type of coverage is subject to the lower maximums for optionally renewable policies. Third, OASDI still requires a six-month

elimination period. Fourth, the optionally renewable aspect provides considerable protection. Among other underwriting rules that we are continuing are a minimum of $100 monthly indemnity to discourage small claims and a maximum benefit period that does not extend beyond age 65. We do not intend to issue true noncancellable coverage for accident and sickness with guaranteed premiums.

Topic A was concerned with the effect of OASDI on the scope of the market for private disability. It is true that an insured with a wife and two children probably has available at least around $250 of federal disability monthly benefits. Under my company's proposed rule, this man with $1,000 monthly earned income could be sold long-term disability coverage of only $300 per month. However, our average issue has been around $150 per month. We feel that an intensified disability sales campaign can significantly increase our average size over this amount but still avoid overinsurance.

Topic C deals with the effect on policy provisions. Here we do not anticipate a necessity for any changes. Our relation-of-earnings-to-insurance clause will remain the same. Also, our definition of disability in currently issued long-term coverage will remain the same. Total disability is defined in relation to "his occupation" during the first year of disability and afterward is defined in relation to any occupation for which the insured is reasonably equipped by education, training, or experience. Although there may be some movement in the industry toward two-year "his occupation" definitions, we do not intend to liberalize this.

It must be emphasized that our approach may not be satisfactory for every company. This will depend on the particular company's volume of disability, average size policy, and objectives.

MR. BENJAMIN R. WHITELEY: At Standard Insurance Company, we have concluded that, in underwriting individual disability income policies, our "issue limits" must be reduced to offset, at least partially, social security benefits.

A practical limit, equitable for all applicants, is difficult to develop because of the variation in social security benefits by number of dependents. Our approach has been to reduce regular limits by an amount which approximates *primary* social security benefits.

Our new rule reads:

> The Company will not issue monthly indemnity which, combined with other coverages from all sources, exceeds 50 per cent of net earned income plus $50.
>
> For the purpose of determining benefits from all sources, Social Security benefits will be accounted for according to the following table:

Monthly Earnings	Monthly Social Security Benefit
$300 and under..........	$100
$301–$450...............	125
Over $450...............	150

The effect of this is to reduce the allowable amounts of disability income and tend to overinsure the lower-earnings classes, but not by serious proportions. To offset the possibility of inadequate benefits during the social security waiting period, we are developing an additional monthly indemnity rider, which provides a level benefit of $150 per month for a maximum benefit period of six months for use with individual disability income policies.

MR. ANTHONY J. HOUGHTON: Although the recent liberalizations in the social security disability program should have little effect on policies providing benefits for two years or less, the effect will be substantial where benefits are provided for longer periods. A covered individual with a maximum earnings base can receive a social security disability benefit of about $136 for an individual and about $310 for dependent coverage. Only about one-third of the approved social security disability claims include dependent coverage, because most of the disabilities occur after age 50 when the spouse is under age 65 and the children are over age 18. Although the social security benefit is important in underwriting individual applications, it is not as important as the presence of other individual insurance or the growing impact of group long-term disability plans.

The excess claims that might be caused by overinsurance due to liberalization in OASDI are minor in comparison to the excess claims that might be incurred if our economy suffered high unemployment approaching the depression years of the 1930's.

I think that it is important to have a relation-of-earnings-to-insurance clause in the policy, which defines "valid loss-of-time coverage" as "provided by any governmental agency or by any organization subject to regulations by insurance laws or by insurance authorities of any state or any province of Canada."

MR. ROBERT H. JORDAN: Although I agree that it is not desirable to offer an applicant a contract that will make his disability income greater than his earned income, I think that the purchase of disability income up to a limit of 50 or 60 per cent of earned income is a relatively rare occurrence. It is more frequently the problem that the total disability income requested exceeds the dollar limit that a company wishes to issue. We should keep in mind that financial results are based on the relationship of benefits to earned income at the time of the claim, not at issue.

Changes in Individual Medical Expense Insurance in Light of Medicare

A. What revisions are being made in new-business portfolios with respect to:
   1. Basic hospital and medical expense coverage?
   2. Comprehensive hospital and medical expense coverage?
   3. Senior citizen coverage?
B. What adjustments are being made in existing policies with respect to:
   1. Persons who are over age 65 in 1966?
   2. Persons who will become age 65 in future years?
C. What claim problems are anticipated under continuing policies on persons eligible for Medicare?

