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## EMPLOYER SPONSORED INDIVIDUAL LIFE INSURANCE

Moderator: CHRISTIAN J. DESROCHERS. Panelists: GABRIEL G. CILLIE, J. TYLER LEE,  
WILLIAM J. TAYLOR

An increasing number of life companies have renewed efforts to distribute life insurance products via payroll:

1. What motivates employers to install such a program? How do they perceive the value and impact of program installation?
2. What special distribution system requirements exist?
3. What are critical administrative considerations?
4. Which products serve the market most effectively and why?

MR. CHRISTIAN DESROCHERS: Each of the panelists will discuss his particular company's approach to this market, why the company is in the market, what type of market it sells to, the characteristics of their distribution systems and administrative requirements.

As you will hear from the panelists each of the companies represented has a very different orientation and has different experiences in this rapidly changing and highly specialized market. Let me take a moment to introduce the panelists.

J. Tyler Lee is Second Vice President & Actuary at Life of Virginia. Life of Virginia is one of the leading companies in universal life products and has developed a universal life plan specifically for use in the employer market.

William J. Taylor is an Actuary at Puritan Life. Puritan specializes in payroll deduction plans using individual policies. Their market is targeted at large size employers.

Gabriel G. Cillie is Vice President & Assistant Actuary at the Prudential. The Prudential is active in the small case employer market, generally selling 2 or 3 life cases.

MR. WILLIAM TAYLOR: My company is Puritan Life and it is heavily involved in payroll deduction life insurance. Chris asked me to share some of the elements and philosophies of our approach to the marketplace, and I am very glad to do that.

As background, Puritan Life is a medium sized stock company wholly owned by the General Electric Credit Corporation and is located in Providence, RI. We have been selling payroll deduction life insurance as a principal market thrust since early 1981. Our average case involves about 230 eligible employees and premium per policy of \$225.00. My personal background is in the area of product development. I am going to limit my comments to that

area. The distribution of our product is unique in that we use salaried sales representatives, who generally have had some background or experience in selling group life insurance. Many of the skills involved in selling payroll deduction life insurance are similar to those needed to sell group life insurance. Our sales representatives spend a majority of their time talking to employee benefit managers--convincing them of the reasons payroll deduction life insurance is a good idea for their employees.

The basic sales approach can be divided into several segments. First is a conceptual sale of payroll deduction life insurance to the employee benefits manager. A large number of working people in this country have little life insurance other than the basic group life insurance provided by their employer. It is no longer economically efficient for an insurance agent to sell small insurance policies across the table to the average blue collar worker. Employer sponsored payroll deduction life insurance is an efficient method of allowing an employer to provide his employees with the opportunity to buy small amounts of life insurance on a guaranteed issue basis at competitive premium rates.

Once the conceptual sale is finished, the second aspect of the sale process involves a competitive demonstration that the particular product offered by our company is competitive in comparison to what the employees could get on the street. The employers are already providing as much insurance as they can afford through group life insurance. It is critical that the product being sold is a good value for the price, because in general it is marketed on an employee "pay all" basis. The employer wants to be sure that he is not sponsoring anything that his employees will not be receptive to and that won't provide at least a good feeling and good morale among his employees.

The last aspect of the sales process is the enrollment. Once the enrollment date has been set, an enrollment coordinator will meet for a review session with all the managers and supervisors of the company. We found that unless the manager and supervisors are committed to the program and understand why their people are going to be taking time off to go and talk to enrollers we don't get very positive results. As a result, the enrollment coordinator goes in a little bit ahead of time, prior to the enrollment date and does a pre-review with the supervisors and managers. That also guarantees that we won't have surprises on the enrollment date. On the enrollment date, the enrollment coordinator returns to the company with a team of enrollers to solicit each eligible employee.

We use part-time salaried enrollers, who conduct one-on-one sessions with the employee, lasting for about 10 to 15 minutes. Enrollers have been trained not to over sell. Our basic enrollment philosophy is to use a money purchase technique (as opposed to a defined benefit technique where insurance is based on salary). We use the employee salary as an indication of his or her ability to pay and have developed guidelines for enrollers which give an indication of how much an employee can afford. For example, if an employee can only afford to pay four dollars a week for life insurance, the employee is counseled not to buy more than that. Again, it is consistent with the "soft sell" idea.

Two employees of different ages who make the same dollar amount with our program would have very different insurance coverages, because the way we promote our product is to have the total premiums of those employees be the

same. The older employee gets less insurance. We find that this helps our lapse rates, which are better than most companies achieve under this type of program. We also find that it helps in limiting anti-selection.

On the administrative side, there are a few items of note. First of all, we issue our policies within 3 to 5 working days of the date the application is made, and then those policies are sent immediately to the employee. We feel that the employee should have the policy in his hand before the payroll deductions start. The idea is for the employee to have something in his hand before the first payroll deduction is made--otherwise you have a real problem. The issue dates are by 1½ to 2 months in the future. That is to provide the employer with an opportunity to set up his payroll deduction and to start deducting the premiums before the first premium notice is sent.

