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PRODUCT DEVELOPMENT PROCESS -- BRINGING NEW PRODUCTS TO MARKET QUICKLY AND EFFICIENTLY

Moderator: JEFFREY A. BECKLEY
Panelists: ANDREW F. BODINE
WILLIAM GATTERMAN
PHILLIP J. GRIGG
JAMES A. YOUNGQUIST
Recorder: JEFFREY A. BECKLEY

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MR. PHILLIP J. GRIGG: Identifying product needs is the first critical step in the product development process. The life insurance industry, like the auto industry, is not lacking in products. We have our cadillacs and subcompacts and an entire range of options and accessories. The choices can be overwhelming, but by identifying product needs, a company can narrow its focus and establish objectives for the product development process.

Why do we develop new products? This question must be answered in the context of overall company strategy. Product development is driven by competitive pressures both internal (for example, the desire to maintain or increase market share), and external, such as changes in the economy and the regulatory or legislative environment. Companies will generally adopt one of two strategies to respond to these pressures. The first is to be a market leader, trying to stay ahead of the competition by being on the cutting edge of product development. This strategy involves innovative thinking and a commitment of resources to research and development. It's a high risk strategy in that not all ideas will be successful. But the rewards of success can overshadow those failures. The second strategy is that of the market follower. Such a company will invest fewer resources in product development and will strive to pursue proven product ideas quickly and at a relatively low cost. Whichever strategy a company adopts will greatly influence its product development process.

Venturing outside of one's traditional market will introduce new wrinkles into the process. An extreme example would be entering into a new line of business, such as individual health insurance, which may require a separate product development path. Moving into new markets within one's product line, such as trying to capture more of the upscale market in life insurance or moving into corporate owned life insurance markets, will require a reexamination of the product development process.

Finally, the regulatory environment and economic changes have recently accounted for a significant amount of product development; for example, redesigning existing products to comply with, say, unisex laws or changes in the nonforfeiture and valuation laws, or capitalizing on new opportunities engendered by changes in federal tax legislation. In many instances, these required changes will interfere with ongoing product development. It is important to keep abreast of these developments.

Regardless of the strategy adopted, it is essential that companies monitor the marketplace. Key developments of competitors and the market's response to one's new products will provide necessary input and guidance for the next wave of product development. The markets move and unless we move with them, we will quickly find ourselves losing market share.

Understanding the overall strategy behind product development will serve to narrow the focus. The next step before embarking on the process of pricing, filing, administration, etc., is to define the product itself. Product development today is like designing an automobile. We bring together a broad array of features in a combination that will best meet the clients' needs while also meeting certain legal requirements. As with automobiles, there are some features that are common to all models and some tradeoffs are required as well. A large car has lower fuel economy, but a small car sacrifices comfort for efficiency. But all require emission controls. Sources of new product ideas include customers, competitors, the sales force, and management.

Defining the buyer and seller of the product and the extent of the market is essential to developing the right product. Furthermore, gauging the administrative systems and field support required to introduce and service the product is essential to understanding the company's commitment.

The key questions are who is going to buy the product and what's important to the buyer? Premiums can be high or low, fixed or flexible. How important is the early death benefit to the purchaser? Is the initial cash value important? What about safety and guarantees? For universal life products, what about the interest crediting rate and cost of insurance rates? Other issues may involve simplified or guaranteed issue underwriting and loan provisions. All of these features need to be balanced against one another. Not all can be most favorable to the client.

The breadth of the market is a key consideration which can make or break a product idea. How big is it and what sort of sales can be anticipated? How permanent is the market? Is this a staple product such as whole life which will endure for many years with minor variations or is it a one time situation such as single pay whole life which may soon be legislated out of existence? Assessing the impact on existing products is key. Will it bring new sales, crowd out current products, or generate replacements?

No product is going to sell without a distribution system, and the nature of the distribution system by which the product will be delivered is critical. Who's going to sell the product? How much training is needed to make the field force comfortable with the product? How flexible is the field force?

Finally, the administrative systems the company has in place will shape the development process. If it doesn't fit current systems or current systems with modest modifications, the choices are to either delay introduction, modify the current system, find an outside system or scrap the idea. In any event the cost must be estimated and factored into the pricing process.