MR. E. PAUL BARNHART repeated the discussion which he had presented at the Washington Regional Meeting, reported in *TSA*, XVIII, D64.

CHAIRMAN MAYNARD I. KAGEN: Participation limits that may be satisfactory in the cases of policies issued under 65 may not be satisfactory when the person reaches Medicare age. Are you proposing that benefits might change?

MR. BARNHART: Yes, that is what I have in mind. At age 65, possibly the room limit and other benefits in the policy might be reduced 50 per cent or to some reasonable level that would be consistent with the participation limit above age 65.

CHAIRMAN KAGEN: Would you prescribe a level premium for the life of the policy?

MR. BARNHART: I believe that a reduced premium would be more logical.

MR. WILLIS W. BURGESS, JR.: At Bankers Life and Casualty, we concluded in mid-1964 that some form of Medicare would be enacted in 1965. With over 1,100,000 policyholders then 65 or over with hospital, medical, and surgical policies, it became imperative that we make preparations. We did so on the assumption that the final enactment would be rather similar to bills previously proposed.

Of the various benefit possibilities, we concluded there were three general benefit plans that we could offer present and new policyholders 65 and over after Medicare went into effect. These were a hospital benefit filling the gaps in Part A of Medicare; this benefit supplemented by a $200 surgical schedule and benefits of fixed amounts for each doctor visit

at home, office, or hospital; and a hospital indemnity benefit. We then decided to offer each as new business.

Full details of the ages and constitution of families covered were contained only in the individual policy files. With over 2,000,000 hospital, medical, and surgical policies in force at the end of 1965, it was impractical to pull files to obtain this information. Since our experience on medical-surgical policies and hospital indemnity policies had been good, and since these appeared to be satisfactory Medicare supplements, we decided to concentrate our exchange efforts on hospital-surgical policies. This reduced the number of policies not quite 50 per cent—still a considerable number but a number that we felt we could manage. We decided to offer to exchange the hospital-surgical policies of those over 65 for policies filling the gaps in Part A of Medicare.

We had been encouraged by the results of a questionnaire sent in November, 1965, to 7,000 holders of hospital-surgical policies over age 65 who had been insured at least two years. Of the 1,500 replies, some three-fourths said they wanted to keep their present coverage or to change to a coverage supplementing Medicare. A decision to go ahead with this exchange program was made at the end of that month. In February of this year, we sent exchange material to a sample of 148,000 holders of hospital-surgical policies aged 65 or over. Within a month we had acceptances from 34 per cent of these, a result we considered very satisfactory; so we went ahead with the remainder of the affected policyholders. By the end of May we had made exchange offers on about half a million policies, with just under two-thirds accepting.

Over 85 per cent of the policies concerned were renewable at the option of the company, but the percentage exchanging was the same for both these and guaranteed renewable policies.

Different letters were used for each type of renewability. However, the new benefits, provided in the form of a rider, were guaranteed renewable regardless of the renewal provision of the policy. No underwriting was done. Now that our exchange efforts by mail have been completed, we have begun to make exchange offers through agents.

MR. JOSEPH C. SIBIGTROTH: At New York Life, in revising our medical expense portfolio in the light of Medicare, we had two general objectives: (1) for ages through 60 at issue, we wanted to minimize changes in benefits and policy provisions, and (2) for older ages, we wanted to supplement Medicare benefits on a worthwhile basis without creating complicated claim-administration problems.

Believing that the effects of Medicare on the medical expense picture

would not become clear for some time and that exchanges of policies renewable for life to those terminating at 65 would be more complicated the more changes that we made, apart from a few very minor changes in benefits for ages 18 through 60, we merely changed the guaranteed renewability and coverage periods from life to termination at age 65 and added, for insureds reaching age 65, a privilege of conversion without evidence of insurability to any senior hospital policy then being issued by the company. For those over age 60, we developed a hospital policy supplementing Medicare benefits and an optional posthospital extended-care benefit rider.

The provisions in these new forms follow many of the basic concepts of Medicare. For instance, benefits are geared to the "spell of illness" definition. Similarly, the definitions of hospital, hospital confinement, and extended-care facility follow Medicare's basic concepts.

Our hospital policy provides daily benefits of $10 per day for the first 60 days, $20 for the next 30 days, and $30 for the next 90 days; a $1,000 miscellaneous hospital expense benefit for expenses incurred from the ninety-first through the one hundred-eightieth days; and up to $45 per day for no more than 20 days for private-duty nursing in a hospital.