By beginning the deductions on a timely basis, the employer earns the interest "float" on the deduction until the first bill is due, usually about a month later. The employer should be making consistent deductions about a month ahead of the bill. For large cases, the interest float on the deduction can be substantial and can be used to cover some of the incidental costs associated with setting up the payroll deduction program.

For a large case, our sales representative (or someone from the home office on other cases) usually delivers the first few bills to the employer's accounting department or the payroll deduction department personally. He will help that department reconcile the initial bills. Reconciliation of the first few bills can be difficult, so we provide assistance until the payroll department can do it themselves. Once we have done that, we find that the program runs smoothly.

In the area of underwriting, our program is on a guaranteed issue basis for cases involving 100 to 250 eligible employees. We started out with guaranteed issue down to as low as 50 employees but we have been slowly but surely moving that number up, as our market has moved to larger and larger cases. For cases below that size we use a short form medical application which really involves four or five other questions. I refer to that process as simplified issue as compared to guaranteed issue, which involves an "actively at work" requirement.

The advantage of not eliminating those small cases altogether, is that occasionally one of our sales representatives will become involved with a broker who is the insurance agent of record on a number of cases. We try to bid on any case although the rules and the requirements change a little bit in the lower size cases. The simplified issue aspect has been sufficient enough to discourage the writing of too many small cases--which is really what we are trying to do.

With regard to eligibility requirements, we usually require a minimum of about 6 months service for employers with low employee turnover. For employers with higher turnover we can require as much as a two year service requirement, but that is a little unusual.

We offer two types of products: a whole life plan - which works fairly well in the small case market and a higher premium term and annuity combination which we make available to the higher paid employees in any case who don't want a whole life policy. We are currently developing our first universal

product, which we have discovered is necessary for the larger case market, where the employer is much more of a sophisticated buyer.

I would like to make a few additional comments on our experience to date. We have only been selling in this market since 1981 so it can be easily argued that our experience is really not yet significant. However, we found that our participation rate is much better than we had anticipated and we attribute that to our enrollment technique. Our mortality experience has been relatively favorable compared to what we have priced in the product. While our lapses have been a little higher than we had anticipated, we believe we have better persistency than other companies have been incurring. We perceive that we have a lapse problem on dependent and spouse policies. When the employee leaves the company and terminates his policy, and he also terminates his dependent's policies--which means that the lapse rates on that dependent policy related more to the age of the employee than to the age of the insured spouse or child. As we look at our lapses, we adjust in the fact that one decision maker controls several policies.

MR. TYLER LEE: As Chris said, we did a few things differently than Puritan. At Life of Virginia we first entered into the payroll deduction market, at that same time as Puritan did, in 1981, using a universal life product. I guess that was no surprise to anyone. The reasons for wanting to expand into this market are really not too different from what Bill has already told you.

One of our main reasons was that we had, since the late 70's, been making our products for the "up" market leaving behind the middle income. The regular universal life policy that we had at that time was a \$100,000 minimum size policy. The payroll deduction strategy at least for us, is a move to back into the middle income market in an efficient way.

Another reason was to encourage our agents to sell universal life. Initially, the commissions on universal life policies were somewhat below those on traditional policies. For over a year we had been telling our agents we realize that while the commissions per sale are lower, the volume written should increase. I think we found it to be true that the payroll deduction market was a way, a clear opportunity, to actually get more volume. We introduced a universal life policy designed specifically for the payroll deduction individual market. It had a much lower face amount than the universal life policy that we had for a non-payroll deduction market. When we first got into the payroll deduction market for the universal life, there were perhaps one or two other companies that were in the market at that time with a universal life policy.

In non-payroll deduction universal life we have seen trends towards higher commissions. We have also seen trends, at least in my company, of lower profit objectives, and I have to attribute that to increasing competition. And of course, just lately, there has been a trend toward back-end loads. We found out that in the payroll deduction market with a universal life policy it is still necessary to keep up with these trends. Consequently we did a second generation product in early 1983 and we are currently working on a third generation product which is scheduled to come out later this year.

One of the most difficult problems at Life of Virginia for payroll deduction plans was determining which operating unit controls the plan. At Life of Virginia we are divided into two operating lines of business--individual lines and corporate lines--which controls and operates group policies. Our payroll deduction universal life product is called "VSP". When we want to design a new version of VSP, it is a coordinated effort by individual and corporate lines. It is priced by individual, it is sold and marketed by individual, and is administered by corporate lines.

Our normal case size is somewhere between 30 and 500 lives. While that is a broad range, that is the market that we normally address. Before we take any case, it must pass a pre-screening test. This is done in our group underwriting department. Traditional group questions are asked on this pre-screening form. You ask: (1) what type of work or what industry is the employer engaged in; (2) what the turnover rate is; (3) what classes are the employees designated for coverage (sometimes some classes can be eliminated because the underwriters feel that it is too big a risk for a certain group, but we can still take the rest of the case); and (4) what schedule of benefits is desired.

