RECORD OF SOCIETY OF ACTUARIES
1984 VOL. 10 NO. 4A

NON-TRADITIONAL LIFE INSURANCE PRODUCTS—CANADA

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A review with an emphasis on the marketing perspective of recent developments and trends, including:

Term to 100 and lapse-supported products

New money and other adjustable ordinary life products

Universal life

Business term

MR. TREVOR C. HOWES: The obvious question that springs to mind when asked to consider non-traditional life products is what is meant by "non-traditional"? Upon reflection, virtually every product of significance in today's market can be termed non-traditional in one way or another.

In the U.S. and in Canada, the Life Insurance industry since its birth has developed along very similar lines, and practically all companies carried the same set of basic products, perhaps with different names, but readily recognizable as level and decreasing term, endowment and whole life, with or without limited premiums. Permanent versions can be described as coming in two flavours, Par and Non-Par.

All these products, though, generally had fixed guaranteed face amounts except, I guess for paid-up additions, which are not predictable, and they also had fixed guaranteed premiums, so these are two features of what you might call traditional products.

These products were sold by career life agents generally, working solely for one company, for the most part,and were remunerated by high first year compensation.

Cash values on permanent plans were based on standard mortality tables, (often the same ones throughout the whole industry) and, low interest rates, and were often identical between various companies. The premium rates were perfect examples of actuarial conservatism, at least to the modern eye blessed with 20/20 hindsight.

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As we all know, the new products of today commonly show few if any of these characteristics. While companies still carry a skeleton set of basic life products that strongly resemble those of the traditional lines, the lion's share of their marketing thrust and their sales are on the new wave of products.

Our topic has specified the Canadian scene and this is a meaningful distinction today. The innovation in and evolution of life insurance products has been partly responsible for some divergence in the life insurance markets in Canada versus the U.S., contrary to the past.

Canada has provided a less structured and restrictive environment in which to cultivate new ideas, because of, among other reasons:

(1) There is a lack of legislated minimum nonforfeiture values. Therefore, there is a great deal of flexibility in terms of shape and size of cash values and other values.

(2) There is an absence of policy form or premium rate filing requirements in all provinces, the only exception being for variable products that are unit-linked.

(3) Another major reason is the great adaptability or flexibility of our valuation rules to various product designs and types and new ideas, and the requirements to take all contingencies including lapse rates into account in developing reserves. Furthermore, there is no direct minimum premium basis specified here and therefore while deficiency reserves can occur in a form, they can be much better suited to the actual shape, design and type of product considered.

For all these reasons, then, Canada has been a fertile environment for ideas in non-traditional products. Our panel today will attempt to describe some of these product trends they have seen and are seeing in Canada, and hopefully share their thoughts on the whys and wherefores of these developments.

MR. GRAHAM R. DIXON: I am going to speak today about the evolution of non-traditional products. What is a non-traditional product? I have two rather simple minded answers to that question. One that was not available 15 years ago and one that is not described in the Jordan's "Life Contingencies".

Over the past 15 years, we have been part of a significant revolution in life insurance products. Traditional products had stood the test of time, mostly, I believe, because of their simplicity. Once the basic concepts were established, they were easy to price, easy to administer and easy to explain - even life insurance agents understood them.

There is one more important characteristic to the buying public, though, and that is, of course, price. For years actuaries could bask in the security of layers of conservatism to such an extent that it took more than incompetence to fail: it took premeditated malice.

During the last 15 years, several things have changed.

- The life insurance industry has encountered sharp competition from other financial institutions, most notably in Canada from the banking establishment.

- Technology has been introduced at an accelerating pace, facilitating even more complex communications, calculations and record-keeping.
- The economy has been in turmoil, with high unstable interest rates, sluggish growth, unemployment and intermittent inflation.

- Within the industry, replacement activity has become for many companies a nightmare.

These factors and others have forced actuaries to abandon their old methods. What I am going to do today is to discuss new ideas and how we have modified traditional plans to compete in the market place of the 80's.

In some ways these modifications are really old songs with new singers, but they do represent at least a new flexibility in our thinking.

I will discuss the new products in relation to the basic elements of pricing. Obviously these are mortality, persistency, expenses, compensation, interest and non-forfeiture values.

Let's take mortality first. How can mortality be adapted to effect positive changes and produce non-traditional spin-offs? Mortality has declined steadily during this century, but that change could be reflected in a traditional plan. We have done two major things with respect to mortality. First, we have distinguished between mortality differences of males and females and of smokers and non-smokers. In the U.S. we are now having to reverse some of this reasonable discrimination with respect to sex. This has not yet happened in Canada. The smoker/non-smoker differentiation produced a major adjustment in product development in the early 80's and is now almost a universal feature.

Second, we have cashed in on the select feature of mortality with the use of select reentry term products. In Canada, select reentry YRT has not been used much and we have thus avoided the heavy losses some U.S. companies have experienced with it.

Financial Life has a YRT plan called ExecuFlex which allows for reentry underwriting at each tenth policy anniversary. We have used the reentry feature though on 5 and 10 year renewable and convertible term plans. My own company, Commercial Union Life, has, for example a select reentry 5 year R & C plan.

How can we modify persistency? Persistency is a fact of life, often one of the less desirable facts of life. Nonetheless, we can insulate ourselves against its effect in two ways.

First, we can offset high front-end acquisition costs with high front-end fees. Several Canadian companies have adopted this approach with Term products. Five companies which use this approach are:-

Laurier Life with Business Term;
Mony with Termadex;
Occidental with Pure Term;
Financial with ExecuFlex; and,
Northern Life with Magnaterm.

I believe Laurier Life's Business Term has been very successful. It is sold in large amounts, over $200,000, and the first year premium is increased by a one-time underwriting fee of $200 to $600 and an acquisition fee, apparently set by the agent but dependent on service and within limits set by the Company. In this way, the renewal premiums can be set at a much lower rate.

The other way to help prevent poor persistency is tied in with a non-traditional approach to compensation and that is the use of level or levelised commissions. Although this topic has attracted a lot of discussion, it has not yet become very popular in Canada, mostly I believe, because most agents still prefer cash in pocket! When it comes down to it, they prefer to pass the persistency risk to the Insurance Company rather than keep it themselves. Level commissions are available. Financial Life's ExecuFlex is an example.

What about interest rates? I am sure most of you know the answer to that question. A traditional product, particularly a non-par permanent plan, guarantees an interest rate for its duration. Now we have whole life plans which guarantee a rate for a relatively short time, typically 3 to 10 years, but in so doing allow a much higher interest rate. These plans usually modify other traditional pricing elements. Take for example, Zurich Life's New Money Life plan. It is a whole life plan with low cash values and a premium rate guaranteed for 5 year periods. At issue and at subsequent renewals, interest, mortality, persistency and expenses are reviewed and a new premium rate is set. Incidentally, this is a participating plan. It pays no dividends but company experience is reflected in changes in premium. Otherwise, it retains traditional features of guaranteed face amount, guaranteed cash values and guaranteed paid-up values.

Another example is Manulife's Guaranteed Renewable Whole Life plan. This is a non-par whole life plan with low guaranteed cash values and premium rates again guaranteed for 5 year periods. At renewal, interest, mortality and expense assumptions are reviewed and a new premium is set for a further 5 years.