The posthospital extended-care rider provides, after at least three days in a hospital, daily benefits of $5 per day for the first 20 days, $10 for the next 80 days, and $15 for the next 85 days; a miscellaneous extended-care-facility expense benefit of up to $500 for expenses incurred from the one hundred-first through the one hundred eighty-fifth days; and private-duty nursing benefits up to $30 per day for a maximum of 20 days while in an extended-care facility and up to $15 for a maximum of 20 days while not so confined.

Policyholders 64 or older on their 1966 policy anniversaries are being offered the option for a limited period to exchange their lifetime hospital or major medical policies to the new senior policy, with or without the extended-care rider. The exchange is at the attained age without evidence of insurability. The pre-existing conditions exclusions are modified so as not to penalize the insured. The exchange offer is in the form of a letter indicating that the exchange may be made or the existing policy continued. An agent will call if this is desired by the insured. Commissions on the exchanged policies are at reduced rates.

Policyholders under age 64 on their 1966 anniversaries may continue their present coverage or exchange for a similar policy guaranteed renewable to 65 without evidence of insurability and on an original-age basis. The exchanged policy permits conversion at 65 without evidence of insurability to such form of hospital policy as the company may then be

issuing. The exchange offers will be made prior to 1967 anniversaries and must be accepted within a specified period. In the letters no effort to encourage or discourage exchanges will be made.

MR. ANTHONY J. HOUGHTON: Major medical policies guaranteed renewable for life treat benefits provided for by federal legislation in different ways. One type of policy does not exclude these benefits even though the policy may exclude expenses incurred in veterans' hospitals or expenses payable by workmen's compensation. This type of policy may provide considerable overinsurance for people over age 65 and, consequently, antiselection.

Another type of major medical may exclude benefits paid through federal legislation as covered medical expenses. This type of policy protects the insurance company satisfactorily but is of little value to the insured over age 65. It would appear better to allow these expenses to the extent that they satisfy the deductible which would avoid overinsurance but still give substantial protection to the policyholder.

A third type of major medical uses as the deductible the greater of (1) a basic deductible or (2) "other insurance." This third type of policy may or may not exclude benefits provided through federal legislation. For this type of policy it would seem preferable to include the benefits provided through federal legislation as part of "other insurance," which would give the policy value and meaning after age 65 and still protect the insurance company against excessive overinsurance.

Optional Modes of Settlement

Have any new settlement option arrangements been made available? What are the recent trends in settlement option election rates? In what way are election rates affected by economic conditions? To what extent are new-money approaches being used to allocate interest to supplementary contracts?

MR. NEIL A. PARMENTER: Our experience at Bankers Life has shown that our "interest only" settlement option has the highest election rate of any involving or noninvolving option. Our fixed-payment noninvolving option is more popular than our fixed-period noninvolving option, indicating that our policyholders and their beneficiaries are perhaps more interested in the amount of payment rather than the length of time that they will receive a payment. Among our involving options, the "ten-year certain and life thereafter" option has the highest election rate. This popularity may be due in part to the fact that most of our illustrations are based on this option and that, therefore, the agent stresses this option in his interviews.

Since 1962 we have included in our regular application form a provision for the applicant to elect our "interest only" settlement option by simply checking the appropriate box. This election is subject to both the right of withdrawal and the right of election of other settlement options by the beneficiary. We found that, based upon a sample of our new issues, this provision was being elected on 46 per cent of all new applications.

Including this provision in the application is a convenience for the agent, particularly with small policies for which complicated settlements may not be justified. This permits a bereaved beneficiary to wait until an appropriate time for making a more satisfactory decision about the use of the death benefit while the proceeds remain with the company and continue to earn interest.

Whether the inclusion of this provision in the application will have any effect on the trend in the noninvolving election rates at all cannot yet be determined, since experience may well show that the "interest only" settlement option elected at issue will be frequently changed after issue or, more probably, surrendered shortly after the option becomes effective because of the relatively greater attractiveness of other forms of investment.

MRS. JULIA S. OLDENKAMP: The Lincoln National Life Insurance Company, by current company practice, offers an annuity settlement privilege in lieu of guaranteed settlement options. This annuity settle-

ment privilege may be elected (*a*) only when the policy proceeds become payable, (*b*) only if such proceeds are available in one sum in cash, and (*c*) only by the person to whom such proceeds are so payable or available. It was felt that these restrictions would protect the interest of contingent beneficiaries and insure our carrying out the wishes of the owner of the policy after his death.

