RECORD OF SOCIETY OF ACTUARIES
1986 VOL. 12 NO. 3

COMPETITION AND PRODUCT CONSIDERATIONS IN A REGULATORY ENVIRONMENT

Moderator:	LARRY D. BABER
Panelists:	GARY L. EISENBARTH
	BURNETT HALSTEAD
	NORMAN E. HILL
Recorder:	SANDRA W. ZDAN

- This session will provide an overview of the constraints and opportunities which result from the regulatory controls of the National Association of Insurance Commissioners (NAIC), Securities Exchange Commission (SEC), Internal Revenue Service (IRS) and other local taxing bodies.

  - Product constraints caused by the SEC regulations
  - How the NAIC affects insurance companies
  - Impact of local municipal taxing bodies
  - Are there unique marketing opportunities in the current regulatory environment?
  - Role of computers in the regulation of insurance
  - Solvency/surplus concerns

MR. LARRY D. BABER: Our panelists will discuss all of the six topics listed for this session. Burnett Halstead is actuary with Federal Kemper Life Insurance Company. Norm Hill, Executive VP and Chief Actuary for Associated Madison Companies, has a public accounting background with work in statutory, GAAP and tax filings. Gary Eisenbarth is with Security Benefit Life Insurance Company, a Senior Vice President of Marketing and Product Development.

Regulation by the NAIC (indirectly through the state insurance departments), the Securities and Exchange Commission, the Internal Revenue Service (somewhat indirectly) and other regulatory bodies has been with us for many years. From my perspective as a life insurance actuary prior to interest sensitive products, primary regulatory concern for traditional insurance products was with policy approval in the fifty or so possible jurisdictions in which a company could be licensed. There were also concerns with interest adjusted cost indices and some disclosure requirements promulgated by the states. Life insurance minimum reserves and values were pretty well defined by the 1958 Standard Valuation and Nonforfeiture Laws.

Since 1980 the interest sensitive products have come on the scene; the 1980 amendments were promulgated; smoker/nonsmoker products became vogue; the tax law has changed twice with a third change pending; and valuation actuary discussion has begun. Throw in variable life, variable universal life, and various annuity products and the task of developing competitive products today has become a juggling act, keeping several balls in the air at one time. This discussion will provide you with an overview of constraints and opportunities which result from current regulatory controls.

MR. BURNETT HALSTEAD: My perspective on SEC constraints is from a company that doesn't want to sell variable products. I'm not going to get into any variable subjects at all. I'll give you a bit of history and then comment briefly on the adoptive release that the SEC just put out. Historically, Section 3(a)(8) of the 1933 Act exempts from registration, any insurance endowment or annuity contracts issued by insurance companies subject to state insurance department supervision. This exemption, though, has been subject to judicial interpretations as well as some SEC interpretive releases.

The judicial interpretations have stressed two factors: (1) there must be a significant investment risk taken by the insurer, and (2) the products must not be marketed as investments.

SEC Release No. 33-6051 was published in April 1979 after the SEC became concerned about what was happening with single premium deferred annuities. This focused on general account deferred annuities and had two basic requirements: (1) the insurer must take a significant investment risk, and (2) the insurer must also have a meaningful mortality risk.

The SEC then published for comment in November 1984, Rule 151 which establishes a safe harbor for qualifying annuity contracts. Three basic requirements for the safe harbor are: (1) the contract must be a contract of insurance, (2) the insurer must assume an investment risk, and (3) the products must not be marketed primarily as investments.

The investment risk assumed must satisfy three conditions. (1) The value of the contract must not vary according to the investment experience of a separate account. (2) The insurer must provide guaranteed principal and a minimum specified interest rate for the life of the contract. (3) Discretionary interest must not be modified more frequently than once a year.