One of the most effective changes to the traditional plans is by changing cash values. The "new money" products I have just mentioned had guaranteed "high-interest" scales of cash values. If these guarantees are removed substantial premium reductions are possible. I would like to look at this for two types of plans. The first is a plan with floating cash values. An example of this is Seaboard/Fidelity's Apple 2 Plan. This is a non-par whole life plan with guaranteed sum assured and premium reviews every 5 years. The cash values accumulate on a formula basis. After each premium is paid, a deduction is made for mortality and expense. These are guaranteed. The remaining money goes to a cash value account, where interest is credited monthly according to a McLeod Young

Weir Bond index. If it is surrendered, a new money adjustment is made to the pay-out. A similar plan is offered in National Life's Ultraterm.

The second modification to cash values of permanent plans is to remove them completely. This type of plan is typically called Permaterm or term to 100. Toronto Mutual, for example, has a plan called Extra Term Modified. This is a low-cost adjustable term to 100 plan with no cash or paid-up values, but with an extended insurance benefit if premiums are discontinued.

Most typically, though, these plans do have paid-up values. Examples of these include Westbury's term to 100 and Manulife's Guaranteed Renewable Insurance Protection plan.

The greatest effect can be achieved, of course, by removing all non-forfeiture values. This has been done with Seaboard's Stripped TLC which stands for Term Life Coverage.

I have surveyed some of the major modifications to traditional plans. Clearly, the direction is towards Universal and Variable Life where advantage can be taken of all kinds of flexibility not available in traditional plans.

Where will changes occur in the future? I believe that product development will place less emphasis on the traditional structures of the past. As an industry, we will likely be more concerned with distribution systems than with products in the latter part of the 1980's. We will see more life insurance sold by financial planners who will charge clients a fee for service and receive level commissions. There will be a merging of the life insurance product with other financial products as the financial institutions themselves merge. We will see more insurance sold by direct marketing. As actuaries we will have to use more and more of our creative talents just to enable our companies to survive. This should be taken as a challenge and an opportunity.

JIM E. McARTER: I am going to look at non-traditional life products as seen from the smaller Canadian company.

There are approximately 20 smaller Canadian companies that are actively writing individual business, mainly through G.A's and brokers.

Although small by U.S. standards, smaller Canadian companies would each average in force individual business of approximately 3 billion dollars, and would be writing new individual premium in the order of 3 million dollars per year.

The development of the small Canadian companies actually started in the early 1970's with the reintroduction of an old traditional product that was buried in everybody's rate manual, the 5 Year renewable and convertible term.

This product developed again somewhat because of inflation and the rise in popularity of mutual funds and other investment vehicles not sold through life insurance companies. People began to compare the high return on investment from traditional life company products such as whole life and endowments with their conservative cash flow, compared to the high yield from mutual funds and segregated fund products.

The consumer changed in his feeling of a life insurance product as a savings and protection vehicle to only a protection vehicle, and protection at a low cost.

In this scenario, smaller life companies, most of whom had no career field forces, began to develop 5 year R & C term rates and market them through brokers. It was an inexpensive way of marketing, using larger companies' existing career agents to sell their products. The larger companies of course had much higher premium rates, much lower commission on term products, and initially were not too concerned with the loss of this type of business. Therefore, the smaller companies became heavily involved, with reinsurers for support.

5 year renewable and convertible term took the form of maximum term insurance to age 65, to age 70, and to age 75. Next developed 5 year renewable and convertible term products that allowed the client the opportunity to be re-underwritten at each renewal period, the privilege being much lower premium rates at renewal. These were known as preferred renewal rates.

This preferred underwriting gained a moderate degree of success in the market until some companies' renewal underwriting became too stringent and many consumers found themselves not qualifying for the preferred rates promised, and they faced much higher guaranteed rates.

In the late 1970's came the revolution of non-smokers which did as much to upset the traditional marketing and pricing of life insurance as anything ever has. Initially three or four smaller Canadian companies jumped on the State Mutual Non-smokers Report and seized it as an opportunity to quickly create a substantial new market.

Most of these smaller companies did not have a large amount of in force business and therefore did not have the concerns regarding replacement of in force business. The general lifestyle change to non-smoking, combined with cheap term protection, inflation, and other attractive investment vehicles, with low policy loan privileges on their existing products, led to the replacement of thousands of existing policies. Consumers became educated to the new revolution in rates and product, and agents found a whole new market, and although not paying as high a commission as tradition products, agents found the sales quick and easy.

Premium rates began to be lowered as competition grew among the smaller companies. Smaller companies were relying on substantial coinsurance terms from reinsurers, and in fact, many smaller companies became marketing organizations for reinsurers who were financing the strain of writing vast amounts of business that many of the smaller direct writers could not themselves afford. Reinsurers at that time seemed motivated by market share alone.

5 year term being the standard, other companies followed with 1 year, 3 year and 4 year renewable and convertible term products.

However, in 1980 it became evident that many consumers were interested in longer guarantees and the 10 year R & C contract became quite an attractive alternative to the 5 year R & C product. This product was guaranteed to age 70, in somes cases 75 and in one case even to age 80. One benefit to the company of the 10 year R & C product appeared to be better persistency.

One company's 10 year R & C plan included an automatic increase, without evidence, in face amount and premium of 12½% at the end of years 1 and 2. Incidentally, after four years exposure, the company has constantly had an 85% acceptance rate on this feature. It is built into the plan and must be refused by the client in writing, on anniversary.

Because this particular company was so successful, it was able to increase its in force business by several hundred million dollars of business without paying any first year commission.

One of the enormous problems of this period has been the huge replacement of business, aggregate to non-smokers, non-smokers to lower priced non-smokers and cash value plans to term. The industry has witnessed a tremendous upheaval, an upheaval probably most harmful to the larger companies and most beneficial to the smaller companies.

A very popular evolution from whole life in Canada has been to term 100 in its various forms.

There is straight term to 100, with premiums paid every year until age 100, or prior death, with no non-forfeiture values - a product that is not highly regarded by the Department of Insurance.

There is term to 100 which if paid to 100, then endows. There is term 100 which has reduced paid-up values and no cash values; term 100 with reduced paid-up and small cash values; term 100 paid up at age 65 with generous cash values and no reduced paid-up, the only non-forfeiture vehicle being extended term. There is term 100 with guaranteed premiums and term 100 with adjustable premiums at 5 and 10 year intervals.

The popularity, of course, of this product is that it is a cheap alternative to whole life or limited pay products, and, along with the 5 and 10 year term, proved to be one of the most successful products in Canada.

Business Term - one company has introduced its Business Term series of products which to quote their marketing department produces "wholesale rates" with "no frills". The plans initially were non-renewable and non-convertible - no cash surrender value and no additional benefits such as waiver of premium and accidental death benefit were allowed. The plan was geared for the business market and durations of the plan ranged from 3 to 5 to 10 to 20 years, to age 65, to age 75 and to age 100.

Now, the interesting aspect of these plans is that the agent assigns his or her own commission, which initially could vary from .5 to 2 times the basic premium (first year only). The commission was set depending on the amount of time the agent felt he had spent on the particular case, and whether or not he was in competition with another agent. In addition to the agent's compensation, a policy fee of $75.00 and an underwriting fee varying from $200 to $500 was assigned.

In most instances, the first year premium was below the competition and becomes more competitive in the second and subsequent years with the removal of the commission - remember there are no renewal commissions available - and removal of the underwriting fee.

The company has subsequently brought out enhancements to the existing products, allowing additions of paid-up values, waiver of premium and accidental death benefits.