Together, all these features serve to define the product. Knowing what the end result should be will give the product development process direction and purpose, and ensure more efficient use of resources and more consistent and successful results.

MR. WILLIAM GATTERMAN: What I've done is put together a brief overview of the pricing process. Before the actual pricing process can begin, some up-front work is needed. The product needs have to be identified and a basic design, or at least design options, have to be determined. Along with the product design there needs to be a clear understanding of the market that the product will be sold in, the distribution method that will be used, the underwriting process to be followed, and any other special considerations that are present. The pricing actuary must have a good understanding of these basic parameters before proceeding to the next step in the process. It is important that everyone involved in the product development process have a clear and consistent understanding of how the product will work, how it will be sold, etc. The better the job that's done to satisfy this requirement up front, the smoother the pricing process will go.

The next part of the process that I'd like to discuss is the determination of assumptions. This is frequently one of the tougher parts of the process. The profitability and competitive outcome of the product is heavily dependent on the assumptions decided on. There are the basic assumptions that need to be made such as mortality and morbidity rates, expenses, lapse rates, investment rates, and taxes. But there are also some new types of assumptions that are needed, due to the design of some of the newer products. For example, premium payment patterns are a crucial assumption in pricing out a flexible premium product like universal life. Another area that pricing actuaries are becoming more concerned with is pricing for the investment risk that is inherent in our newer products. Another new factor present in our environment is the impact of AIDS.

In developing assumptions, the starting point is frequently an examination of past experience, whenever it is available. Modifications should be made for current trends in experience. Also, changes in the environment that impact your assumptions should be anticipated. The pricing actuary also needs to consider how the current product design, market, etc., will impact experience.

For example, there may be a particular feature added to the product to enhance persistency. This factor should be considered when developing lapse assumptions. Assumptions should be developed for a variety of scenarios, with different scenarios appropriate for different aspects of the pricing process. For example, when pricing the guaranteed basis in the product, very conservative, disaster-type assumptions should be made. Pricing the current basis in the product should follow a best estimate scenario.

Now that you have a good idea of how the product should work, and the assumptions that are needed to price the product, you need to look at your pricing system to make sure that it is compatible for pricing the product at hand. Any changes that are needed should be made and properly tested. These changes may need to be made to more than one system depending on how a particular company's pricing system is designed. To do a complete job of pricing the product you may need to look at a per unit profit analysis, a financial projection for several years of issues, as well as an illustration of values for competitive comparison purposes. Developing a system that will support all of these functions can generate some efficiencies. One suggestion to keep in mind in setting up the pricing system is to allow for easy and efficient changes to be made so that it is easy to test different assumptions.

The last item that I've identified in the groundwork stage is company objectives. It is important to have identified the company profit objectives for a particular product line or type of product before you ever engage in any pricing work. This means both how profit is measured, such as profit-to-premium ratios, return on investment, asset share-to-reserve ratios, etc., and also the level of profit. One of the more recent developments in this regard involves taking target or required surplus into account in the profit determination process.

The other company objective to identify is the relative competitive posture that a company wants to achieve. This ultimately needs to be reconciled with the company's desired profit objectives. Also, it is influenced by the distribution system and markets in which the company sells. Company growth objectives also need to be considered in setting the competitive objective. You should clearly define who your competition is. Also you should define the relative importance of different competitive aspects; for example, agent compensation, product benefits, and product price. You can't be tops in everything.

Now that the groundwork is laid and you know what you're pricing, you know the assumptions you're going to use, you have a system to do the work, and you know what the company objectives are, you can start to do some profit testing. To quote one of the popular wine cooler slogans, "This is where the fun starts!" Trying to balance the profitability and competitive requirements is a tough task in today's competitive marketplace. The profit testing, premium adjusting, and benefit adjusting process is an iterative process involving a lot of give and take. There are many factors that the pricing actuary can adjust during this process. Premium rates, agent compensation, cost of insurance charges, expense charges, surrender charges, and investment margin are all examples of items that can be "fine-tuned." The key is to find the proper balance of these items so that an acceptable level of profit is achieved, while at the same time producing a saleable product. It is not uncommon for the pricing actuary to occasionally question if this is all possible, but somehow we seem to always find a solution.