Rule 151 was finally adopted on May 20, 1986. At the same time the SEC adopted Rule 151, it withdrew Release No. 33-6051. I have 10 comments with respect to Rule 151 adoptive release:

1. The release eliminated 6051's "meaningful mortality risk," but the mortality risk is still relevant outside the safe harbor.

2. A "bail out" or "opt out" provision (as they call it) doesn't by itself make the marketed product an investment.

3. An even-handed approach to guarantee of interest and principal for front-end and back-end load contracts was provided.

4. They applied a "rule of reason" to the term "year" with respect to the one year guarantee on discretionary interest. A "year" is allowed to be a calendar year, policy year, or even a stub year.

5. The SEC will permit excess interest above the discretionary rate under the safe harbor, provided the excess interest is in itself guaranteed for another year.

6. There would be no "three tier" contracts.

7. "The specified rate of interest to be credited" means the minimum rate under the relevant nonforfeiture law in the jurisdiction the policy is issued.

8. The principles applicable to annuities are also applicable to life insurance which means that 151 is applicable to things like Universal Life.

9. Market value adjusted products cannot rely on the safe harbor.

10. Deposit fund riders have to be tested separately from policies to which they are attached.

The only practical thing we've done as a result of all this is that we had to develop an amendment for our Universal Life policy because our discretionary rate of interest was not guaranteed for a year after the first year.

MR. GARY EISENBARTH: I might amplify Burnie's comments about Rule 151. This is from the perspective of a company that sells variable products. I haven't studied extensively what it would mean if your products were deemed to be securities, but I assume it means that your general account has to be registered with the SEC.

We have had difficulty being sure we comply with this rule. We sell variable annuities, for example, that offer both an equity and a fixed option. Also, in the case of products like single premium deferred annuities, the problems are related to the way that those products are distributed.

I want to talk just a couple of minutes about SEC Rule 6e-(3)T. This rule provides exemptive relief from certain provisions of the Investment Company Act of 1940. Very simply, the rule looks at (1) the separate account assets that are derived from the sale of flexible premium variable life insurance, and (2) certain exemptive provisions for custodianship of those assets, sales load, capital requirements and several others.

The most important provisions, I believe, relate to sales load limitations. Sales load cannot exceed 9% of the sum of guideline annual premiums to the lesser of 20 years or life expectancy calculated according to the 1980 CSO. However, a sales load of as much as 50% can be used in the first year of a contract provided that the contract complies with certain provisions calling for refund of excess load in the first two years.

At present, the SEC appears to be taking the position that mortality and expense risk charges in excess of .9% must be justified as being outside the normal industry practice. The practical effect of all of this is that it's extremely difficult to design a variable flexible payment universal life contract that is competitive with nonregistered universal life contracts. I believe for that reason, many of the contracts and registration today will in essence be single premium contracts.

MR. NORMAN E. HILL: The SEC enforces GAAP accounting rules set by private organizations such as the AICPA and the FASB. Therefore, concern over FASB pronouncements in areas such as Universal Life accounting amounts to concern over ultimate SEC enforcement.

At the moment, it appears that the FASB is leaning towards a type of deposit method for GAAP reserves. A separate method would be used for deferral of acquisition expenses. The mechanics of this method are still up in the air. Possibly onerous accounting regulations for recognizing GAAP profits on Universal Life will make the product unattractive and limit its long-term appeal to the industry. The outcome will hinge on the deferral question.

Accounting rules affect sales of Keyman insurance. Corporations buy this insurance on the lives of key employees. Premiums are not tax-deductible, and death benefit proceeds are not includable in income. For GAAP accounting, premiums must be charged against earnings, while eventual increases in cash values are offset against these charges. As a result, in early years of contract, charges against GAAP earnings may be heavy.

The accounting profession has reaffirmed that this traditional method should be used, rather than any attempt to spread out these charges in income over the expected life of an insurance contract.

The Securities and Exchange Commission has imposed maximum commissions for Variable Life. Even the 50% first-year commissions now allowed on some types of Variable Life are low compared to traditional first-year payments.