Some administrative questions are also asked; (1) how spread out or concentrated are the employees? (Are the employees in one location, or is a 100 life case with 5 employees each in 20 locations from Maine to California); (2) what are the payroll cycles; (3) are spouse and child coverage to be available?

In the payroll deduction market, we see little, if any, employer participation. It is usually employee pay all and therefore has much smaller participation percentage, or penetration percentage, than is typical for group cases. For this reason there is more anti-selection -- so a pure group underwriting process is not applicable. We think that you can control the anti-selection, and we ask several important questions on the pre-screening form. First of all, we ask who is going to enroll the plan. This is an important question. Sometimes it is a specialist. There are payroll deduction specialists in the market place who have proven track records of getting 50, 60 or 70 percent of eligible employees. Often, they are the ones to go with as they are experts in this field, they are experienced and know how to enroll. As Bill said, enrollment procedures are a very important item.

Often though, we will find that our own agent is going to enroll the case. Occasionally, the employer himself wants his company to enroll the case. I wouldn't recommend this. When an employer enrolls the case, he is going to be using his personnel or benefits people who are untrained enrollers. You will find less penetration and consequently more anti-selection. We had one case in which we allowed the employer to enroll his own case. One of the enrollers went to an employee's home one Sunday and enrolled the person at his home (this was guaranteed issue). The person went into the hospital on Monday and died of cancer a week later. I wouldn't recommend going with that approach, but even if you did, the pre-screening form can help.

Another question which is very important is whether the employer will allow a one-on-one interview with the employee or whether they will only allow a group meeting. We see this as a very important part of the procedure because you will be getting a high percentage of participation. It has both

a direct and indirect effect on the success of the plan. Currently one-on-one interviews produce a higher participation percentage. Group meetings just can't substitute for personal interviews. In group meetings there is always the lack of control. Even though we do have waiver cards for the people who do not want the coverage, it is very difficult in the group meeting to determine who has been talked to and who has signed waiver cards.

Indirectly, I think that one on one meeting is important because it tells you something about the employer. I think that what it tells you is whether or not the employer himself is not really supporting the introduction of this plan to begin with. It often happens in companies that attitudes and ideas often float from the top down. I think that employees can sense a half-hearted endorsement of a particular plan. In cases when we have allowed group meetings, the participation has been simply pitiful. I wouldn't recommend it to anyone.

Before I pass the mike on to Gabe, I would like to take a minute to discuss where we seem to be heading at Life of Virginia at least in the payroll deduction market. Certainly, I believe product changes will occur as long as products continue to change in the non-payroll deduction individual life market. The products in the payroll deduction market have followed changes in products in non-payroll deduction markets. I am confident that next year at this time we will be working on the fourth generation of payroll deduction product.

There are some trends which are just emerging which make me believe that there are some other types of changes in the area of what I call "flexibility". The distinction between group and individual lines is likely to become even more blurred. More and more we are asked to tailor-make a payroll deduction individual universal life product--much like group or pension plans have been done over the years. This is very unusual. I have been in individual product pricing for my whole working career, and I never recall a time when we have been asked to individualize individual policies anymore than right now. We recently did this for a company of about 10,000 employees who wanted universal life as part of their 401(k) program. This required a great deal of effort in both product and administration. We had, in this particular case, decided with the employer that we were going to do this particular case and gave him specifications for the product. We had two months until they were doing their first enrollment and that means, within two months, that we had get the product on the system, file the forms, and do whatever had to be done to get administrative system to work. This required a lot of effort and time.

When employers ask for custom products they generally ask for changes in several different areas. First, they often want lower commissions than you have in your normal payroll deduction policy. They often want liberalizations of underwriting standards--guaranteed issue. What Bill said for his company, is also true in our company--for normal underwriting requirements we require at least 100 lives before we would issue a guaranteed issue on a payroll deduction plan. When we do special quotes, there are often 10,000 or more lives. Not only do they want guaranteed issue, but they also want guaranteed issue for a higher amount than you would normally give them and for a higher issue age than you normally would do.

They almost always have special demographics of their particular group. I have to admit that these are very often different from the averages we use in the normal case policy form. You may find that you have a higher average size policy than you priced your other product for. You may find that there is a different male/female mix--which is important because rates are unisex now. You may find that the employer has some kind of wellness program or gives annual physicals to his employees. These demographics can work both ways, however. I have had problems convincing our marketing people of that. We recently had a case that wanted a special exception because of the female/male mix. It was 50 percent female--which is much higher than our normal female mix. After getting the data on that group we also discovered that the average size policy was going to be \$10,000 less than our pricing assumption. In recognizing all these special requirements in the price, we found out that they were no better off than if they had taken the normal product. Sometimes you have to be willing to go both ways on a particular product.

Another thing which we are seeing now is that some employers want to get involved in reinsurance. There are usually two reasons for this, which don't always coincide. The first reason is that they want to get a piece of the action. Sometimes the agents, in exchange for lower commissions, will want to use some kind of reinsurance as part of their compensation. A reason that employers sometimes want reinsurance is to lower the cost to the employees. If a particular case is rated, the employer will sometimes ask us to do a reinsurance quote or to reinsure with him, and he will take the mortality risk.