It is common during this process to question, or to have others question, the assumptions used. While it is appropriate to use the market as a check on the reasonableness of the assumptions you're using, you need to be very careful about making changes that can't be supported. Before finalizing any pricing it is important to do some sensitivity testing of your assumptions to make sure that you understand and are comfortable with the risk of adverse deviation in each of the assumptions.

It is also important to perform various consistency checks before finalizing your pricing. This should include checks within the product comparing rates by age, sex, smoker, nonsmoker, etc. Also you should make comparisons with existing products, making sure the relationships make sense. Errors caught at this point are still much easier to correct than those found after filing, systems installation, rate book printing, etc.

The final step is documentation of all assumptions and profit results. Proper documentation of expected results is vital if you are going to do an adequate job monitoring actual to expected results.

To close I'd like to briefly discuss suggestions to make the pricing process work a littler smoother. The process can be time-consuming and can often involve several iterations. Try to minimize the work for each iteration. However, you need to be careful when doing this. You need to have enough cells to get a good idea of what is happening, but some ideas can be tested by maybe looking at just one age rather than several ages, or by just looking at nonsmokers rather than smokers, etc.

I think it is very helpful to maintain and circulate a written working copy of up-to-date specifications, assumptions, and results. This will aid in avoiding confusion, and will help to raise issues sooner. You want to minimize any last minute surprises.

As I said earlier, know your objectives and get agreement on these up front. This is especially important with your competitive objectives. You don't want to be chasing a moving target.

The last idea is to recognize that no matter how good a job you do up front laying out the product design, changes are inevitable. Try to maintain a flexible structure so that changes can be accommodated quickly and efficiently.

MR. JEFFREY A. BECKLEY: Often one of the biggest bottlenecks in today's product development process is systems. Many of today's products are by-products of the technological explosion of the last 10 years. It is therefore ironic that the introduction of new products is slowed down for the development of systems. My brief comments will be broken into two parts. First I will discuss administration systems and then illustration systems.

From an administrative standpoint there are several things that can be done to improve the speed and efficiency with which products may be brought to market. First, the easiest method of making systems a nonissue in the product development process is to develop your product to conform to your system. However, in today's world it seems that this is seldom possible.

The second area of potential savings is the very basic question of who will actually do the administration of the product. Too often, this is not even a question that is addressed. Companies assume that they must administer the product in-house. However, there are alternatives such as timesharing, or use of a Third Party Administrator (TPA). Use of timesharing has become more popular in recent years for both life and health administration. Many of you may not be familiar with third party administrators. TPAs have been involved in the administration of health business for a number of years. TPAs can administer health insurance claims cheaper and more efficiently than 99% of the insurance companies in the nation. In recent years TPAs have expanded their operations to include the front end administration of health business. Some TPAs are even administering individual life business. In the future, I believe TPAs will play a larger role in the individual life business.

The use of a TPA or timesharing can often result in quicker, more efficient development of systems to handle new products, provided the correct vendor is selected. Obviously the selection of the vendor is critical. However, these vendors specialize in administration of products and therefore, they must adapt quickly to new products and innovations. The major drawback with using outside vendors is the lack of control which often leaves companies feeling uncomfortable. However, I believe that in many circumstances companies should consider the use of timesharing or TPAs when time is of the essence in developing a new product because many times these outside vendors can produce a working administrative system quicker and more efficiently than we can in-house.

No matter what the source of your administrative system, it is critical that you involve your systems people early in the product development process. I believe that your product development team must include systems personnel who are technically knowledgeable with regard to your administrative systems. This provides instant feedback to the product committee with regard to the difficulty of administering any new product. Further, early involvement promotes a feeling of cooperation and does not put the systems department in the position of feeling dumped on. Early involvement also allows systems to begin any necessary modifications during the product development process and not after the product is ready to be marketed.