Let me cover the IRS. Since the 1984 tax amendments, tax reserves for new products cannot be revalued to net level based on $19 or $21 per thousand. Therefore, reliance on minimal or even zero gross premiums per thousand that rely on allocated benefits from this revaluation is a thing of the past.

Products today must rely on their own underwriting experience.

There is a tendency today for statutory and tax reserves to be the same (for new issues), that is, based on the weakest interest rates allowable. Companies receive no deductions for statutory reserve increases in excess of tax reserve increases. Also, this avoids duplicate valuation. Because of the connection between cash values and statutory reserves, this causes cash values on permanent products to follow higher interest rates as well.

For some products, tax reserves will remain less than statutory reserves. Under the 1984 Act, the resulting effective tax rate in early policy durations will be more than 36.8% of pre-tax income. This differential may start to be considered in pricing.

This same act requires corridors, that is, minimum differences between cash values and (higher) death benefits. Otherwise, the products do not qualify as life insurance for tax purposes. Maintenance of these corridors is especially critical for interest-sensitive products.

Due to estate tax considerations, single premium life products, including Universal Life, are often sold in lieu of annuities.

Section 845B provides unprecedented power to the government to challenge reinsurance treaties. Therefore, reinsurance arrangements designed to share initial surplus strain of new products must be carefully structured. Risk transfer is essential.

COMPETITION AND PRODUCT CONSIDERATIONS

The proposed Senate version of a 1986 income tax revision adds a couple of new elements. A minimum tax will now be imposed, possibly on GAAP earnings. For a rapidly growing company, this could severely impact cash flow. If such cash outflow were allocated to new products, their profitability could be severely impacted. Policy loan interest paid by individuals would be phased out as a deductible item. (Under a June 20 amendment to the Senate bill proposed by Senator Dole, policy loan interest, paid by corporations that would otherwise be deductible, would now be only partially deductible.)

The National Association of Insurance Commissioners has attempted to issue new regulations dealing with current types of products. In general, the NAIC tries to avoid rate regulation, it is not willing to preclude it if considered necessary to make regulations effective. NAIC proposals are not binding on individual states. Nonetheless, they serve as the model for regulations around the country.

The NAIC has influenced reserve regulations as follows:

- On renewable term products, long-term premium guarantees must often be considered when testing for deficiency reserves.

- Reserves for annuities with "bailout" provisions normally cannot be reduced by surrender charges. If the company does not credit a minimum amount of interest, such that the policyholder then has the right to surrender or "bailout" without penalty, credit for surrender charges is usually disallowed.

- The current model regulation for Universal Life reserves sometimes results in very complex calculations. If expense charges are computed on account values (that is, on reserves themselves), a trial and error process must be used. Some companies have welcomed proposals to amend this formula, while others, which have already set up the reserve software, wish to leave it as is.

Several NAIC-related pronouncements affect cash values:

- o Cash value scales under the 1980 Standard Non-forfeiture law must progress smoothly. "Pegging" of cash values in certain durations may no longer be possible, even if it provides marketing advantages.

- o The NAIC model regulations for Universal Life cash values has only been passed in about a dozen states. Since regulatory actuaries are dissatisfied with the regulation, a revised model has been proposed including retrospective minimum cash values.

- o If products are sold with high cash values, either currently or eventually, the actuarial opinion must indicate whether current reserves make adequate provision for such future guaranteed benefits.

  In effect, actuaries must be prepared to state that any pre-funding of future cash values in excess of reserves is covered by margins in current reserves.

The actuarial opinion will eventually have to address the question of matching of assets and liabilities on interest-sensitive products. One day, this requirement may extend to all permanent insurance.

"Surplus relief" reinsurance is now viewed with disfavor. An NAIC Model regulation and New York Regulation 102 disallow reserve credits for certain types of reinsurance. A lack of risk-sharing and triggering of automatic required recapture by the ceding company may disqualify such treaties for reinsurance credits. These restrictions would probably increase the cost of reinsurance, which must in turn be considered in pricing.