In short, the market and the products are still being defined to some extent. At least the market that we are in at Life of Virginia. I will turn the mike over to Gabe--hopefully he will have a totally different market because we don't want to compete with the PRU!

MR. GABRIEL CILLIE: From the Prudential standpoint, the small case is a case which has less than 250 lives. We feel that from a marketing standpoint, it is a market that the agent can control--a small case market. We entered it hoping to increase agent daytime activity, increase agent income and productivity, and perhaps lead us to some spin-off sales.

Prudential has experienced both the risks and rewards of this market. Early in 1979, Equitable of New York introduced a program called Equi-Sur-Plus. The program was built upon two Whole Life products to be sold to employees, with the premiums normally paid through payroll deduction remittance. Premiums were discounted and simplified underwriting was used. The product was an immediate sales success and by mid 1980 Equi-Sur-Plus was producing some 17% of Equitable's individual life new business premium income.

In February 1980 a task force was appointed at Prudential by executives of the Actuarial and Agency departments to study the possibility of Prudential developing life products to compete with Equi-Sur-Plus. In October 1980 the task force made its final report and recommended a program which it believed to be both marketable and financially sound. It concluded that a June 1981 introduction date was possible. The program was called Pru-PEP.

Prudential's Pru-PEP program was announced to the field in September 1981. Important features of the program included:

## PANEL DISCUSSION

- o Special low premium individual life insurance policies (Life Paid-Up at 70 Policies).
- o Simplified underwriting -- applications will be taken on a "guaranteed-no-rejection" basis for proposed insureds actively at work and will almost always be underwritten on a non-medical basis.
- o The standard class covers risks up through the normal Special Class 2. Pru-PEP also has two broad substandard classes, A and B, in contrast to the eight classes for our normally underwritten business.
- o For a proposed Insured who is carrying out the normal duties of his or her occupation, life insurance coverage will start as soon as the application is signed. The first premium is not due until two to three months later.
- o Policies are to be sold on a salary deduction basis only. The first premium is to be collected by deduction. The Pru-PEP remittance program has new features that improve upon the current Payroll Budget System.
- o More than one policy may be written on members of the same family with a single application.

Another unique feature is the immediate crediting of a portion of the first year commissions, even though no premiums had been collected. Our regular commission payment practices including potentialization apply to the remaining portion of the first year commission.

For dividend determination purposes we assumed that standard Pru-PEP mortality during durations 1 through 4 would range from 110% of Prudential's Gibraltar Series Mortality (Policies with Face Amounts less than \$25,000) at issue ages 15 and 25 to 210% of Gibraltar mortality at age 75. Lower percentages were used at the longer durations.

In addition to the basic Life at 70 Policy available to employees and spouses ages 55 and under and to children, a 15 Payment Life policy is available at ages 56-70 and a supplementary 15 Year Level Term Rider is available at ages 10-50. An employee can purchase on his own life up to two times annual income subject to a maximum of \$150,000, on the life of his spouse one times annual income up to a maximum of \$50,000 and on each child up to one times annual income with a limit of \$20,000.

The product was designed for the less than 250 life cases since we use a roster billing system, so it is not an efficient program for large cases. Each page on the roster has about 20 lives. It is clearly not something that a large company payroll department would want to deal with.

Pru-PEP was an immediate sales success with the number of policies sold exceeding 15,000 per month in the months following the introduction. The average case was quite small averaging about 3½ lives while the average face amount was about \$12,000.



But problems began to surface. The authorization of commissions without premium collection, together with the recapture on non-placement, made it against the agent's own self-interest to report a case as not taken. Not-taken rates averaged 30% on Pru-PEP sales in contrast to our average not-taken rate of 10% on other individual life sales. In many instances, insurance coverage continued to be provided, even though there was no bona fide group; or if there was a bona fide group, there was no possibility of collecting the first premium. We had a great many policies with no income being received.

A substantial number of early claims appeared, several of which showed extremely poor field underwriting by agents.

Early estimates of mortality, based on reported claims and exposures derived from sales figures, suggested that actual mortality rates were higher than expected. Early lapse rates were also in excess of expected but only marginally so.

The first reliable measure of experience mortality came from Prudential's 1982 Calendar Year Mortality Study. Based on 89 claims, Pru-PEP standard issues showed a claim rate of more than 350% of the Gibraltar series claim rate, and substandard PEP mortality was more than 1,000% of that of the Gibraltar series, based on 30 claims. These figures, of course, include the extra claims during the initial period of free coverage for which there was no corresponding exposure. Because of this fact, and the much more intense anti-selection possible with Pru-PEP, mortality rates were expected to fall off rapidly by duration. In fact, the experience on Pru-PEP in 1983 showed consistent improvement over that in 1982, both on standard and substandard issues. Based on 76 claims, Pru-PEP standard issues showed a claim rate of 155% of 1965-70 Basic Table Mortality and based on 8 claims, Pru-PEP substandard showed a claim rate of 418% of 1965-70 Basic Table Mortality.