If the current administrative system will not handle the product, then it must be modified. It may be possible to speed the introduction of a new product by concentrating the system's modifications in critical areas, while leaving items that can be put off to be done later. For example, when PRUCO introduced their variable life product, their prospectus stated that no policy increases would be allowed for one year after issue and certainly not before a given date. The given date was the date that they anticipated completing the system modifications to administer increases.

Finally, with respect to administrative systems, I believe that there is one other critical item that a company should do. I believe that every company should establish a permanent model company within their operation. The model company is an invaluable asset in testing system modifications and determining system capabilities. In this model company, there needs to be representation from the Actuarial Department, Information Systems, and Administration. The members of the model company who perform the best tend to be highly motivated nonmanagement personnel. I firmly believe that a good model company is one of the most valuable assets a company can develop to assist in making the product development process more efficient from a systems standpoint.

With regard to illustration systems, there are several key things that can be done to help bring the product to market quickly and efficiently. As with the administrative end of systems, get your illustration systems people involved early. They do not need to be involved as early as the administrative systems personnel, but they do need to become involved as soon as the product design is known. Programming of the illustration system can begin before rates are finalized. The rates and other incidentals often go in files attached to the main logic and can be easily added at a later date.

Second, provide illustration software developers with complete and final specifications. Too often, I have seen incomplete specifications, or numerous versions of specifications result in an unnecessarily long development process. The format of the illustrations should be laid out early by your marketing people. Once again, rates and other incidentals do not need to be finalized before laying out the illustration.

If you use an outside software development firm, make sure that as part of the arrangement you receive documented source code. Documented source code is important for two reasons. First, it allows you to make future modifications in the software quickly and easily. Of course, this assumes that as part of your contract with the software developer you have such rights. The second reason for requesting documented source code is that many times I have found the source code to be quite useful in debugging the illustration system.

MR. JAMES A. YOUNGQUIST: "We now have Imaginative Life III available in all states beginning January 1 . . . except in New York, Texas, California, Pennsylvania, and New Jersey." How many of you enjoy making statements like this to your field?

Bringing a product to market quickly and efficiently includes gaining state approval quickly and efficiently. The main point I would like to emphasize is that no matter how good your product is, how important it is to the consumer, and how much thought and work went into the product development and pricing process, it must have a state's approval before it can be used in that state. Of course some states exempt forms from review or allow companies to deem forms approved, but these actions are still within the official approval process.

I will clear up some details related to the filing: the drafting process, the content of a filing submission, and timing; and then get into ways to speed up the process. For additional information related to the filing and approval process I would direct you to the panel discussion by Karen Weiss at the Kansas City meeting in June, 1986 which appears in the *Record*, Vol. 12, No. 3. Also, one of the best sources of information related to individual contracts is the Life and Health Compliance Association whose current president is Carl Barnes at Kansas City Life. This association provides a wealth of information through handouts at their meetings.

The drafting process begins with developing policy language from clear specifications. These specifications have to come from the product development people. Start with another company's contract if the product is new to your company. Approved contracts are public documents and are on file at the state insurance departments. Use your own previously approved contracts for standard provisions. Don't reinvent the wheel for a reinstatement provision -- save your imagination for the benefits section.

Consider readability standards at the front end of drafting. People are more cooperative in helping to develop readable language when the contract is being developed, rather than when they think a project is supposed to be completed.

Early filing is totally dependent on various pieces from the pricing process. Sample numbers for the specifications page are needed for filed contracts.

Gross premiums and nonforfeiture values for sample age 35, durations 1-20, are needed well in advance of completion of values for all ages and durations. The NAIC Policy Summary with cost indices at 10 and 20 years even requires a dividend scale for the sample age.

A properly submitted filing submission contains a number of items which are itemized fairly straightforward in state regulations. Forms must be submitted in duplicate with an application attached. The forms need sample fill-in data. The form number must be in the lower left hand corner. This number isn't something that can be arbitrarily changed by your service departments when the form is reprinted. A postage paid return envelope must be included so that the state can return the duplicate forms with their approval stamp. We omitted a 73-cent return envelope and had the entire filing returned by one state; that return cost the state $2.00 in postage.