A proposed revision for health insurance reserves is now in the exposure stage. For certain types of products -- major medical and group coverages priced on a level premium basis -- a new reserve formula is required. Filed net premiums computed at issue, accumulated at interest, less accumulated actual claims, represent new minimum retrospective reserves. These are likely to be higher than current levels of policy reserves.

In a broad sense, state legislatures as well as the NAIC constitute state regulatory bodies. Several legislatures have passed restrictions on underwriting activities related to AIDS. If companies cannot investigate applicants exposed to this disease, increased mortality must be considered in pricing.

MR. HALSTEAD: I'd like to limit my comments, to the NAIC's Life and Health Actuarial Task Force, sometimes called the Becker/Montgomery group. (It's currently chaired by John Montgomery of the California Department and Ted Becker from Texas.)

This task force meets several times a year, usually in conjunction with NAIC meetings but sometimes in conjunction with Society of Actuaries meetings. The membership has been somewhat variable over the last several years. Usually a group of five to ten actuaries representing various insurance departments are present at each meeting.

The task force obtains input from an industry advisory committee, various task forces, the ACLI, and other industry organizations. They consider and have influence on many subjects that relate to NAIC or state regulation. All actuarial matters of any significance are run through this task force before a regulation results.

The meetings for the most part are open to interested parties. The attendees vary considerably depending on the subject and the urgency with which it is being considered.

The agenda topics for recent meetings gives a good overview of the areas the NAIC is currently reviewing. At both the March and June meetings, there were six priority one projects in the life insurance area. These dealt with (1) proposed changes to the valuation and nonforfeiture sections of the NAIC Universal Life Model Regulation, (2) variable life guidelines, (3) modified guaranteed plans, (4) actuarial aspects of reinsurance transactions, (5) alternative valuation concepts (the valuation actuary), and (6) disclosure regulations dealing with the interest yield index. There were more than a dozen projects of lower priority that were also considered. In addition, there were an equal number of projects in the health insurance area.

The biggest item they're looking at right now is probably one Norm mentioned, dealing with universal life reserves and nonforfeiture values. What they're proposing basically is a reserve arrangement that provides reserves equal to the cash value plus a margin equal to the excess of minimum reserves over minimum cash values for comparable traditional plans. (A minimum reserve equal to the greatest present value of future benefits was dropped at the June meetings, as I understand it.) The minimum cash value is a retroactive accumulation of premiums less mortality charges, service charges, partial withdrawals, and the maximum initial expense allowable. The maximum initial expense allowance would be based also on a comparable policy.

MR. EISENBARTH: I must say I'm impressed. I'm on a panel with two people who seem to understand the Commissioners Reserve Valuation Method for universal life contracts. I had assumed that no one in the country did and apparently, at least a couple do.

Let me share with you the results of a survey that measured the average time frame for approval of various types of products in various states. This is for any one of you who has taken heat because you can't get products approved in X state. No attempt was made to make this a scientific survey; however, I believe the results are representative:

Individual life: Connecticut -- 138 days, New Jersey -- 145 days, Ohio -- 9 days.

Universal life: Texas -- 159 days, Pennsylvania -- 159 days, Louisiana -- 9 days.

Annuities: New Jersey -- 236 days, Pennsylvania -- 164 days, Massachusetts -- 160 days, Oklahoma -- 9 days.

If in fact we are entering a period where the ability to deliver innovative and competitive products is crucial to success, then our ability to compete with other types of financial institutions may be affected because of long delays in getting approval from regulatory authorities. I certainly would like to see the NAIC try in some manner to address that problem.

MR. HALSTEAD: There seem to be six states that currently allow individual city premium taxes: Alabama, Florida, Georgia, Kentucky, Louisiana, South Carolina. In Georgia, the city tax is deductible from state premium taxes. In the other states, they're in addition to the state tax.