Several things have been done to correct the problems in the Pru-PEP program.

- o The Regional Home Offices were encouraged to apply tough field underwriting standards to Pru-PEP.
- o A new application has been designed which precludes immediate coverage in the case of a recent serious health history, cancer, heart attack or other heart disorder, or stroke within the last two years. We had a number of claims where people were actively at work while they were in the later stages of cancer.
- o Certain types of businesses will no longer be eligible for Pru-PEP because of their expected high "not taken" and lapse rates.
- o Commission will no longer be authorized before the first premium has been collected.
- o Higher mortality and expense assumptions were used in developing the 1984 Pru-PEP rates and dividend scales.

Once we stopped fronting the commissions, sales dropped substantially. Hopefully we are getting a better class of business in. Actually, the sales

had fallen off from the initial spurt. Sales averaged about 4,000 policies per month. From the results I am seeing now, they are averaging 1,000 - 2,000 per month.

Some Brief Comments on Questions Listed For Today's Panel Discussion

(I) What Motivates Employers to install such a Program?

How do they perceive the value and impact of program installation?

- (1) Pru-PEP offers employers the opportunity to provide a valuable service to their employees -- with no contributions required on the employers' part.
- (2) Pru-PEP affords employees a low-cost way of obtaining permanent life insurance protection with a convenient method of premium payment built into the program.
- (3) Pru-PEP offers a variety of specific and valuable benefits to employers and employees.
  - o Low going-in premiums
  - o Simplified underwriting requirements
  - o Easy, automatic premium payments through the Pru-PEP remittance program.
  - o No premiums due for up to 90 days for qualified applicants (agents like this feature)
  - o The advantages of cash value permanent policies
  - o The additional availability of low cost 20-year level term rider coverage
  - o A Waiver-Of-Premium Benefit
  - o Availability of spouse and children's coverage as well
  - o Portability -- Employees can continue their coverage even if they change employers by changing to another premium mode. We have had quite good success in people continuing their coverage. That is one of the benefits of the program.

- (II) What special distribution system requirements exist? In Prudential's case Pru-PEP is marketed through the same field force, both District and Ordinary Agencies which market our other products. For the small case market no special distribution system requirements are necessary.

## (III) What are the critical administrative considerations?

- (1) Have the agent develop a good working relationship with the Employers from the start so the program is installed properly, deductions are started, the initial premium is paid, and Prudential is notified when any employee leaves the company so coverage is continued without interruption. Many agents have found that collecting the first premiums from the bookkeeper helps get the program started on the right foot. Such efforts will pay off in low not-taken rates and low lapse rates.
- (2) Have the agent review with the Employer and the Bookkeeper
  - o The approximate date they can expect to receive the Advance Notice listing program participants, and the first Billing Notice;
  - o The importance of timely premium payments and the length of time which premium payments can be overdue before employees are dropped from the program;
  - o The employee status changes which should be reported to Prudential
- (3) After the policies are issued, the agent should personally deliver them to each employee.

## (IV) Which Products serve the market most effectively and why?

For Pru-PEP's market, it was concluded that a unique permanent policy with low going-in premiums (not necessarily low cost since dividends are low) which develops high cash values; supplemented with the additional availability of a low cost 20-year level term rider along with the availability of spouse and children's coverage would effectively serve the market. Pru-PEP's product, the Life at 70 is unique since the regular portfolio offers Life at 65 and a variety of Whole Life Policies.

MR. CHRISTIAN DESROCHERS: Thanks Gabe. Before we open it up for questions, I have two or three issues for the panelists to try and address. The first is: How have your companies reacted to the Norris decision and how is this reflected in your products? Tyler discussed it indirectly by talking about a unisex product. I think that people will be interested in exactly what process you went through to adjust your product or not adjust your product after Norris.

MR. TYLER LEE: Well, I have a few more grey hairs. Basically, when the Norris decision came out we realized that regardless of nice intellectual arguments that it really is not an insurance company problem--Norris deals with Title VII which is an employer problem--the realities are that if you are going to be in the market you have to have a unisex product. If the employer goes to his lawyer and his lawyer says Norris affects this particular product then he is going to ask you what you can give him which qualifies. If you have nothing then you are not in the market.

It was easy to do something with the new sales and we did that fairly quickly. We unisexed our rates and by saying that the male rates are now unisex rates. Actuarially, I have a problem with anti-selection when you have taken to account male/female mix, and they can go out into the open market and buy sex-distinct policies. We still have yet to see what effect that is going to have, but we do have a blended rate. We still have not done anything with inforce policies and we have a lot of them out there.

MR. WILLIAM TAYLOR: Unlike Tyler who's hair turned grey, mine fell out. Tyler was in a unique position because he was selling universal life products. He could just change his cost of insurance rates and he would be done. We were selling whole life policies and it wasn't quite as simple as that. We wanted to re-price our products quickly. We now have a unisex whole life product.

As far as our inforce, ideally, we would have liked to have gone in and changed the rates so that the female got charged a little more and the male got charged a little less.