The income available under the annuity settlement privilege is 3 per cent greater than that available on a new single-payment immediate annuity. No commissions are paid, and no excess interest is paid. Therefore, once the privilege has been elected, the income is level and guaranteed throughout life. Any form of income for which a single-payment immediate annuity can be issued is also offered on the annuity settlement privilege. This includes nonrefund annuities payable for life, jointly and to the survivor, or jointly and two-thirds to the survivor, as well as life annuities on one life with a certain period of 5, 10, 15, or 20 years and the instalment-refund period certain.

The administration of the annuity settlement privilege is fairly expensive, because a letter showing a detailed comparison between the guaranteed settlement option (with excess interest, if any) and the corresponding annuity settlement privilege is sent out in every case in which the annuity settlement privilege is offered. A comparison must also be made to determine whether to offer the annuity settlement privilege. It is not offered unless the income is larger than that which is guaranteed by the policy. So far, fewer than one-half of those who are offered the annuity settlement privilege have accepted it. Most of those who do not accept it take a lump-sum settlement. However, since our excess-interest rate on guaranteed options was increased to the difference between 4 per cent and the guaranteed rate, some have chosen the guaranteed options if the income is higher for even the first few years.

The annuity settlement privilege is a good tool for the agent to use in making sales presentations, although he is warned to tell a prospect that the present annuity settlement privilege incomes are not guaranteed for settlements occurring in the future and that the privilege itself may not be available at some time in the future. It is much more convenient for quotation purposes than excess interest on guaranteed instalments.

At the Lincoln, the trend in the rate of election of settlement options has been down for the last four years. The figures in the tabulation on page D282 are based on insurance only and include death claims and maturities of both endowments and the retirement-income (with insurance) type of contract. The trend is about the same, whether or not life contingencies are involved.

On annuities only, the rates of election of income settlements were 56.6 per cent in 1963, 53.1 per cent in 1962, and 52.7 per cent in 1965.

Regardless of what we may think should be the effect of economic conditions on the use of settlement options, it appears that the availability of attractive interest rates from other financial institutions is a real factor influencing policyholders.

Mr. Moorhead raised some philosophical points at the Washington meeting. He felt that settlement options should be "sold" to those eligible to elect them. There is a limit to what a company can do through direct correspondence with the policyholder or beneficiary in explaining the advantages of an income settlement option. We attempt to call such options to the attention of these prospective payees in a general way, but we leave it to them to ask specific questions. It is also suggested that they

RATIO OF TOTAL SUPPLEMENTARY CONTRACT CONSIDERATIONS TO THE TOTAL PROCEEDS FROM DEATH CLAIMS AND MATURED ENDOWMENTS ON DIRECT ORDINARY INSURANCE

Year	Supplementary Contracts Involving Life Contingency	Supplementary Contracts Not Involving Life Contingency	All Supplementary Contracts
1961........	7.6%	11.5%	19.1%
1962........	9.5	12.0	21.5
1963........	8.6	10.3	18.9
1964........	7.0	10.4	17.4
1965........	7.1	9.5	16.6

may wish to confer with one of our agents. It seems that the agent is a key factor, and, if we really want to increase the use of settlement options, we will probably have to motivate the agent. We have noted that, even though the incomes available are on a very favorable basis, there is an inclination for the recipient to prefer a lump sum when the income is a small amount, such as $10 or $20 a month. Apparently these small income payments do not now seem worthwhile, although they may have seemed so twenty or thirty years ago when the policies were purchased.

Mr. Moorhead felt that settlement options should be more attractive to policyholders—not only more attractive than the company's own annuity rates but more attractive than the *lowest* cost annuity available elsewhere. If a company has a conservative attitude toward annuitants' mortality and possibly is not earning as high a rate of interest as some of its competitors, it is difficult to see how such a company could justify such attractive options. The result of such an attempt on the part of companies

in general would be for the entire industry to use the least-conservative estimate of future mortality and interest earnings for current income settlements.

Philosophically, proceeds which remain on deposit are not new money. In determining excess-interest rates, we do not use a new-money concept. However, the ease with which a policyholder can convert such proceeds to new money requires an arrangement such as the annuity settlement privilege, which is based on a new-money concept to the same extent that the immediate annuity rates are based on such a concept. Whenever a new-money approach is used for a segment of business, there is always the danger that the effect of such an approach will not be taken into account in determining the average interest rate suitable for many other purposes. If it is not taken into account, the result is an overstatement of the average interest rate.

