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PRICING ON A UNISEX BASIS -- CONSIDERATIONS

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- o Regulatory developments
- o Protecting against adverse selection
- o Pricing considerations
- o Experience analysis

MR. CHRISTIAN J. DESROCHERS: When the program for this meeting was being written, we felt that if we scheduled a talk about sex, even at an early hour, we would attract an audience. I am glad that so many of you decided to attend.

I'd like to begin by introducing the panelists. My name is Chris DesRochers, and I'm a consulting actuary with Chalke Incorporated in Washington. I'm the moderator for this session, and I'll be speaking about pricing on a unisex basis. Barbara Lautzenheiser is the actuary most associated with the unisex issue and has been talking about sex for 20 years or more. She's the principal of Lautzenheiser & Associates in Hartford, a past president of the Society, and currently a member of the Actuarial Standards Board. Barbara will be discussing legislative and regulatory activities that are ongoing this year and will give us an update on the current status of the unisex movement throughout the various states. Our other panelist is Klaus Shigley, who is vice-president of John Hancock in Boston responsible for individual life product development. Klaus will be discussing the Massachusetts regulation on unisex.

MR. KLAUS O. SHIGLEY: It's customary to state that the views one is about to express are one's personal views and not the views of the management of the company one represents. In this case, the views that I'm about to express reflect the views of the Massachusetts Insurance Department. My objective is to give you an overview of Massachusetts unisex regulations, and at the risk of putting you to sleep, I will outline the regulation for you because, one, it's short, and two, it may serve as a model for future legislative initiatives. I will also try to give you a flavor of the political environment which gave rise to the Massachusetts regulation, and I will discuss examples of the compliance issues raised by the Massachusetts regulation.

The regulation is only two pages long. It resides in volume 211 of the Commonwealth of Massachusetts Regulations, section 35. The regulation consists of six sections. The regulation follows a somewhat standard and even logical regulatory sequence. It begins by citing the legislative authority in Section 3501. Then a statement of purpose is given in Section 3502. Some definition of terms are listed in Section 3503. These terms are then used in Section 3504 and in 3505, which are the sections that define the requirements and the scope of the regulation, and I will examine these sections in detail. The last section on severability is the regulatory equivalent of escalating an arms race with multiple warheads, and I'll explain that later.

The regulation was effective on September 1, 1988. It claims equal rights as its purpose in a string of generic language in Massachusetts' regulations and laws giving the commissioner the authority to make rules which implement the law -- in the case, the equal rights amendment (ERA). However, there is no specific legislative authority for the regulation. The genesis of the regulation rests on unisex legislation, which was sponsored by Massachusetts House Majority Whip Mary Jane Gibson, and which passed the Massachusetts House in July of 1986, but failed the Senate, so it never became law.

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The regulation which was promulgated was very similar to this legislation which failed. There are some differences, however, between the legislation which failed and the regulation which we now have. The bill which passed the Massachusetts House contained an amendment which struck out all retroactive provisions. Another amendment which would have permitted the use of gender ratios for group plans failed to pass. I believe it was the failure to achieve an acceptable compromise for group plans which led to industry opposition of the bill in the Massachusetts Senate, where the bill was ultimately defeated.

After the bill was defeated, the Massachusetts Secretary of the Executive Office of Consumer Affairs and Business Regulation (this is our Consumer Affairs Secretary, who oversees the Division of Insurance) requested an opinion from the Massachusetts Attorney General on whether the insurance commissioner could issue such a regulation on other authority. An affirmative opinion from the Massachusetts Attorney General's Office came in January 1987. In August 1987, the regulation was issued. We now have a regulation that is more onerous, and that has more retroactivity than the bill which failed. This scenario could easily happen in any state which has an ERA.

If the regulation is upheld in our courts, and there are two court challenges at this point, then the moral of the story is that we should have worked harder to work out a compromise with our legislators rather than be governed by our regulators.

The substantive sections of the regulation are 3503 through 3506. Section 3503 defines terms. Only two items in this section are worth focusing on. The first item relates to pregnancy. The regulation explicitly states that discrimination with respect to pregnancy is sex discrimination. The key concept in Section 3503, and the second item worth noting in this section, is the definition of a renewal by agreement. A policy is renewed by agreement when the premium under the existing policy is changed by an amount not predetermined by the terms of the policy. For example, a smoker to nonsmoker conversion or a decrease in the insurance amount are renewals by agreement because they cause the premiums to change. This definition for renewal by agreement is modified for universal life (UL) type policies. A renewal by agreement for UL policies occurs when the schedule of charges changes. Now, why do we care about the definition for renewal by agreement? It is important because if an existing policy is renewed by agreement, then the entire existing policy must be converted to a unisex basis. This is the retroactive part of the regulation.