The products have turned out to be very popular after an initial reluctance by the majority of agents to accept the compensation method, and as Graham has mentioned, there are other companies that are now trying this approach on some of their new product lines.

Return of Premium - basically it is a benefit that returns all premiums paid at maturity of the term, be it 20 years or at age 70, or at age 75, or on prior death. Premiums for this benefit are in the range of 30% of the basic premium for a 20 year term product.

Instant Issue - although this concept has been tried previously and not too successfully, there are adherents to this concept. In effect, an abbreviated application forms part of the actual policy which is completed by the agent, and if the limited number of underwriting questions are negative, the policy, which is good for 60 days, is left with the client. A copy of the application is sent to the head office to have a cursory underwriting check and an M.I.B. check done, and if negative, a validation endorsement is forwarded directly to the client. No further agent contact is required.

When tried previously, premium rates appeared too high when in comparison with competing products. With more competitive rates on this type of instant issue product, the plan should have success. I would see this type of product geared to property and casualty agents and based on a simple to understand product, perhaps family oriented and paying a levelized compensation.

Classification of Smokers - Two Canadian companies have marketed some of their products to smokers with the client being classified by the number of cigarettes smoked on a daily basis. Categories are 1 to 9, 10 to 19, 20 to 39 and 40 plus cigarettes per day. There has been a limited success in the marketing of this concept and some difficulty remains for the companies in finding whether or not they are attracting the light smoker market, or if all smokers are conveniently mistaking their consumption.

The rate increases range from approximately 60% for the 1 to 9 category over a non-smoker, 12% to 15% for a 10 to 19 smoker over a 1 to 9 smoker, and 60% to 65% for a 40 plus smoker over a 1 to 9 smoker.

Never Smoked Policies - The latest revolution to hit the Canadian market is never-smoked policies. If you have never smoked cigarettes, cigars, pipes, marijuana, and your client signs a declaration to that effect in his own handwriting - that's a declaration, not an answer to a question -

then you qualify as a never smoked client. The company indicates that improper completion of this declaration will result in voidance of a contract, not an adjustment in the rates to the proper classification. Rates for this type of product which is sold as a 10 year renewable and convertible term to 75 are very low, in fact, range 30% below the average non-smoker rate and at least 10% better than the nearest competition.

Statistically, the justification for such rates may be open for questioning. From a marketing point of view, it will be a popular move and to simplify it even more, if you smoke, you just double the never-smoked rate.

Maybe in this last product we are seeing another evolution in product pricing. Not so much actuarily priced, but marketing priced. Possibly, mortality is not the big cost in premiums anymore. No doubt the majority of business will not be in force when a claim occurs; it will have moved to another company. Companies may actually prefer to see business move after a minimum few years instead of pricing them as though they are going to stay in force forever.

The Concept of Total Financial Planning appears to be a strong trend; life insurance companies tying up with trust companies, with mutual fund companies and with brokerage companies.

It will no doubt be successful, but does the consumer really want one stop financial planning? Does the consumer want to buy his life insurance, group insurance, disability insurance, R.R.S.P., mutual fund, car insurance, homeowners' insurance, all from one individual, or one company? The answer is no doubt yes if that individual or company can guarantee that it be done simply and without risk and return as good an investment yield as he can do through various independent sources.

I do think that you will see the first successful integration will be with life products and general products. I feel the consumer is still interested in purchasing protection from an insurance company. Primarily, his life, the lives of his family members, his home and car. Investments will be considered, but not necessarily through an insurance company. Regulatory bodies, because of their usual bureaucratic red tape may not permit that it be handled on a simplified basis, and if not simplified for both consumer and agent, it will not sell.

An interesting phenomenon has been the linking of certain companies with other companies marketing a different line of product. Examples include a traditional line life company allowing its agents to market another company's term products, or another company's disability income products. The benefit is the company is able to maintain some control over its career agents and in some cases, a portion of the remuneration goes to help pay the first company's branch administration costs.

With the daily improvement in computer technology, no doubt mass merchandising will substantially increase. Consumers will be purchasing more and more insurance through direct mail after reviewing material through their own computers and cable T.V. This type of direct mail may before too long, be up to 10 to 15% of the market.

I would also look for some type of uniform guaranteed issue life product for smaller amounts, for example $10,000 or $15,000. It could be that this type of guaranteed issue life product will be forced on us by the government.

It appears that the days of one company marketing every type of life insurance product to the satisfaction of its agents and the consumer are over. The trend to specialty has arrived, and this has been the success of the smaller Canadian company in the past ten years. They have chosen a limited market, created innovative products to capture that market and reacted quickly to the changing consumer.

I am convinced that companies that strive for simplicity in their product design and show flexibility in meeting the desires of the consumer will do very well in the future.

MR. W. VERNON HALL: I am going to comment on non-traditional products in Canada as seen from the perspective of a large mutual company that is dedicated to maintaining a career agency sales force.

Our success has been based on our sales force and it has contributed to a track record we are very proud of. For example in 1983, we had:

1. the largest volume of individual life sales in Canada of any company;

2. the largest total annuity premium in Canada;

3. the lowest lapse rate in Canada by volume and by premium income among peer companies with a minimum of $4 billion in force.

Because we are proud of these facts, we want to keep it that way. We have publicly stated our commitment to our field force and in so doing, we realize we must provide our agents with most products that are available in the market place. This is not always an easy task as we all know it is impossible to be "all things to all people".

You will notice that I said we must provide most products. We will only provide products that we philosophically agree with.

By that I mean a product must be in the best interest of the client, the agent and the company. Clients must get their value for their money; agents must be adequately compensated and agents and the company must sell products that are soundly priced and will not come back to haunt us because of commitments we can't live up to in the future.

In 1978 we introduced a completely revised product line that had the underlying premise that as far as our individual products were concerned, insurance should be used for protection and annuities for savings. This was a corporate commitment and as a result we stopped selling high cash value plans. Our term and permanent plans were low cost and competitive.

In the period from 1978 to 1981, our individual product development was concentrated on our annuity products. The result is, we have a very competitive accumulation annuity product.

In this period, we made few changes to our insurance product line but several external factors were at work that were affecting it.

The first factor was increased competition and replacement activity. This was especially the case in the term market in the large metropolitan areas. As I mentioned earlier, we have the lowest lapse rate in Canada by volume and premium, and we have held this position for many years. We were not happy with the pressures the competitive situation was putting on our lapse rate.

The second factor affecting life insurance was inflation and the high interest rates inflation brought about. Inflation made consumers much more aware of a greater need for life insurance and the larger amounts of insurance made the consumer much more conscious of price. As well, higher interest rates made consumers more conscious of the return they were receiving on their money for plans that had values.

The third factor was increased consumer awareness. The consumer was made aware of options by the media. It was a period, at least it seemed to me, when the unusual life insurance product developments got the headlines in the financial press and were touted as the wave of the future. In particular, I think of Adjustable Single Premium Whole Life plans but the 1981 budget put an end to the popularity of these plans.

The fourth factor was especially significant: the emergence of additional risk classifications, most notably smoker/non-smoker rates. Smoker/non-smoker plans were offered by the smaller companies at first, but shortly after, were offered by several major companies.

The fifth factor that influenced product development in the 1978 to 81 period was advances in technology. It became much easier for companies to implement more complicated products. As well, agents could more easily prepare a detailed analysis of a client's needs. For example, we introduced an Inflation Adjusted Capital Needs Analysis that demonstrated the need for larger amounts of insurance than in the past. While an agent could have manually developed such a presentation in the past, we provided computerized methods of doing it.