Taxes vary considerably by city and may be either a flat fee, a percentage of premium or a combination of both. The worst state in terms of the size of the tax is Kentucky. The tax in Kentucky is assessed by 175 different cities, and it varies from zero to 14% of premium. Five percent seems to be the most common tax. It is assessed by 36 different cities. For our company, the average city tax in Kentucky was 4.47%. Combining this with the state tax of 2%, our average premium tax in Kentucky was 6.47%.

The city tax in the other affected states average under 1%. When combined with the state tax though, a total tax close to 4% is produced. Our problems with these taxes are in two areas. First, we haven't priced for taxes of this magnitude, and second, the flood of tax forms creates an expensive administrative burden.

MR. HILL: In the South, certain municipalities impose their own taxes on insurance companies. Fortunately, this is still not widespread.

Companies are constantly concerned about any local regulatory discontinuities that affect marketing. If taxes are not too severe, companies often prefer to absorb them as part of a nationwide cost of doing business. If they increase too much, it could become necessary to have separate pricing and product filings, resulting in extra costs, in states with such taxes. In an extreme case, the viability of state regulation would be endangered.

MR. EISENBARTH: I think careful analysis of any new tax law may provide insight into some unique marketing opportunities. The following provisions in Senate finance committee bill may affect product design and distribution: (1) If you have a top individual tax rate of 27%, for example, how attractive is a tax shelter? (2) If you have equal treatment in terms of ordinary income and capital gains, does that mean that the inclusion of equities in a tax shelter, such as a variable annuity is more attractive than it once was? The argument has been that since capital gains have preferred taxation, you should invest in securities that generate capital gains outside of a tax shelter. Perhaps that's no longer true. (3) There are severe restrictions on the availability of Individual Retirement Accounts in the Senate bill. Most life companies have had a strong presence in this market. It was dominated early by banks. However, if the use of IRAs is severely restricted, that will have an affect on many of our companies.

MR. HILL: I think a combination of indeterminate premiums, competitively priced premiums and low cash values (on permanent products), represents a sound marketing approach today.

The 1986 proposed tax law may bring an end to IRA sales by life companies. Universal life is doing very well, I don't expect it to go away. I'm very concerned about possible restrictive accounting rules and regulations that may make the write up of acquisition expenses so unfavorable that it'll really detract from the popularity of universal life. As a consequence, more traditional participating insurance with dividends based on interest margins, essentially an interest credit, but not called an interest sensitive product may regain appeal.

In any event, I think the marketing opportunities in the regulatory environment are going to demand the utmost in creativity of everybody who is involved in that area.

MR. HALSTEAD: I've had a lot of chances to talk with general agents over the years about what creates sales and what doesn't. Most successful GAs have often said that they have the most opportunity when things are the most unsettled.

The tendency for companies is to be conservative when there are a lot of changes in the air. A lot of companies would prefer to wait until the rules and economic conditions are relatively stable before they make major moves. Things have been changing so fast though in recent years, we may never ever again have any sort of reasonable stability in our business. However, these changes are what create the opportunities.

In the tax area, the area that's probably offering most of the opportunity, change has been at a dizzy pace in the last few years. Since the Tax Reform Act of 1976, we've had the Revenue Act of 1978, the Economic Recovery Tax Act of 1981, the Tax Equity Fiscal Responsibilities Act of 1982, the 1984 Deficit Reduction Act, the 1984 Retirement Equity Act and now a proposed new tax law.

The 1969 code, which was supposed to be major reform, changed 171 code sections. 1976 and later acts changed 5,760 code sections. The 1985 Revenue Act, if it had been enacted, would have changed 4,051 code sections.