A filing letter also in duplicate is enclosed in the submission. This letter (1) lists the forms included in the filing package with a brief description of each form; (2) indicates whether the form is new versus replacing a previously approved form; (3) describes unusual concepts in the form; (4) includes a copy of home state approval or indicates home state filing status; (5) includes a Flesch readability certificate; and (6) includes other certifications and transmittal forms.

An actuarial memorandum is required on all health filings. Among other items, this memorandum gives the rate basis, the anticipated loss ratio, and the relation of premiums to previously filed rates. Finally, a complete set of all rates is required for approval in North Carolina, Connecticut, and in all states for all health filings.

Time for approval is an important item because sometimes our project executives wish to measure approval time in minutes, when I need months. A goal for the number of state approvals should be set during the product development process. Certain states take more time and effort in which to gain approval, whereas 40-45 states may grant approval within one or two months. Decide on the acceptable number of states in which you want approval for your eventual announcement to the field of the availability of the new policy. For complete state approval we estimate a life filing will take four months, an accident and health (A&H) filing will take six months, and a variable product will take nine months. To these times we add one week just to assemble 50 state packets and another three weeks to prepare all required state variations.

Finally, how do we speed up the process? The following items are not in any particular order of priority. Home state rapport is vital since home state approval is required before approval in about half of the states. Good rapport and a promise of completion ASAP can sometimes gain approval of an incomplete filing in a home state.

Keep a log of previous questions with your answers. Preanswer these questions in your cover letter. If Texas is going to ask if your minimum size disability income policy is $200, tell them ahead of time.

We keep a check list of the state variations for review one last time before mailing. It doesn't make sense to mistakenly send a standard suicide provision to Missouri when you know that all your previous submissions required a variation.

Special considerations are justified in some states. Although we try to treat a filing as an assembly line process, sometimes a state may have enough separate requirements that if we spend several extra days preparing a filing for that state we can save several extra weeks in approval. New York is an example.

Double-checking of a complete mailing may find certificates or fees which may have been reversed. Washington state material can get reversed with Washington D.C., Virginia with West Virginia.

A number of states don't require home state approval but may require only the home state filing status. You may save the time it takes to get home state approval by mailing your submissions to these 20-30 states prior to getting home state approval.

Many states have a 30-day deemer period. To prove a state has had a filing for the required 30 days, we send filings by registered mail with return receipt requested.

Phone calls to states may help gain quicker approval. Frequently the cause of a disapproval is unclear from a letter. A phone call can determine the exact cause of the disapproval and can frequently be used to determine a solution. However, we don't like to use the phone on more routine filings, such as a new application; we save the phone calls for priority items.

A face-to-face visitation may result in solutions to product concepts well before the filing process has begun. Wisconsin suggested the idea of an amendment to an existing product rather than a new product, so that we could stay on the 1958 CSO basis for an extra year in 1982. An amendment also may be approved more quickly than a policy.

Finally, convince the regulators that they can trust you. A regulator may grant approval of a product that will require future disclosure without initially seeing that disclosure at the time of filing. He will only do this if he believes you will satisfy his requirements at a future date in an acceptable manner.

MR. ANDREW F. BODINE: Reinsurance has been receiving a significantly increased amount of attention at Society of Actuaries meetings in the last year or two as compared with prior years. Much of this is associated with self-administration of interest-sensitive products which develop risk amounts on an unscheduled basis and thus are difficult for administration by the reinsurer.

There are other matters, such as the mirror-imaging of reserves and statutory regulations aimed at prohibiting reinsurance arrangements, which achieve only a transfer of surplus without any meaningful risk transfer. Although these are related to the subject of product development, and deserve to be considered, I will try at this time to limit my remarks to the subject of common treaty negotiations between a ceding company and its reinsurers with respect to development of a single individual life product.

Obtaining reinsurance at the lowest cost is the most obvious negotiation point, but it is certainly not the only consideration. Price quotes from several reinsurers will have differences which make it difficult for direct cost comparisons.