The final factor, and I have already alluded to it, was the 1981 budget. The budget introduced proposals for taxing the cash values in life insurance. In the end, an exempt class of policy was defined. This exempt class permitted low cash value plans to accumulate tax free. We found that we were well positioned, relative to the tax legislation, because of our move beginning in 1978 to viewing life insurance for protection and not for savings.

Of these factors, the key ones that were putting pressures on our life insurance product line were competition and replacement activity, inflation and high interest rates, a more aware consumer, and smoker/non-smoker rates. We decided we needed to take a square one look at our life insurance products. In early 1981, we looked at all aspects of them. The weaknesses we determined we had in our product line were:

1. lack of term plans based on smoking habits;

2. lack of permanent plans based on smoking habits;

3. lack of a new money plan;

4. lack of a cash valueless permanent plan or a term for life plan.

We decided that our most urgent need was for smoker/non-smoker term plans and that we should make such plans available as soon as possible. We viewed smoker/non-smoker permanent plans to have the lowest priority.

During and prior to this time, Universal Life was "the" product in the U.S. I don't need to remind you of how much was being written about this product then. After assessing the alternatives open to us, we decided we could best solve the lack of a new money plan through Universal Life. Also we realized that Universal Life because of its flexibility, could be used to compete against a cash valueless permanent plan or a term for life plan. As a result, once we had our smoker/non-smoker term plans well underway, we concentrated our resources on developing Universal Life.

We made a conscious decision to develop Universal Life from scratch including all systems support. There were computer support packages available from the U.S. One or two Canadian companies elected this route. We didn't believe these packages fit what we wanted for our field force and what was needed in the Canadian marketplace.

We first started discussing a Universal Life plan design in mid-May 1981 and we had it available for sale with full computer support in mid-June 1982. The plan that was available in June 1982 was a basic Universal Life plan with a Waiver of Risk Charge Benefit. We have since made other benefits such as Disability Income and Guaranteed Insurability available. We did this deliberately. It enabled us to get our plan in the market place more quickly and agents could understand the plan without being confused by other benefits available.

Our plan stacks up well against the competition. In illustrations I have seen, we outperform the competition given the same assumptions. We have a $300 initial charge and then deduct daily risk charges from the reserve and add daily interest to the reserve. As far as commission is concerned, we pay higher commission than term, but lower than traditional permanent.

You will get varying opinions from Mutual Life people about the sales success of our Universal Life plan. To the end of August it represented 13.4% of our individual life sales by volume. It was never intended that Universal Life should be the main plan in our product portfolio.

In addition to providing us with a new money product, Universal Life also provides us with a plan that has complete disclosure to the consumer about the insurance being purchased. With the technology available and the fact we developed our own system, we have fully automated support for our Universal Life plan.

I view our sales results to be very respectable, especially when you consider that inflation and interest rates are not as high as when we first determined the need for this plan.

As I said we thought of Universal Life also being our answer to the cash valueless permanent or term for life plans that have become such a factor in the market place. In fact, this has become much more of an issue in Canada than it was 2 or 3 years ago when we were developing Universal Life. While Universal Life can be run much like a lifetime term plan, it often doesn't compete.

Not being an actuary, I can't give my learned opinion on the pricing of the lifetime term plans that are available. However, I do respect and trust the judgement of our actuaries and they have significant reservations about the soundness of the pricing of these plans.

As I understand it, the reason that lifetime term plans are cheaper than life plans is simply that the persisting policyholders get a sizeable advantage from all who terminate after the first few years. Lifetime term plans as a rule do not have cash values and for terminating plans, the value is used to reduce the cost to persisting policyholders. The larger the assumed withdrawal rate, the greater the gain to persisting policyholders, and the lower the premium for all. It seems to me, the lower the premium, the more likely it is that policyholders will keep their policies. Is a company selling a low premium lifetime term plan setting itself up for future losses? Studies we have done indicate that reasonably conservative withdrawal rates result in lifetime term plans that are only very slightly cheaper than a comparable plan that provides for cash values.

We are not a company that prices "loss leaders". We have always tried to have our products support themselves. We are not prepared to develop a lifetime term plan with the expectation there will be losses down the road.

We are concerned that the continued trend with lifetime term plans will bring about minimum non-forfeiture laws in Canada in the not too distant future.

Be that as it may, I can't deny that lifetime term plans are a factor in the market place today. It is only natural for a client to be interested in a minimum premium outlay for a maximum amount of insurance regardless of what some people's opinions may be about the validity of the plan.

We are grappling with the issue. We must have an answer for our agents. I do know we will have an answer, but right now I don't know what that answer will be.

A product that has seen little development in Canada is Variable Life. We introduced a product about 12 years ago that was similar to Variable Life. Our sales of the plan were very limited and as a result, we dropped it two years ago. We found our agents had little knowledge of equities and, therefore, were not confident enough to sell it. As well, Canadian consumers tend to be more cautious than American consumers and, therefore, not as willing to take an investment risk. This could well change in the future, especially if agents become more knowledgeable about equity products. However, I still do not see a rapid development of the Variable Life products in Canada.

From my experience, there has been much more demand recently for large volume term plans to cover a short term need. For example, a five year term plan that is non-renewable and non-convertible to cover a bank loan. I expect the demand for such products will grow.

Let's move away from specific products for a few minutes. As I mentioned, we have both smoker/non-smoker term and permanent plans. The move by the life insurance industry in Canada to smoker/non-smoker plans was not the result of a conscious effort to have additional risk classes. Instead, it was brought about by competition. Smaller companies decided to go after the non-smoker market with very competitive rates; that's what free enterprise is all about. Most other companies, big and small, followed.

However, it appears that the smoker/non-smoker classification system is not working well. Some companies and agents are selling non-smoker plans to smokers with the intention of adjusting the claim, that is, reducing the death benefit, if it can be proved the person smoked at the time of the application. I suspect this will be difficult to prove. If such a case were taken to court, it seems likely the full original death benefit might be awarded to the plaintiff. If this happens, the whole smoker/non-smoker risk classification system would be undermined and it could cause a movement back to blended rates.

I believe alternate risk classifications will be the significant issue facing our industry over the next several years. A few companies are making efforts at defining other risk classifications, for example, London Life with their Lifestyle Term. But even these approaches aren't foolproof because much of the information isn't verifiable.

I'm not sure where we will end up on this issue, but there are several attributes that we would want a sound risk classification system to have.

The data must be verifiable. It is important to know that the facts used in the underwriting decision were correct.

The classification system must be simple for the agent to use at point of sale. This does not preclude a complicated system, but it would have to be computer supported at the point of sale.

The system must be socially defensible. It should not violate the rights of individuals.

A sound classification system must have relatively stable classes. An individual's classification shouldn't change easily so that he or she would want to be continually moving from one class to another.

Finally, a risk classification system must be cost effective.

Having said that, I realize we can't establish a risk classification system that meets these criteria but can't be sold because none of our competition uses it. Such a system could result in us only selling plans in situations where our rates are hot but our agents would have uncompetitive rates in many other situations. This would undermine our commitment to the career agency system. Even though I believe risk classification is a significant future issue, maybe it can't be resolved.