What does it mean to be "unisex" and what are the requirements? The requirements of the regulation are defined in Section 3504. The first requirement is that no insurance policy may use a sex distinct table as the basis for the classification of a resident of the Commonwealth for any purpose. This includes not only premium and benefit classification, but also underwriting classifications based on sex distinct tables. Thus, underwriting based on build and blood pressure has effectively been unisexed. At John Hancock, we are no longer underwriting with sex distinct build and blood pressure tables for Massachusetts residents and I think it's clear that this is the intent of the regulation.

The most controversial requirement in this section of the regulation, however, is the commissioner's apparent insistence that all products must use a single gender ratio -- for nonforfeiture benefits, for cash values, guaranteed mortality charges; all products must use the same gender ratio. Life insurance, annuities, settlement options, even joint and survivor annuities and joint and last-to-die insurance must all be based on one, and only one, of Table A, B, C, D, E, F, or G, which are variations of the 1980 CSO Table for different gender ratios. This requirement, if it stands, will be effective January 1, 1990. The Life Insurance Association of Massachusetts (LIAM) has just written a letter to the commissioner requesting the withdrawal of this requirement by noting the problems that it would create. This rather draconian requirement is motivated by the commissioner's fear that insurers will circumvent the regulation by designing two policy forms: a "pink" form and a "blue" form. The blue form would then be marketed to males, and the pink form would be marketed to females.

The regulation prohibits different treatment for any covered person or applicant who is a resident of Massachusetts with respect to the availability, terms, conditions, rates, benefits or requirements from an insurance policy.

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Section 3505 defines the scope of these requirements. That is, under what conditions do these two requirements apply and what are the effective dates? They apply to all policies issued or renewed by agreement to all residents of Massachusetts on or after September 1, 1988.

In addition to imposing the requirement of the regulation to new issues and to a renewal by agreement, the application of the regulation was broadened to include all changes made to existing policies with respect to payments, amounts of coverage, premium or benefits, the terms of which are not calculable from the terms of the original policy. Under the regulation, there are two conditions under which you have to unisex the policy -- (1) if there's a renewal by agreement and (2) if there's a change. Paragraph one pertains to renewals by agreement and paragraph two is for changes to a policy. The second paragraph of this section expanded the scope of the failed legislative draft because our attorney general believed that the regulation should provide some relief for existing contract holders. The logic here is that a renewal by agreement is essentially a new contract and that falls short of changing a policy or making a change to a policy which is not as definitive as writing a new contract. A mere change, however, should also have the benefit in the view of the attorney general of providing some relief to existing contract holders. The rest of Section 3505 defines September 1, 1991 as the effective date for group plans, permits blended tables for Norris cases, and permits the issue of family policies. That's the overview of the regulation. Now let's look at some examples.

The first example I want to look at is dividends. A simple attained age change in dividends without the change in scale does not trigger the application of the regulation. However, a change in dividend scale does trigger the application of the regulation. Such a change in scale is not a renewal by agreement, which would trigger unisexing the entire policy. A change in the dividend scale is a change as defined in Section 3505, paragraph two. As such, the regulation requires only the item which is changing, that is the dividend, to be unisexed, but not the entire policy. This interpretation is detailed in a November 7, 1988 interpretive bulletin from the Insurance Department.

The bulletin doesn't address how to create a unisex dividend scale. Do you pay the same amount of dividend or do you unisex the mortality component of the dividend formula? At least one company, and perhaps two, has taken the view that the regulation requires that the mortality factor in the dividend formula should be unisexed. And in one case, when this unisexed mortality factor is applied to the respective cash values for males and females, the difference in the dividend amount paid to males and females actually widens. So I can't give you any guidance on how to unisex the dividends. My own company already has unisexed dividends.

Incidentally, a somewhat similar, but slightly different logic applies to indeterminate premium term policies. The premium increase triggered by changes in the attained age is not a renewal by agreement. However, a change in the schedule of current charges is a renewal by agreement because it is a change in premium. The renewal by agreement forces the unisexing of the entire policy in contrast to unisexing just the dividends, but not the entire policy in the previous example.

A renewal by agreement is defined in a different way for UL and other flexible premium products. First of all, the regulation defines a term called a "joined insurance/savings plan" to represent the generic UL. A joined insurance/savings plan is a policy comprised of a separate investment of savings component and a mortality or morbidity component. For such decoupled plans, a renewal by agreement occurs when the entire schedule of charges for mortality or morbidity changes. A change in the overall premium does not trigger a renewal by agreement. However, a change in the schedule of current charges does trigger a renewal by agreement, which will force the entire policy to be unisexed.