Yearly Renewable Term (YRT) rates are likely to consist of a set of different schedules by sex and smoking class, but they may also differ from the ceding company's mortality assumptions, with respect to the length of the select period and the slope of mortality rates by duration. Coinsurance quotes might be simply a constant percentage of renewal year premiums for all classes of insureds, following a high first year allowance, such as 100%. More commonly, coinsurance allowances may differ by duration periods, such as the first 10 years versus 11th and later years, or by young and old issue ages, or by smoking class. Coinsurance allowances or YRT rates may differ between policies on which the ceding company keeps its full retention versus facultative cessions where less than full retention is kept. For companies which are not particularly seeking relief from first year surplus strain, reinsurers may offer very attractive renewal year rates or allowances as an alternative to low first year net rates.

How are these rates compared? Some relatively similar reinsurance quotes can be judged to be more or less costly by a quick "eyeball" review. When this cannot be done, common pricing techniques can be used to determine the various levels of profitability both for age/amount cells and on a model office basis. This could include extensive testing for the more complex products involving interest-sensitive values and other indeterminate features which may affect balances between risk amounts and cash values in future years. Such plans should be subjected to sensitivity testing.

Pricing assumptions, including the expected mix of business, are not only important for competitive price analysis but should be discussed with the reinsurers to avoid differences of opinion. Reinsurers can simplify, or shorten, the negotiation process and otherwise be more helpful to the ceding company if, in preparing their quotes, they have an appreciation for how much reinsurance cost the ceding company can stand or the minimum level of coinsurance allowances needed by the ceding company to meet expenses. Assuming a soundly priced product, the price negotiation process should end up with both the ceding company and the reinsurer being able to cover their own costs, with the added margin in the premiums split between the two parties relative to the risks being shared or favoring one of the parties as a result of the negotiation process.

Any meaningful market research done by the ceding company prior to product development should be shared with the reinsurer. If relatively high mortality rates are expected because of special underwriting techniques, special market penetration, or for other reasons, this should not be withheld from the reinsurer. A scenario could develop under which a reinsurer is overly optimistic and it wins the competition against other reinsurers, and then several years later is faced with the financial necessity of increasing reinsurance charges for future issues. This action creates several unhappy relationships including negative surprises to the ceding company management if the volume of business for such a plan has been significant to the ceding company, and it can damage relationships between the home office and field force if it leads to the need to reprice the product.

In this rapidly changing environment regarding product design, companies may reach a point where, in response to comments from their agents, they must bring out a product with which they have little experience. It may be difficult for the ceding company's pricing actuary to have a good feel about assumptions for such product pricing. In these situations, he can turn to the reinsurer in the early stages of product development for assistance in understanding what type of experience to anticipate. The reinsurer in many cases will have developed such experience, or at least have an understanding of expectations from their experience with other ceding companies. Basic pricing concepts can be shared in the same sense that problems are discussed in Society of Actuaries workshops, seminars, teaching sessions and panel discussions, without any breach of confidentiality from the client-company relationship.

This brings us to the timing of initiating reinsurer involvement as a pricing consideration. If the ceding company's pricing assumptions and ultimate premium levels are not overly aggressive, profitability can be tested without recognition of specific reinsurance costs. There should be little problem with such products in the reinsurer negotiation process in finding adequate reinsurance support where both parties' costs are covered and the margin's shares are as previously mentioned. However, if reinsurer support in the sense of aggressive YRT rate schedules or coinsurance allowances must be depended upon to achieve the direct writing company's profit goals, then coordination with reinsurers regarding the extent of their support and their recommendations is critical at the early price design stages. Even without such a critical support need, early involvement of the reinsurer might be very helpful to the ceding company's pricing actuary for certain assumptions such as basic smoker and nonsmoker mortality rate trends.

You might want to consider the choice between proportional risk retention and level risk retention. Level retention should ultimately reduce reinsurance costs for permanent plans as the growth of reserves leads to reduced risk amounts. However, this has an effect of which the ceding company's top management should be aware, in that the ceding company retains a larger amount of risk for traditional policies in force at longer durations. It may be a matter for the "comfort level" type of decision for the CEO or the board of directors.

Consider whether premium taxes should be reimbursed to the ceding company or included in the basic rate and allowance quotes. If reimbursable each year, the basis for reimbursement should be the company's gross premium, not the premium net of coinsurance allowances. Of course, this somewhat subtle difference, as well as the broader question of reimbursement, could already be reflected in the development of the price quote by the reinsurer's pricing actuary. There is an obvious administrative simplicity by agreeing to a structure which would not involve premium tax reimbursement, but there might be concern about the future risk of the levels for future state premium tax rates.