I haven't mentioned remuneration, but it does have a significant effect on product design and pricing, especially when you are dealing with a career agency sales force. We want to provide our agents with a superior remuneration package. I see a couple of trends developing in Canada. Recently, there has been a movement in the large case market to charging a high front-end fee for a plan. I think this is a reasonable approach because often there is not a great deal of after sale service in these cases. The client or frequently the client's advisor is simply phoning around for the best rate. I do, however, have concerns about the agent being able to select the fee for the plan. Maybe I remember too much my time as an agent, but I see it as being nothing less than rebating if the agent has the option of determining different amounts of commission he will receive for selling identical plans to two different people.

I also think it is possible that we will see level commissions in the foreseeable future. I believe it wouldn't be a popular move with a lot of agents, but it would slow down the replacement problem that exists and the continual rolling of business from one company to another. Companies may simply be forced to pay level commission because of the losses they have to absorb from early termination of heaped commission business.

In summary, I believe the development of non-traditional products will over the long term cause the best plans to be developed for the consumer. I do have some reservations about some of the steps being taken over the short term. I think we must always keep the consumer in mind. From my perspective with a career agency company, I see the development of non-traditional life insurance products in Canada as being an evolutionary process. Product development is no longer a one-shot proposition. We must continually be providing our agents with competitive products. The evolutionary process has not been slow in recent years and I believe it will progress at an even more rapid pace in the future.

MR. LAURIE WEISSBROT: I have a client corporation in the United States that's putting in a Universal Life plan for its up-scale employees, and they have about 800 employees in Canada and Universal Life is what the American employees want, but that's not going to jangle with Canadians too much. What would be the top of consumer product? What would be really a heavy product now in the eyes of the insurance consumer public in Canada to satisfy their needs?

MR. HOWES: Obviously, the first question to answer that would be you are talking about up-scale employees; you are talking about larger amounts of insurance and you are talking about permanent insurance needs as opposed to temporary, with savings elements?

MR. WEISSBROT: With the U.S. Group we are talking about Universal Life with variable policy loan interest rate so that they can get tax leveraging out of it, highly paid people; high insurance amounts; the product is going to be lower in cost because it's already marketed, probably without commissions.

MR. HALL: It doesn't surprise me that Universal Life is not a hot button with the Canadian people you are dealing with because Universal Life has not enjoyed the publicity in Canada that it did have in the States, and not as many companies have come into it. You are talking though about a permanent plan?

MR. WEISSBROT: Aren't there some taxes or ramifications in Canada that make Universal Life a lot less attractive?

MR. HALL: There is a defined exempt limit on policies. Now, Universal Life can have values in it up to the defined exempt limit. There may not be the same tax advantages that there are in the U.S. but I am not familiar with the U.S. taxation situation. Those same exempt limits would apply to our traditional permanent plan, too.

MR. HOWES: My opinion is there probably isn't a hot product because there is such a lack of uniformity in Canada in terms of a particular type of product or design. Universal Life is being sold and there is a lot of interest in it. I think at last count, there were six companies offering it and at least several more developing it. Of those six, at least three are what may be termed large companies and maybe another three in the medium sized range.

In terms of exempt policies and the difficulty, I believe that some companies tackle that problem by putting in a clause that restricts the maximum cash value growth, or other restriction to prevent the policy from becoming non-exempt. That solves some problems in an administrative point of view and also potential problems with the customer in moving into the non-exempt class.

My impression was also that the Canadian tax law is designed to prevent too high a savings rate within a life insurance policy; that is, buying it almost purely for investment return due to tax exempt status. Under normal sales, although there is premium flexibility in true Universal Life, people tend to stop or pay less frequently or less highly than might have been planned at the point of sale rather than more highly, so I don't think you will run into that many problems with the taxation status.

In terms of alternatives to Universal Life as the hot product, that always depends on what agent you talk to. There are a number of companies that have had great success with the new money life type of policies. These are typically non-par, adjustable from time to time (5 years is typical) based on current interest rates or trends in interest rates since the last adjustment.

There has also been continued emphasis on the par line in terms of making them hotter and hotter, working with enhancements, paid-up additions, new money paid-up additions and vanishing premium concepts. Other than that, I am sure there are a number of companies or agents who would still sell hot term rates and invest the difference.

MR. PHIL ELAM: I believe Mr. Hall was the one that said he wouldn't be surprised in the future if there is pressure in Canada for non-forfeiture requirements. Could you comment on the regulatory concerns and the possible ways that these concerns could be addressed without requiring cash values.

MR. HOWES: He was remarking on a point that you made that there might be possible regulatory concerns in connection with low cash value or non-cash value products and the possible introduction of minimum forfeiture. I think he wished elaboration on what form that concern might take and how it might come about.

MR. HALL: I can't really answer that in detail, except, you have almost summarized what I would say; we do have very serious concerns as a company about it and we feel that the regulatory authorities will view cash valueless plans as being detrimental to the consumer and therefore we could see minimum non-forfeiture laws as exist in the U.S., but what would actually trigger that I am not sure.

MR. HOWES: One can only speculate about what they might do. There have been several instances of individuals from the superintendent's office commenting on that topic in public, such as at actuarial meetings, including the superintendent himself. One individual expressed some concerns about the possibility of products with no cash values, recalling in that persons mind the Armstrong investigation and situation a number of years ago that brought about minimum non-forfeiture in the first place. The more recent comments have maybe even lessened that concern if anything in that basically their authority and mandate is to supervise the solvency of companies and ensure that the valuation of these types of products are properly done. I think that would and should be their primary concern. There certainly has been nothing other than those occasional references to that area that would cause anyone to believe that non-forfeiture laws are really imminent. A number of companies that have introduced these products, I believe, have mentioned it informally to the Department, so I think they should be aware of product trends. Also the response that a number of companies have given if they are questioned on it by others, is that these types of products are generally sold to a more sophisticated consumer in larger amounts, and are often sold with an alternative of products that do have cash values and therefore the consumer has the option to make the informed choice.

MR. STEVE PRINCE: I had a question for Mr. Hall. You seemed critical that allowing the agents the choice of the set-up fee and therefore his commission was a form of rebating, and felt that this was wrong. I have never heard, a good argument for what's wrong with rebating in the sense that the agent always has the choice as to what he is going to pay because he can sell a term plan or a whole life plan, and if he has a choice of what's basically the same product with two commission levels, I don't see why this is any different.

MR. HALL: Well, if they have the choice between term and permanent, they are two different plans with different features. It's different if the the agent picks a fee based on his opinion of what service he has put into it for the same plan. It seems to me if there are two people there and one doesn't want to pay as high a premium, he is going to pick the lower fee and that doesn't seem right. Rebating is against the law. I said that maybe my thoughts are based on my feelings from being an agent, but it is against all the rules.

MR. PRINCE: But this happens in other business all the time, and I don't see why.

MR. HALL: Perhaps it does in other businesses, but are we the same as other businesses?

MR. PRINCE: That would be your only argument?

MR. HALL: I don't think it is equitable to the consumer. That's where I am really coming from. If the consumer in two equal situations, if one knows about it and one doesn't, one pays the higher amount and one pays the lower amount.

MR. PRINCE: The only comment I am making is that many times the consumer doesn't know that there are cheap term products. The effect is the same.