In these years, we've had the elimination and tightening of provisions which provided tax benefits to us and to our policyholders. However, they have by no means taken away all our tax advantages and in some cases had added new ones. Interest sensitive life policies came out of these changes. Single premium annuity policies, and now single premium life policies have become popular. With a little imagination and study, tax efficiencies of life products continue to be exploitable compared to nonlife products. In our company, we saw the opportunity in single premium life before DEFRA. We delayed our product to coincide with DEFRA and then doubled our premium income in one year, essentially, with this one tax-effective product. We don't know if the product will survive the next round of tax changes, but it represented a recent opportunity which we took advantage of.

MR. BABER: As our example of how regulation affects product development, I have a client who was developing IRA completion products. These are products which provide, upon death or disability, for making IRA deposits just as the insured was making them. That was one market this client was trying to work, I should say, prior to tax revisions being discussed now. At this time we don't know where that will go.

I think the key word in all this is creativity. We have to remain creative and as Burnie said, all of these things offer opportunities, we just have to find them. With all of this regulation, the role of computers is greater than ever.

MR. HILL: I started with a company in the 1960s that was just getting into computers. It had just finished an era of the punch cards and tab machines.

The company computed its deferred premiums literally by manually measuring with a tape measure the trays of valuation cards and applying a factor to get deferred premiums. The quality control was having the same individual do the tape measuring of the valuation card trays.

Compare that with today's environment. Under the 1980 Standard Valuation Law, dynamic interest rates for minimum reserves on new issues can change every year. Minimum values are now computed by the NAIC, rather than relying on traditional black volumes filled with tables of reserve factors of the Society of Actuaries. This approach was probably unthinkable back in 1970, and only became feasible with current generations of computers.

Regulatory requirements of various agencies put a strain on all available resources -- those of the company in making necessary computer calculations, and those of regulatory bodies in checking of these calculations.

Under the current Universal Life model regulation, a very complex valuation process may be required. A trial and error approach may be necessary if maintenance charges are tied to asset values.

Computerized projections are required for analyses of assets matched against reserves. Manual calculations will not suffice.

Federal requirements also require the use of computers:

- Tax reserves -- CRVM reserves at maximum interest rates call for complete separate valuation, unless statutory and tax specifications are the same.

- Guideline premiums must also be calculated by computers.

MR. HALSTEAD: One organized use of computers in the life insurance regulatory community involves the so called IRIS system. The NAIC financial ratios are intended to provide an early warning to the company and state insurance departments of unusual changes in the company's financials. The system is hardly perfect though. We found ourselves being warned because we successfully sold a lot of business; because we successfully switched our sales emphasis from term products to single premium products; and perhaps worst of all, because we negotiated reinsurance allowances and bonuses that were too good and created a lot of surplus for us. This wouldn't be so bad if it was just the insurance departments that look at this, but people like Best's and rating organizations also look at it. They have made an attempt, at least in our case, to reduce our rating because of it, and we had to provide explanations to them.

More important probably than the use of the computers by the regulatory people is the implicit recognition of computer availability in some of the laws and regulations. In drafting laws and regulations, the assumption seems to be companies have unlimited computer power. Norm mentioned the Universal Life Model Law's dynamic development of reserves based on investment experience as an example. The requirement of special tax reserves is another example of computer power needed. Calculation of guideline premiums is another example.

These regulations may require calculations so complex that the regulators will never be able to properly administer them. The regulators seem to already realize that in some cases. I had lunch with an examiner for the Illinois Department recently who has this kind of a problem. To adapt, he's asking for a PC on every examination he does any more. He also puts companies' master files on the state's computer in order to check reserves.

MR. HILL: There may be a tendency towards some type of regulatory measurement between premiums and statutory surplus. This has been the case for some time with property and casualty companies.

The NAIC relies on certain early warning tests (IRIS ratios) for spotting companies with solvency problems. However, the tests have limitations, such as lack of consistency in considering commission ratios for reinsurance ceded, but not for reinsurance assumed.