MR. J. STANLEY HILL: Most life insurance policies contain an option to have the proceeds paid at a specified monthly rate as long as the principal and interest last. Under these options the interest element is nontaxable up to $1,000 per year, and, therefore, these options are attractive when compared to other possible uses of policy proceeds. Life insurance companies should stress this advantage when furnishing information about settlement options. Doing so may ease the flight of assets in the form of cash settlements.

MR. BARTLEY L. MUNSON: Aid Association for Lutherans adopted a plan to confer a higher interest rate on our fixed-amount settlement options at the beginning of this year. If the proceeds are to be paid out within ten years, we guarantee 4 per cent. Three per cent is guaranteed if they are to be paid out within the following ten years. This enables us to give our policyholder something attractive in comparison to what other savings media can offer in competition.

We have an annuity purchase option that provides income equal to 104 per cent of what our immediate annuities will provide. We do not give our insured a choice of whether he can have the guaranteed annuity or the annuity purchase option in his contract. We give him the larger of the two.

Our single-premium immediate annuities are participating. The dividend is paid monthly along with the guaranteed payment, so that the insured annuitant receives a level periodic income. Our single-premium annuities have a fee of $100. The same fee applies on annuity purchase settlement options.

MR. E. FORREST ESTES: I am intrigued by the discussion about interest rates guaranteed on advance premiums in contrast to interest rates for life annuity settlements.

We are justified in offering liberal interest guarantees for premiums paid in advance for two reasons. One is that accounting problems are reduced considerably, and the other is that persistency is improved. With life-income settlements, on the other hand, we must consider future mortality which, with all the work that is being done in the medical field, is constantly improving.

I favor providing generous settlement options through a provision for dividends, with the idea that dividends may be adjusted as the need arises to meet future conditions.

MR. G. DAVID SODERQUIST: The Columbus Mutual Life Insurance Company offers both annuity purchase option and current purchase rates. I would like to explain just why we do this.

When we were developing the 1958 CSO line, we included the annuity purchase option in our new series of contracts. We then decided that this would be a rather unwieldy tool because of the need for monthly gradations for each elapsed month of age since the policy anniversary, so we adopted a current purchase rate, which is slightly more favorable to the insured than the annuity purchase option would be. This simplifies a rather complex calculation at the time of settlement, so that one can simply refer to the table and pick up the correct factor.

During 1966 we are making a further change. We are converting all our existing supplementary contracts to the current purchase rate basis, if the current purchase rate would produce a larger income. We apply the new purchase rates to the existing supplementary contract balances to produce a higher income than the individual had been receiving.

MR. BRUCE E. NICKERSON: Most life insurance companies are willing to make rather attractive guarantees on premiums paid in advance—4 per cent or more for periods of ten years or longer.

Would it not be reasonable to make a similar guarantee on money left under supplementary contracts not involving life contingencies? Further, would not such a guarantee constitute a valuable competitive asset to oppose the higher current rates of interest, not guaranteed, which are being paid by certain savings institutions with whom we are competing?

MR. JEROME J. L. WOLF: In addition to the generation settlement options in the contract, which in practice participate throughout the full

payment period on either a level- or reducing-dividend formula, London Life Insurance Company offers a nonparticipating alternative income option, that is, the then-current single-premium annuity rates discounted. Close to 90 per cent of the settlement options involving life contingencies are on this current annuity basis.

The accompanying tabulation exhibits recent trends in our settlement option election rates.

Year	Net Death Claims and Matured Endowments	Amounts on Deposit	Per Cent	Consideration for Settlement Options Involving Life Contingencies	Per Cent	Consideration for Settlement Options Not Involving Life Contingencies	Per Cent
1955......	$ 9,872,990	$1,976,521	20.0	$621,177	6.3	$536,841	5.4
1960......	14,954,810	1,762,921	11.8	335,323	2.2	730,521	4.9
1965......	23,827,698	3,928,654	16.5	282,927	1.2	584,103	2.4

These figures include the total death claims and matured endowments from both our regular ordinary business and debit ordinary business. There would certainly be a far smaller use of settlement options on our debit ordinary business as compared to regular ordinary, and this may be one reason why our elections of settlement options are rather low.

Even though consideration for settlement options has shown a steady decline over the last ten years, proceeds left on deposit—almost $4 million in 1965—represent about 17 per cent of the death claims and matured endowments. This may be due to the greater flexibility of this arrangement and to the fact that our agents are not paid a commission or service fee on settlement options.