MR. MARK FOWLER: Before I get to my question, which will be for Mr. McArter, I would just like to perhaps amplify somewhat on what Mr. Howes has reported to the people here about the role of the Federal Department of Insurance, with respect to premiums and policy benefits. Because of the historical evolution of our country, matters involving determination of premiums charged to the public, and the inclusion of various clauses and benefits etc. in contracts have fallen to the provinces of Canada. So as a result there is limited, if any scope at all, for federal action in that particular area. One possible way of manipulating, if you will, the evolution of these kinds of products in Canada, would be for the Department to embark on perhaps some arbitrary or unusual methods of requiring reserves, but that's probably something that would be dealt with more appropriately at another section.

Mr. McArter, I would like to know on the basis of your experience in seeing these new products marketed in various small companies, what do you observe in so far as the procedure going on in a company when it entertains the notion of underwriting a new product. I try to visualize myself perhaps as being a non-actuary, but president of a small company, and someone, perhaps someone such as yourself, comes to me with a marketing venture, and you may come armed with all kinds of reports and studies, and whatnot. Would you say that one of those ingredients or reports would be something from a qualified actuary, which indicates quite clearly what the assumptions are, what the probabilities are, what the premium rates are, how they were derived, and something certifying to me as the president, that these products are not likely to result in new problems for me sometime later?

MR. McARTER: I would suggest that an actuary always has some involvement in assessing the rates. I would say that perhaps in the past, some companies have come out with products that have not been priced, perhaps as well as they could have been, but I would think generally now, as a president, I would expect to receive from my marketing people justification that this type of product is going to sell, and from my actuary, that selling the product at the rates that are set is not going to cause too great a strain on my company, either now, or fifteen or twenty years, or whenever down the road. I would think that any president that did not take that into consideration, perhaps should not be in his position.

MR. HOWES: One of the points that I had made when Jim made his remarks was that he referred to an evolution in product pricing where products are not so much actuarially priced, but marketing priced. I am wondering if Graham as an actuary, or Jim would care to elaborate on that any further.

MR. DIXON: I think that some companies might be criticized on the way they price some products, that's going to happen in any industry. Any product that is going to be priced by an actuary, will take into consideration all the elements that I mentioned, and probably no two will come up with the same solution to the problem. I don't really know what you mean by market priced. Is it just take another company's rates and subtract a dollar? Is that the method you are suggesting?

MR. McARTER: Use one example that I gave in my speech, and that was never-smoked products. To get the smoker's rate you just double it. Now, to me, I am not an actuary, but that seems like a rather simplified formula to use, and that's what I meant - is it marketing oriented in the pricing, rather than actuarily? Perhaps someone from one of those companies that had such a product would like to comment on how actuarily sound that is. To me it seems only marketing.

MR. DIXON: I wouldn't mind commenting on it. I think we are in an era where the difference between smoking and non-smoking premium rates is still under a lot of investigation. I don't think we really know what happens at a lot of different ages, and the differences in the two rates. We are in the business of taking risks, and I think we take not only risks on peoples' lives, but we take some risks on our assumptions, too, just as any other business would take a risk on that business' assumptions. We are taking the risk that overall non-smoker mortality is going to be, say, half of the smoker mortality. I don't think that's an unreasonable assumption. You can look at a lot of statistics and mull it over and come up with what you think is going to be reasonable. Sometimes, you are going to be wrong, but as long as you made a reasonable assumption, based on what you had, I don't really see that there is going to be a problem. You can never be sure that, for instance, a lapse rate is going to hold the way that you thought it would when you priced. The bottom may fall out of your product portfolio and you lose almost everything. A number of companies have gone through that recently. It is something that happens and we have to react to it as best we can.

MR. McARTER: In your pricing, do you feel that you are really pricing for a contract to stay in force for a long period of time, 20 years or more, or are you pricing for that type of contract to stay in force for three to four years, which seems to be the trend on term insurance?

MR. DIXON: I think that most products that are priced now, especially term products, are priced for very short periods of time. If they stay in force longer, then a company is going to make more profits than they thought they would have done. There are situations where it pays the company to have a policy lapse because the profit situation is best at one point at time and that might be 5 years in rather than 10 or 20 years in. For permanent products, I think the break even pricing would be probably be 15, 20, sometimes even 30 years. When I price a product, I look at what can happen if it lapses in 15 years on average, or if it lapses in 25 years and see what the worst scenario is, and try and guard against the worst scenario. You have to be competitive, too, so sometimes you have to assign probability to those things.

MR. HOWES: My own comment, as the only other actuary at the front, is that almost always a product's rates when finally produced, have been massaged from a marketing point of view, if not outright created from that point of view in the first place, but that doesn't mean that actuarial thought hasn't gone into the basis of them or that the product as a whole has not been proved to some actuary's satisfaction to be profitable. This whole point of lower and lower rates and shorter periods of expected life time of products, I think, is a point of concern. I am curious as to how Jim or Graham would react to that concern. Jim stated that the initial thrust in the brokerage market was normal 5 year renewable term and then re-entry five year term with lower preferred rates, and then non-smokers term and now most recently, the prospect of never-smoked term. If each one of these improvements is going to cause mass roll-over of business and yet more replacements, that's one issue. Another issue is that it's lowering the rate per thousand yet again another notch, which puts that much more pressure on the company's premium income, for what they are selling and producing, and that in turn places that much more pressure on the agent's own livelihood, his commissioned income because it is based on a smaller premium dollar. We have seen in the past couple of years, a few small companies being amalgamated, merged, taken over. We hear about the possibility of more, and I am curious as to Jim who has worked with a few of the small companies and Graham, maybe more with the mid-sized companies, aren't you concerned yet again, how can these small companies survive if their premiums are being forced down this way and the brokers too, how can they survive?

MR. McARTER: I don't like the outlook for smaller Canadian companies because unfortunately, I feel what is going to happen to the smaller Canadian company is one of two things. It is probably going to be taken over by a larger company. I think the larger companies will put tremendous pressure on the regulatory bodies to limit the amount of business that the smaller companies can write. I also think that the smaller companies have been able to write all the business that they have been writing over the past few years because of the tremendous support of reinsurance companies, and I think there has been a change in philosophy by some reinsurers who are beginning to look at and question their motives of being marketing oriented as opposed to profit oriented. So, I see pressure coming on the small companies. There has been one small company recently acquired by a larger company, and I would see that as a trend. As I indicated, there aren't that many smaller Canadian companies and I would estimate perhaps by the end of this decade, that you will see probably half that number, the other half being swallowed up by the larger companies.

As far as the smaller company goes, I would suggest that perhaps if they are going to continue to survive by writing low cost business, that they are going to do it more on a direct marketing basis. I don't feel that they can continue to lower rates and continue to take it out of the agent's commission, so I would see more of a trend on the smaller company's part to direct mail marketing.

Another subject that has me a little curious and that is the selection of risk process that companies use. I think that one of the savings that could be looked at by companies, large and small, is the savings in having a little less conservative selection of risk process. I feel that a lot of companies are still underwriting risks the way they were 10 years ago, underwriting them on the basis of mortality and not on the basis that a lot of this business is just not going to stay in force for that long a period of time. I think you have underwriting departments that are ordering this type of evidence and that type of evidence and not really looking at the cost of it. I think the savings that could be found because of some of the elimination of this underwriting criteria could no doubt go into more competitively priced products. I don't know if anybody has any quarrel with that scenario, but I think it's a valid point.

MR. IAN MCINTOSH: Jim McArter, as an old underwriter, has just shocked me into getting up here. He should know that although a lot of this business won't be around, the business that you save money on your underwriting and accepted the wrong risk, that will still be around 10, 15, or 20 years from now.