We took this to a company committee. What the committee decided--there was a very strong legal representation--was that all the obligations and promises that we had in those contracts had to be met. Our legal department took the position that although Norris required equal benefits there was nothing that allowed you to reduce benefits. Essentially what we did was to lower the male premium rate on our inforce policies to the female level--which in effect gave the male more insurance. We didn't want to change the deduction because we didn't want to go in and tell the payroll department to start taking out a different deduction for these people. We sent a little notice to the males to let them know that they would receive more insurance. On the female side, we had to notify them of the higher surrender value because we topped their cash values up to the male levels. We took the worst case hit and topped up all the benefits.

Although it cost us something, we gained a marketing advantage. We went back to each of the employers and took time to sit down and explain to them our decision. Every one of their lawyers told us that if we didn't do something then they were no longer going to deduct premiums. We explained the Norris decision and how we were going to respond. We used this evidence of Puritan's reaction to regulatory change. We used it as a good faith sign of how important we considered our program. We told them that we were in this market place to stay. It was hard to sell our management and the management of the General Electric Credit Corporation, but because we had the backing of our legal department all the way it was not too bad a fight. I am very glad that this didn't happen 10 years after we had been in the market place. We had only been in there three years and the number of policies were not what it could have been had we reached our premium goals in those prior years.

MR GABRIEL CILLIE: At the Prudential, we simply unisexed the rates. We didn't go back and adjust the inforce. It was fortunate that the decision was so close--and the August 1 date applied. We just started issuing male policies for both male and female.

MR. CHRISTIAN DESROCHERS: One of the things that we are asked by clients who are interested in the market is the use of professional enrollment

firms. I wonder if anyone has any experience using the professional enrollers and what comments they might have.

MR. WILLIAM TAYLOR: We have tried some of the professional enrollers. What we found was that if the enrollers are commissioned we notice a large increase in the premiums and a large increase in the net taken rate and a large increase in our subsequent lapses. Whenever we have entered into agreements with these professional enrollment firms, even though we might pay the firm on a commission basis for the use of enrollment services, we insist that the actual enroller be paid on a per diem basis because we really don't need over selling. If you over sell the employees, you have an unsatisfied employer-- which means you have a bad case. We find that it is really very industry specific. If you develop a bad name within an industry it kind of goes to the other companies in that industry. The employee benefit manager of one company knows the employee benefit manager of the other company down the road.

So we avoid that altogether.

We have our own home office enrollment team. That is one of the things that caused us to develop our own home office enrollers. We have a substantial number of enrollers in our company. When we get enrollment schedules that we cannot handle with our own enrollers, we still do use those professionals, but the actual enrollers get paid on a per diem basis.

MR. GABRIEL CILLIE: As far as Prudential goes, we are in the small case market and we don't have experience with professional enrollers.

MR CHRISTIAN DESROCHERS: One final thing that I will ask you to comment on-- how do you see the competitive environment changing? It certainly sounds as if one way for companies to address the problem of selling relatively small amounts of life insurance is through a payroll-type program where there are economies of scale. We have seen, for example, Life of Virginia is in the market because of a desire to use the universal life product. Puritan is in the market because that is their corporate marketing philosophy. What do you see happening in the next few years in terms of number of companies being interested in this?

MR. TYLER LEE: From our standpoint Chris, as I mentioned, competition has definitely increased from three years ago. It seems like everyday new competition has entered the field. This is the very reason why I said that we will probably be developing a fourth generation product next year at this time. I see it continuing.

MR. WILLIAM TAYLOR: I agree with Tyler. The competition is going to be ridiculous. There are more people coming in it. The introduction of the 401(k) plans made the use of payroll deduction life insurance much more attractive. 401(k) is a hot word in the Fortune 500 companies and is one of the reasons why we decided to develop our own universal life. We know that in the larger companies, one of the reasons why they wanted universal life was that it fits quite smoothly to a 401(k) scenario. I am always getting phone calls from people who are entering into the payroll deduction market place looking for information. I am amazed at how many companies there are. Once upon a time we considered ourselves the only payroll deduction life insurance company. That is clearly not the case anymore.

MR. GABRIEL CILLIE: Generally, on the competitive front in 1983, Prudential had a good sales year. This year is frankly not going as well as last year. The company is experiencing a lot of competition from interest sensitive type products and is developing several products along those lines. In talking to the agencies, I think they segment the payroll deduction in three blocks: (1) less than 250 lives, which we have now as Pru-PEP, (2) more than 1500 which they feel the agent cannot control and (3) a niche market running from 250 to 1500 lives--which they think is not that big and that an agent can control it. In that market they think they will need interest sensitive produces and guaranteed issue. Pru-PEP is not for that market, however.

MR. JOEL WOLFE: I have a couple of question for Bill: First, how often to expect your salaried sales reps to sell increases in coverage? Second, have you sold any increases and if so do you charge another policy fee? If the answer to that is yes, do you plan to roll those increased policies over into your universal life when you develop it?