Product design today causes initial statutory strain as it always has. However, with generally lower premiums today, the strain may be relatively more severe. Statutory surplus is also under pressure due to demands on life companies by parent organizations for dividends.

PANEL DISCUSSION

MR. EISENBARTH: I want to make a couple of comments about the NAIC model bill covering surplus relief reinsurance. This bill disallows reserve credits if (1) there are provisions allowing automatic recapture, (2) termination can take place at the option of the reinsurer, and (3) deductibles or other provisions act to limit the reinsurer's claim liability.

Product innovation in our industry like many others, I believe, springs from small and medium size companies. This regulation may act to severely limit product innovation by small companies since it limits their ability to obtain financial support they need for those products.

MR. HALSTEAD: My comments on solvency concern relate to the early 1980s when interest rates spiked up to record high levels. Triple A bonds in 1979 were yielding 9% approximately, and by 1981, just two years later, they were yielding over 15%. This was a rise of 600 basis points in two years. At that time, companies were caught with a lot of long bonds in their investment portfolios. The market values of those bonds dropped precipitously and a number of companies probably would have been insolvent if their assets had been valued on a market value basis. As it was, there was a lot of disintermediation and a lot of cash outflow at the worst possible time.

Our company wasn't heavily involved with cash value products at that time. However, we were nervous when we saw our market value of assets backing a significant block of business drop 15% or more below the cash value liability of the same block.

This experience had a significant effect on our investment policies and a similar effect on others as well. What happened for us was that we stopped using long bonds altogether and brought the average maturity down to 5 to 7 years in our portfolio. The experience also had a significant effect on the industry and has led to increased awareness of the C3 risk, development of asset liability matching, the idea of a valuation actuary, and changes in guarantee funds. More regulatory activity certainly seems likely in this area.

MR. EISENBARTH: Regulation will always be with us and will always affect product design. I suspect that "federal regulation" is a synonym for dual regulation. In my opinion, government should not be in the business of regulating the price nor should its approval practices be so onerous as to severely limit product innovation.

However, regulators have legitimate concerns about solvency and disclosure. Their responsibilities are extremely difficult given the complexity of our products, the complexity of the investment policies needed to support the funding of the benefits and the inadequacy of traditional valuation and disclosure methods.

It's up to us to educate regulators, and probably in the process to be educated by them.

MR. HILL: It has been said that the 1980s are an era of business deregulation. This seems definitely not the case for life insurance companies. Because of all the pricing regulations we face, it will be a challenge for all of us to keep making money. The demands of the various regulatory bodies mentioned above will strain the ability and ingenuity of actuaries to the utmost.

An agency not mentioned yet is the Federal Trade Commission (FTC). This agency publishes periodic reports on life products and pricing, to give consumers some measure of competitiveness. In addition, the agency can bring anti-trust actions if it believes that some type of collusion among companies exists in setting premiums.

Because of all the regulations we have and our pricing activities, I think it's going to be a challenge for all of us to keep making money.

MR. STEVE EISENBERG: On the proposed tax bill from the Senate, there's a minimum tax that applies to all corporations, not just life companies. Could you expand upon income, GAAP income, or book income in excess of taxable income that will be taxed at basically 10%, (I think it's 20% of half that income)? On corporate owned life insurance, if book income will include death, now death benefits could be taxed for corporate owned life insurance under the minimum tax provisions? Do you see how this may additionally affect corporate owned life insurance?

MR. HILL: The question pertains to how the proposed tax law might affect keyman insurance. GAAP accounting would not change. Annual charges would be premiums less increases in cash value. Death proceeds would be GAAP income.

For computing regular taxes, the same procedure would remain. Premiums less cash value increases would not be deductible. Death benefit proceeds would not be includable in taxable income. However, the proposed Senate bill would make a significant change in computing a minimum tax. With GAAP income as the base, death benefit proceeds would now be subject to a tax. At the moment, since the tax is relatively small, it is difficult to measure the affect on keyman insurance.