MR. McARTER: You see underwriters do change after all, and I guess underwriters will always be around, I agree, but I sometimes think that underwriters have not followed the trend of the business today. They are still, I feel, underwriting a little too conservatively. We have raised non-medical limits and raised inspection limits, and so forth, but I still think there could be a lot of areas in the underwriting department that could save some money, which, in turn, could be passed along to reduce the premiums.

MR. DIXON: I think that the biggest cost right now that goes into most insurance products is compensation of agents, so if anyone is going to really push the price down significantly, apart from chipping away at the edges, which I think is what Jim is talking about, it has to be done by lowering the overall compensation package that agents get. That's going to be very difficult to do, and it is going to be particularly difficult for small companies to do. So, if you can't force prices down, you have to figure out other ways to get a good foothold in the market place, and that's going to be with service. I think we are going to see a lot more support material, a lot more financial analysis attached to the selling of life insurance. Life insurance agents won't just be able to go in and give their little spiel and ask the guy to sign on the dotted line. They are going to have to go through what the guy is going to do with his money for the next 20 years, and what his objectives are, and do a capital needs analysis, which is what they have been doing for the last 20 years. But it is going to be an essential and it's going to be something that people listen to and you have to do in a understandable manner. So, I don't know if I answered that question, or if I walked all around it, but, if it's going to be price that determines it, I think it is going to be compensation that goes down and we will move to level commissions over a period of time. If it's not price, and I really don't think it will be only price, it will be in terms of giving more support, more explanation and more packaging with other financial goods. That will be the way that we will be able to attract more clients.

MR. MCINTOSH: I agree with Graham very much, that compensation is one of the large factors in your premium rates and there have been allusions today by Graham and by others about moving to level commissions. Agents, of course, don't like that very much, and agents have been making a lot of money in the last few years by rewriting business on a high-low basis. When the commission gets low, they go out, and then the companies have been making it pretty easy for them with bringing out new products at lower rates so they have a good reason for rewriting it. There is a lot of talk about the companies going to level commissions, but I don't see anybody actually doing it. A couple of companies have announced that they have level commissions, but they aren't really level commissions because at least one of them anyway, has a very large policy fee in the first year on which they pay a level percentage, and the commission actually turns out to be high-low.

In the group area, the tradition has been to go to level commissions, but that turns out not to be very level either because the companies pay a bonus on top of the level commission in the first year. So, I really wonder whether it is possible. We would all like to move to level commissions. Is it possible?

MR. DIXON: I agree with you. It's not going to be very easy to get to level commisisons. There has been a lot of talk about replacment problems and level commissions as a method of solving it. I think it's a question of comfort level. We have a certain amount of discomfort with replacements right now. I think in the next five or ten years some companies are going to go bankrupt. Some prominent insurance companies will lose a lot of money and then the comfort level will go down, and then someone will do something about it. But, I don't think we, as an industry, move very quickly and I think it is going to take a good kick before we will actually do anything. At that point, we will see a lot of alternatives looked at, and one of them will be level commissions, and there will have to be some sweeteners in there. We won't have as many people selling life insurance as we have now. We will probably have perhaps 25% of the number of people selling and those people will have to be very good. They will have to be knowledgeable. They will have to work probably a lot harder to sell what they are selling now. I think there will be agencies set up for doing financial needs and tax planning, and life insurance will be sold after those seminars, so it will be sold to a lot of people at a time. People will pay a fee for service, and the agent will be paid for providing that information up front, and will be paid by the companies on an on-going basis for business as it is received. It's not going to happen in the next two years. It might begin to happen after five years, but I am pretty sure it is going to be there after ten.

MR. McARTER: If an agent sells a product on a levelized compensation basis, we will say its a term to 65 or a term to 75, and the level is 15 or 20%, what justification does the company have paying an agent 15 or 20% after say the second year?

MR. McINTOSH: I think it's part of the initial compensation that we hold back to make sure the policy persists.

MR. McARTER: Yes, but when people talk levelized compensation, they are talking about compensation for a long period of time and I sometimes wonder if it is really warranted, as opposed to the approach of the company that's doing the business term concept of applying a consulting fee. The agent assigns his compensation, which you know could be one times the first year premium or two times. Is that not a more logical way to do it, and then provide a small service fee of 2 or 3% on an ongoing basis. I really fail to see where an agent warrants a 15 or 20% after the first couple of years.

MR. McINTOSH: I agree with you that basically up front is where the agent has done the work and where the agent ought to get paid, but the problem is that if the business doesn't persist, the company can't afford to pay it. What we would like to do is pay a large up front commission but charge it back over the future policy lapses, but who do you charge it back to? You can't find them. The alternative certainly is for the company or the agent to set an up front cost in addition to the regular risk premium and some companies have done that and they have been very successful with it. I think we may see more of that.

MR. McARTER: I think you will and I think everybody is talking about level compensation, but I don't really think it is the answer and that's maybe the reason why it's never been successful thus far. Does anybody else have any comments on levelized compensation? Is there any experience in the U.S. on it?

MR. ANDREW BEAMISH: In hopes of encouraging others to join us, I will tell you that we pay level 15% on our 5 Y RCT . We don't sell very much but I don't think that is because of the commission.

I have a couple of other comments. One is on this question of rebating. I don't think it is really a moral question so much as a severely practical one. Letting an agent set his own rate of compensation and to drop it in face of competition is going to leave him with a lower and lower reward. Once he will make an additional sale, but as time goes on, there are more and more agents who reach the stage where they can adjust the cost to meet competition, they will find that they are getting less and less reward, and I think that's really the reason why we don't like rebating.

I have a question for Vern Hall. You found with the product which you had available for a while, that agents were not selling it very much and perhaps this was because agents themselves weren't very comfortable with an equity based product. Is this perhaps one of the reasons why your company is now offering unit funds?

MR. HALL: We are not offering investment funds at this point in time. We have issued a press release saying we will be offering them early in '85, and that's the extent to which I can comment on that. I don't see that our life equity plan which was the name of our variable life plan has any tie in with that decision at all. It is a separate issue.

MR. BOB HOWARD: I don't want to comment on our life equity plan. It had a flaw in design anyhow. However, since we are talking about non-traditional products, I would like to take three shots at a non-traditional product which is I think is a very bad one to have in the market place and that's term to 100.

First, it is an inequitable product. The policyholders don't get what they pay for when they buy this plan. There is an enormous discontinuity between the price paid to the policyholder who persists and the one who withdraws. Indeed, of those who decide to withdraw, many of them will withdraw thinking that they have no value in this product, and in many cases they were told that's what the case was. They took the company at it's word and away went the value when their needs changed, but in fact, anytime anyone has had a policy around for many years, and is no longer insurable, that policy has value. It may not be a guaranteed cash value but it does have value to somebody particularly to a lottery buying country like Canada. And there's going to be somebody who will give a cash value for that policy.

Secondly, I don't like term to 100 because it is inflexible. It's the least flexible plan in the market today. People buy it thinking that their circumstances or insurance needs are not going to change, and with those who are the farseeing among us and see maybe six months or a year into the future, sure there are't any changes in circumstances. But, I will guarantee you that 99% of the people who buy that plan will have major changes in their insurance needs in the future, and with no value in the policy, there is nowhere they can go. They are stuck with it, and if it comes to the point of not needing insurance, then they have to look for the auction somewhere.