MR. WILLIAM TAYLOR: You are referring to what we call re-enrollments. We do promise to go back in and do re-enrollments. There seem to be two schools of thought on re-enrollments. That is, if you have a good enrollment experience the first time and you have a large participation, does that mean the company is ready for another enrollment one year later? We always enroll new eligibles on a timely basis. The other argument is that if you had a bad enrollment the first time, you could get better results a second time. We have done three re-enrollments and the results are mixed. I would say that both the arguments have some merit to each of them.

On the re-enrollment portion of your questions, our policy doesn't have a policy fee. We have standard rates on a money purchase basis, which are in equal dollar increments. We have what we call a three dollar plan--you sign up for three dollars a week. It basically says how much insurance you will get for your age at \$3.00 a week. Then we have a four dollar a week plan which has a little smaller premium rate per \$1,000. If the person has signed up for a three dollar week plan at his original age and he is re-enrolled for an additional two dollars - he may be better off using the five dollar premium rate at the older age or he may be better off maintaining his insurance coverage on the old three dollar plan, with a little higher rate but at a younger age and buying the additional two dollars per week. That is another problem with re-enrollment that we haven't solved. What we do is we do a calculation which essentially gives him the better price. If the discount in the new plan is significant we counsel him to drop the old one and take out the new one. That is because we know what he is going to do anyway. We would like, and our expectation is, that when we do develop that universal life policy this problem will go away. That is another big reason for doing it.

MR. THEODORE J. KITSOS: I have a question for all the panelists: What kind of minimum participation requirements do you have, if any?

MR. TYLER LEE: I'll take that first. We changed ours recently because we found we had a lot of not takens, people were trying to reach the participation requirements for a guaranteed issue. We changed about 6 months ago, so there is absolutely no guaranteed issue below 100 lives. A case has to be

100 eligible lives before there is any guaranteed issue, then we require a 30% participation for guaranteed issue.

MR. WILLIAM TAYLOR: I'm afraid that I'm going to have to cloud the issue a bit. It is important that when I talk about our participation requirements or expectations that I define what I mean when I say participation. We really track two numbers - participation and penetration. We define participation as the number of employees who take out a deduction divided by the total number of eligible employees. So participation rate really represents how the program was received by the employees. We use that more as an indicator of how well the case was sold - did the employer really back the program the way he should.

We have another indicator which we call the penetration rate, defined as the total number of policies (which would include any dependent policies) issued on that case divided by the total number of eligibles.

What we found out was that we get about 35% participation rate, that is pretty standard based on the way we do it, and is very good. We have a very low not taken rate. We had priced a two digit non-participation rate and it is about half of that. As far as the penetration rate goes, when we first started out the program in the small case market (50-100 life), we were getting substantial penetration--in the neighborhood of 75-80%. For every eligible employee we were getting .8 insurance policies. We found that as we move upscale in the market, that both the participation rate and the penetration rate have gone down. The participation rate has not gone down significantly but the penetration rate has. We were down to the 5% level which is what I consider a fairly significant decrease. Now, we have more employees per case so even though the penetration rate is lower, on the average we probably come up with a reasonable number of policies anyway. We view penetration as a measure of anti-selection. We would much rather have a higher penetration rate and a lot more policies, than have a high participation rate.

MR. GABRIEL CILLIE: As far as Pru-PEP goes, we insist that the employer has at least 5 employees and at least two of the employees must enroll.

MR. WILLIAM TAYLOR: I should add one more comment. We started out with participation and penetration guidelines and we told our sales rep you have to get these numbers. The problem is they don't know when they sell a case what the numbers are going to be. Even though we give them guidelines, we don't hold them to those guidelines on a case to case basis. We keep a running tally on each sales rep as to how much participation and penetration he is getting on his case. If it goes below that on any given case it is not really a bad sign, it may be indicative of that particular enrollment team didn't mesh well together. So even though it is a requirement--it is not a case to case requirement.

MR. TYLER LEE: I have to echo what Bill said. We have what we consider guidelines. Very often what you have to do is keep track of your agents or broker. You know who is going to get the business and who's not. Very often you use that to determine whether you are going to use guaranteed issue or simplified issue for a case. The 30% figure is the basic guideline.

MR. FREDERICK K. MOLEN: I have a question for Tyler: you mentioned that some of your employers are asking for reinsurance arrangements, could you tell us a little about how those are structured and when you consider it, whether they require them to have a captive subsidiary and how much of the profits they get?

Mr. TYLER LEE: The question has come up on at least two or perhaps three cases and I mentioned that as a trend that I see. We have not at this point written any reinsurance. At this point they have not been serious enough to take the deals that we would have offered. This is about as specific as I can get to your question.

MR. MARK KINZER: I am wondering if any of you have looked into the question of smoker/non-smoker rates for an employer sponsored plan?

MR. TYLER LEE: We have smoker/non-smoker rates, if that is what you mean, in our payroll deduction plan. We instituted them with our second generation product in early 1983. We have resisted preferred non-smoker.