I would guess that many ceding companies conclude their price negotiation process with a reinsurer without carefully considering the mix of business and testing for profitability with respect to substandard rates, allowances for supplemental benefits and flat extra charges, and consistency as to when flat extra charges are a commissionable item to the writing agent. Even if these items are not significant compared with the costs for the basic risks being reinsured, they may be used as a basis to choose between reinsurers when the competitive reinsurance bids are relatively close.

Other negotiable items, less directly a matter of pricing, include the recapture period. This appears to be a great concern among reinsurers, who are depending on high persistency levels for achieving their profit goals.

Reinsurance costs based on coinsurance allowances will often contain a maximum risk amount to which such allowances apply, with the excess risk amount reinsured based on the table of YRT rates. This maximum amount and the alternative YRT rates can be negotiated.

Maximum amount limits where cessions can be submitted automatically to the reinsured are important to the underwriters and the field force. Jumbo limits, the total amount in force on a proposed insured life before the new case, regardless of size, must be submitted to the reinsurer for facultative consideration, and can also be important, depending on the market and nature of the field force.

If the product being reinsured is term insurance, what are the conditions of reinsurance rates and the recapture period following conversion to a permanent plan? For modified coinsurance, an interest rate is an obvious point for negotiation. Although I have never been involved in negotiating such a treaty, I would suspect the interest rate would not be a fixed flat rate but would be relative to rates which vary, as with current interest-sensitive products.

Claim consultation with the reinsurer is often required when over half the claim is reinsured. It may be appropriate to negotiate a minimum size policy for such consultation. Otherwise, many pro rata cases may result in consultation on relatively small cases.

I find our legal department wants me to negotiate better treaty terms with respect to participation in punitive damages, claim litigation, and the site where arbitration will take place. I have to admit to little success in such treaty negotiations but it has never become a material question in practice. I have recommended that, regardless of treaty terms, reinsurer participation in any claim litigation which might result in punitive damages should be discussed at the early stages of such litigation and agreed to in writing with respect to that specific case.

Automatic reinsurance for a single product does not have to be restricted to one reinsurer. There are several bases on which more than one reinsurer can be involved including pools, alphabet splits, and pro rata shares.

The most important consideration to be considered other than obtaining the best reinsurance price should be the relationship of the underwriters with the reinsurer's underwriting staff. To what extent is the existing relationship satisfactory? Is this a time to seek a change if there are signs of rating disagreements? Has the reinsurer demonstrated a willingness to work with the underwriting staff on special case situations? To what extent would a new reinsurer who is trying to obtain a share of a particular ceding company's business be able to provide better opportunities for direct sales which would strengthen home office/field force relationships?

Long-standing reinsurance relationships should not be terminated merely because of aggressive price quotes from other reinsurers trying to get a foot in the door. If the long-standing relationship remains reasonably competitive and the reinsurer's knowledge of the ceding company has led to favorable results and support as needed, special case considerations, expertise on developing legislation, help on product evolution information, state forms filing assistance, and legal advice particularly in claim litigation, then this clearly has a value. Although similar support may be available with the new reinsurer, it is an unknown quantity. It may be a matter of giving up such support for the price difference, which clarifies the price tag for such support.

Implicit in all of the comments I have just made, there is a working agreement between the ceding company and reinsurer which depends on faith, honesty and high ethical standards in a way I have not seen with any other business relationships, especially those evidenced by legal treaties. This is a two-way street in which the ceding company must not take advantage of the reinsurer nor should the reinsurer take advantage of the ceding company. Negotiations should not be done on a price-only basis; they should be done on a basis of maintaining long-standing relationships with several reinsurers and not being dependent on only one reinsurer. Changes in reinsurer relationships should not be frequent, but should take place when warranted.

MR. MELVIN J. FEINBERG: My comments relate to what I call the fun part of product development and may relate more to bringing products to market efficiently, rather than quickly. This is the show biz aspect. If your agency force does not understand why you have spent resources to develop new products, and they do not understand the products themselves, or why they are superior to what they are currently selling, I do not believe that you are going to be too successful.