Thirdly, it's an unsound plan, at least it is unsound if you want to get the price down. If you want to assume a rate of withdrawal in the future, you would take into account the fact that there is value built up and that there is probably somebody around who will give you the money for it, then we are not talking about a very big decrease in the cost of it. But supposing we have assumed in the future fairly high rates of withdrawal. In the past perhaps we have assumed bad rates of withdrawal in the ultimate years in some plans, such as renewable term for instance, and perhaps permanent plans with guaranteed cash values. But, on those two plans, the amount of risk of withdrawal is not very large. With term to 100, it can be astronomical, and the withdrawal assumption is critical. We have got to make an assumption which has at least some small margin of conservatism for the future, and we are going to have the Department of Insurance perhaps on us to make sure that we have adequate reserves, which may mean an ultimate withdrawal rate of 1 or 2 percent, perhaps as high as 3%, but could it possibly be higher than that?

The deficiency reserve that some of these small companies are going to be facing could be very large, and might very well impair their solvency. We are very proud in Canada to say that no policyholder has every failed to have the benefits guaranteed in the contract paid to him, and there have been instances where the company has gotten in trouble and in some cases, the Superintendent of Insurance has actually stepped in and gone to one of the majors and said 'would you buy out such and so small company because they are in trouble. They are about to go under' and it's been done. I'm sure many of us here work for companies that have actually bought other companies that went into trouble, but if the majority of the liabilities are on this term to 100, without sufficient conservatism in the reserves, who is going to step in and take them over, if they get into trouble? I couldn't recommend it to my company. Could any of you recommend it to your companies? I think it's unsound, and there is a trap in here that our profession and the life insurance industry as a whole, I am afraid, is going to face. It may be that those few companies that sell the plan will go bust, but the black eye goes to each of us and we are going to bear that for a long time.

MR. HOWES: Further to a couple of those comments, there is the observation that there is the very strong likelihood of a protection scheme for life insurance buyers that will involve the whole life insurance industry. It has been in the press several times recently in Canada. Although the industry in an internal poll couldn't reach any decision about how it should be done or if it should be done, it is now looking much more likely it will be forced to do it, and the only question is how and in what form? Will it be run by the industry or run by the Government? Will it be assessments to cover insolvencies done before or after, that is, postassessment or preassessment, and I think those are the only types of choices that really remain. If this type of products could greatly raise the risk for the industry as a whole, then I am sure there will be heightened concern in the industry.

I think there is another danger here too, and it is not just a financial one in terms of potential risks of lapse rates being lower than projected in some of the low cash value policies. That goes back to one of the advantages I stated at the very beginning. In Canada we have a type of flexibility in our valuations - it's also a responsibility and not just a flexibility - that allows us to respond to products that key on low cash values or no cash values, and on other contingencies that may be considered to be part of the policy. But if we as a group of actuaries don't carry out our responsibilities adequately, in properly assessing these risks, and it's found that companies introducing term to 100 type of products have failed to take proper measures, then I think it would not be far beyond that when we would lose a lot of our flexibility and would return much more to a rigid system that would be a lot more painful for all of us to work with.

MR. CHRIS McELVAINE: I think there have been a lot of comments made today about solvency, and the assumptions in pricing, and I think what has not been said, or has been overlooked, is the independence of the valuation actuary versus the pricing actuary - in theory, at any rate. Certainly the responsibility for the solvency of the company is on the back of the valuation actuary in many respects; and the assumptions that he will make in setting aside the valuation liabilities may or may not be similar or identical to those used by the pricing actuary in pricing the product. Nevertheless, I think it was Mr. McArter who pointed out earlier in his remarks that there is many a generic term to 100. There is term to 100 which endows and there are terms to 100 which are whole life contracts and there is term to 100 which terminates at age 100, and I think we should be careful. I fully agree with the points that are being made by Mr. Howard, but I think that we should be careful in ensuring that we do identify which products are involved. The lack of a cash value does not necessarily imply all of the dire disaster which has been referred to. There can be plans that have paid-up values. In fact, I think what concerns me a little more than some of the products that have been referred to today are the tontine kind of products which tend to have no non-forfeiture values whatsoever until it has a very large value suddenly made available at a singular point in time. Now this to my mind is much more of a tontine kind of problem which seems to create inequities and great difficulties in trying to determine what the actual termination rate would be. I think in my mind it is a little more visible problem than the true term to 100. Although the problem may become more evident in the terms that Mr. Dixon referred to, maybe we have to have a company failure before this thing really strikes home. But, maybe it is those products that have the large cash values that endow at a certain point that may become more evident and may become a more visible problem earlier than the true term to 100.

MR. DIXON: I agree with a lot of what has been said. We do live in a free enterprise society. Most businesses take risks, even banks take risks. They take very bad risks sometimes; a lot of our money is now tied up in South America. I think it's not unreasonable that the life insurance industry should also take risks. I think it is a little presumptuous of us to keep saying things like nobody has ever lost a dollar through a life insurance failure in Canada. I don't think we can be competitive and continue to make statements like this. We are going to have some failures. Those failures represent the fact that we are in a free enterprise society and we are competitive. Does anyone want to respond to that, or as an industry, can we only take the one conservative position?

MR. McELVAINE: If I may, I would just like to respond to that from the position of the mutual company or a stock company that is writing both par and non-par insurance. I think you have to segregate that out. The pricing actuary and the valuation actuary must be quite clear as to whether the risk he is taking is that of a shareholder or whether the risk he is taking is that of other participating policyholder.

MR. DIXON: A good point. Do you really think there is going to be a lot participating insurance in force in ten years time?

MR. McELVAINE: I can't answer that question directly, but I think when some of these non-traditional products start coming under the guise of a participating product, I think we are basically transferring that risk from a shareholder to a participating policyholder.

MR. DIXON: That's true.

I really don't see the term to 100 product is that bad for our industry. I think it is a reflection that we are willing to try some new ideas and that we are willing to lower premium rates. The consumer must be made aware that he is not buying a whole life policy, he is not buying the same animal as before, but I really think there is a use for a term product. Not everyone wants cash values but a lot of people although they don't want cash values, they want coverage until they die. Term to 100 is a way of solving that problem and I agree that there are certain varieties of it that are not very sound and which we should as an industry probably try to cut down on, but I don't think the whole concept in term to 100 is bad. I think it is difficult, but it is something that we have to rise to.

MR. BOB TIESSEN: I would like to go back to the problem of companies selling plans where the experience might not match the pricing assumptions and companies becoming insolvent and the risk of guarantee funds being set up by the government, things of this nature. I think Bob Howard alluded to the fact that in the past large companies were generally willing to pick up the slack when small companies had gone under because the circumstances might often have been unforeseen, and in situations where companies selling the newer non-traditional products go bankrupt, they might be less willing to do that, figuring that the circumstances could have been foreseen. I think that a similar situation is present in the U.S. banking circles right now where a lot of U.S. banks are going under because of the deregulation and the greater risks that some banks are taking, and that other U.S. banks are becoming less willing to bail them out like they have in the past, and obviously the risk of similar circumstances happening in the insurance industry is also present. I think that one of the things that might well result from that is that people will figure that although noone has ever not gotten a guaranteed benefit out of Canadian insurance companies, that that situation might not hold for all companies in the future. Whether this poor image can be restricted to only some companies, or whether it will spread to the entire industry, I think is a problem that could be quite major in the future unless the industry takes a stand on some of these issues.