MR. WILLIAM TAYLOR: We do not have smoker/non-smoker currently, we were in the middle of developing our smoker/non-smoker policy when Norris came down. We do expect that our universal life, plus our new repriced unisex whole life product, will have smoker/non-smoker discounts.

MR. GABRIEL CILLIE: As far as Pru-PEP goes, we do not have smoker/non-smoker rates. We feel the competition is not too great in the real small case market. Our regular portfolio, of course, has smoker/non-smoker. I think that if we went into the bigger case market, we would definitely have to go to a smoker/non-smoker scheme.

MR. TYLER LEE: I would just like to add one other comment. On our own payroll deduction policy (all of our policies have smoker/non-smoker) we have the highest proportion of smokers. That particular policy is running about 40% smoker. This is kind of unbelievable to me. At least they don't seem to be lying about it.

MR. S. VINCENT ZINK: Tell me about minimum premium, the smallest size--\$3.00 or \$4.00 a week, for example.

MR. TYLER LEE: We basically have a \$4.00 a week minimum premium although we have gone down to \$3.00. Everything we have seems to be guidelines and not something that's set in stone. But \$4.00 is basically our minimum premium.

MR. WILLIAM TAYLOR: We have a \$2.00 a week plan up to \$9.00 a week. We will only offer \$3.00 to \$9.00 to employees. We have a \$2.00 a week plan which is used in initial enrollment only for children, but we have been using that \$2.00 a week plan on re-enrollment cases where a person already has a \$3.00 deduction and really cannot afford another \$3.00 deduction. I do not have to tell you about the problems involved in pricing a \$1.00 a week plan. We pretty much made the decision that if all they need is \$1.00 a week we are really not going to be able to help them in that situation. They have to get their deduction up to an additional \$2.00.

One problem is that even though we are on a money purchase plan, the minimum policy we will issue is \$3,500. At the older ages there isn't a lot we can do.



MR. GABRIEL CILLIE: As far as Pru-PEP goes, the minimum policy size is \$5,000. I would like to echo what Bill said that a lot of most of our district agents sell our products on a weekly deduction basis--which is very popular, \$3.00 or \$4.00, as I say our minimum policy size is \$5,000.

MR. WILLIAM TOZER: This has to do with policy dating. If I am not mistaken, Bill stated that he was dating his policy at about 45 days down the road. Most policies that I have seen in the salary savings market are set up on the internal files on a monthly mode, but you are running a weekly payroll deduction very often. Don't you get into a funny billing operation--that you are usually billing for 4 or 5 weeks. What kind of problems are you into as far as dating policies and really not getting enough money on your first monthly billing to get the policy paid for.

MR. WILLIAM TAYLOR: I should be a little more exact about the way we issue. The rule is: the issue date is the first day of the second month following the date the application is signed. So, anybody who gets issued a policy who signs the application this month, their date of issue is not the first of next month but the first of the month ahead. So that is why I said anywhere from two months to as low as one month. We do try to get the employee to start his deductions as early as possible. We modified our administrative system heavily for the payroll deduction marketplace. One of the things that we had to put in was what we call special frequency billing. We have the capabilities essentially to bill as often as the employer wants to be billed. Our most frequent billing mode is every four weeks instead of monthly, almost thirteenthly. It was a major modification.

MR. TYLER LEE: We did start with a monthly billing and it didn't work. This is a serious administrative problem to overcome. It may be product which gets you into a particular employer, but it is service that keeps you there.

MR. S. VINCENT ZINK: While you are on the topic of billing, have any of you had requests from employers who get around their payroll system and let the employee use some sort of a bank check plan? Also, do you use a bank check plan for people who have terminated employment?

MR. WILLIAM TAYLOR: Yes, when someone terminates employment, we originally had a policy that we insisted that people use what we called pre-authorized check. Unfortunately, many blue-collar workers don't have a checking account and that becomes a problem. We have been billing. We advertise the fact that when an employee leaves the employer there is no change in the premium. But if you look at our current premium rate, we have built into the pricing only one bill for a mass of policies. If we have to do billing every month on the individual policy, the premium cannot support it. We cannot get the profit out of it that we want so we have to modalize. We have a lot of resistance and we go back to the employee after he has terminated employment with that employer trying to get him to accept an increase in his premium. That is where we stand right now. For people who have checking accounts, and we strongly urge them to let us set them up on PAC we do, for those who say they don't have a checking account, we go ahead and modalize the premium and we charge them accordingly.

In regard to the time at issue, when we first set up the case. We don't consider going in with PAC a good faith sponsorship on the part of the employer. It is really not worth that time and effort if he is not going to

back the plan at least enough to set up the payroll deduction. We had to go in on one particular case and move all people over the PAC or monthly direct. We have not had any situations where on a case that we really wanted, the employer insisted that we go PAC from the start.

MR. GABRIEL CILLIE: As far as Pru-PEP goes we really insist that the employer accept a roster billing system. That is really representing good faith on the employer. If he doesn't want to do that we really discourage the case. As far as conservation when employees leave, early in the game we were sending a coupon book out to the agent (we changed our system so we send a coupon book directly to the insured) and that is how we find out that he has left the employer.