What we have done at New York Life are "road shows." This involves visiting the agents in the different regions, presenting them with materials on the products, and letting the training managers in each of our general offices know what is occurring.

MR. GRIGG: PRUCO Life has its own unique marketing staff which is not associated with Prudential. This is a six-person team who spends their entire time going around the company educating our agents on our variable products and any other products coming out of PRUCO. They have been very successful to the extent that the PRUCO is now Prudential's new sales. Further, if you include dump-ins, PRUCO generates in excess of 50% of the new premium. To a large extent it is the product that generated the sales, but it is also this marketing staff that generates the excitement for the product. Certainly my involvement in product development has been one of going the extra step and making certain that the field understands and appreciates the products that you have designed. For a company such as Prudential with thousands of agents, most of whom are not very sophisticated, getting the agent to understand the new products and how these products can be used is essential to the success of a new product.

MR. YOUNGQUIST: When we have introduced all of our new products, we have put together road shows. Generally there are six, or seven, two-person teams consisting of an actuary and an attorney. These teams visit each of our 120 agencies with a professionally polished show. These shows include slides and speeches that have been coached by professionals.

MR. GATTERMAN: At Time Insurance, we do not go out to the field to introduce a new product. However, we typically time our new product introductions to our annual meetings that we have.

MR. BECKLEY: Obviously, the first priority in the product development process is to make certain that there really is a need for a new product. I do not believe that we can go out and sell our agents on a new product if there truly is no need for a new product.

MR. BARRY L. SHEMIN: You have talked a lot about the specific elements that go into the product development process. However, in looking at the entire process, there are so many elements. I wonder if any of you have had any experience with project management, that from the beginning of the process will allow you to complete the process more efficiently, or will allow you to predict more accurately when the process will be complete.

MR. GRIGG: We use pert charts. These are insidious little things that tell when everything is due and how it all fits together. It is sort of like a large tree where the root of the tree is the final product and the branches of the tree are the various things that must be done to get that product in place. It is a method of coordinating the entire project. We have used the pert charts since 1983 when we began entering the nontraditional marketplace.

We tie up a lot of people in this process. Probably the smaller number of people that you involve in the project, the smoother the whole project will go. The downside of having only a few people involved is that the company is relying on these few people who are experts, and at some point that knowledge must be passed on to others.

MR. BECKLEY: One of my clients has what they call a "network committee." Basically, this is a method of coordinating new product development. The network consists of the managers from the various departments. These managers assign their personnel to each product as necessary. The personnel may even be assigned on a full-time basis. The whole process is built around establishing deadlines, responsibilities, and priorities. Further, the network monitors the process through these deadlines.

MR. GATTERMAN: One of the biggest problems with meeting deadlines is the changing of specifications. If specifications, or at least the potential options that will be considered, are nailed down early, the process will proceed much smoother.

MR. ALBERT E. EASTON: Jeff, you mentioned the idea of using a model company in product development. Could you elaborate and perhaps give an example?

MR. BECKLEY: A model company is a small group of people set aside within your company whose responsibility is to test your administrative system, or modifications thereto. This group should also spend time exploring the capabilities of the system. Most of the systems available for purchase today do not have very good documentation. Therefore, it is necessary for the model company to experiment and determine exactly what the system can accomplish.

The value of the model company in the product development process is threefold. First, knowing the capabilities of the system is critical in product development. Second, the model company can provide rapid testing of any necessary modifications to the system. Finally, the model company can be invaluable as an educational resource for the administrative areas of the company once the testing is complete.

MR. BARRY JACOBSON: How long do you allow for the development of a new product, particularly a new universal life product?

MR. GRIGG: Much of the time frame is company dependent; however, we generally target a one-year time frame.

MR. GATTERMAN: That is a very difficult question to answer. It is highly dependent upon the product and can vary from anywhere from two months to several years. Generally, I would say that we target six months to one year.

MR. YOUNGQUIST: Generally, it takes us one to two years, but there is a lot of variation. It is highly dependent upon the products and the priorities.