Another problem is residency. The regulation applies to all policies issued to residents of Massachusetts. This requirement can cause severe problems since many companies, ours included, administer policies based on the state of issue. The November 7, 1988 bulletin, moreover, requires the application of the regulation to Massachusetts residents who temporarily reside elsewhere. On the other hand, the November 7, 1988 bulletin does not require an insurer to amend a policy for individuals who move into the state.

Finally, where either the owner or insured lives outside of Massachusetts, the November 7, 1988 bulletin permits the buyer to select the jurisdiction. This means that business insurance issued in

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New Hampshire by a New Hampshire corporation, for example, could select New Hampshire for its situs.

What happens with riders under the regulation? The Massachusetts Insurance Department has determined that the policy and rider are not separate contracts. That's the bad news. The good news is that if a change to a rider is a renewal by agreement, then the rider must be unisexed, but the base policy doesn't. The logic here is that the base policy premium doesn't change, so there's no renewal by agreement to the base policy. However, there is a policy change, as defined in Section 3505, paragraph two, which requires only the item which is changing, that is the rider, to be unisexed. The same logic applies to rider addition. The new rider must be unisexed. However, the base policy is unaffected.

Roughly, the same logic can be applied to most other contractual changes. First you determine whether the contractual change is a renewal by agreement. If it is, then the entire policy must be unisexed. If it's not a renewal by agreement and it is a change which is not predetermined from the terms and conditions of the old policy, then only the isolated change must be unisexed, as required in Section 3505, paragraph two. An exception to this general logic occurs when the application of the regulation would otherwise abrogate a guaranteed right under the policy. In that situation, if it's more favorable, the biased provision must be retained. The regulatory logic, as it applies to the following contractual changes, as well as others not listed, is contained in the November 7, 1988 interpretive bulletin: contractually guaranteed maximums and minimums, reinstatements, attained age term conversion, changes predetermined by policy, change in face amount, and nonforfeiture options. The general rule is that renewal by agreement requires that the entire policy be unisexed, and a section 3505 "change" requires only that the changed terms be unisexed.

The last item I want to share with you is the final section of the Massachusetts regulation. It's called the severability provision. This is one I referred to earlier as the regulatory equivalent of the multiple warhead. The section reads, "If any section of Volume 211, Commonwealth of Massachusetts Regulation 35 is held invalid by the court, the remainder shall not be affected thereby."

MS. BARBARA J. LAUTZENHEISER: One of the interesting things about all of these unisex issues is, as Klaus indicates, you end up practicing being an attorney at the same time you practice being an actuary because you have to keep interpreting everything that is occurring while trying to see all the legal ramifications.

I'll start with a comment on the severability issue. I believe that is a common clause in a lot of regulations simply because they want to make sure that they don't end up losing the entire regulation, or even more significant, the unisex issue. This is particularly true in Massachusetts because of the challenges that have occurred there.

Massachusetts is, in some respects, an example of what *could* happen. I don't think it's an example of what *would* happen in other states. In some respects it has some unique characteristics that I don't think will ever happen elsewhere. It clearly is the worst scenario that we have across the U.S. right now. Worst, why? Mainly because of the retroactivity portions of it. I do believe that is unique to Massachusetts. Usually, the retroactive portions are blanket retroactivity as opposed to this discretionary retroactivity with these new definitions of "renewal by agreement" and policy changes, which is language that was just created in Massachusetts.

The only way the retroactivity seems to occur in legislation has to do with it saying it's applicable to all policies as opposed to being applicable to policies issued after a certain date. We've been able to legislatively defeat all of those things that are applicable to all policies because of total impairment of contract. No other state has gone to the extensive efforts that Massachusetts people have in order to apply as much retroactivity as they possibly can without creating impairment of contract. I happen to believe they have created some impairment of contract, and I'll touch on that. But anyway, Massachusetts is, as I say, the worst.

The second element of the Massachusetts regulation that I think will not be duplicated elsewhere has to do with the residency requirement. Every other state that is proposing legislation or even regulation talks about contracts issued in the state. This was a unique feature in Massachusetts because, as Klaus indicated, we began with legislation in Massachusetts. There have been some

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extremely zealous people in Massachusetts who want the retroactive features because they think that all elderly women should be getting more pension benefits than they have been getting in the past. They want it applied across the board, retroactively as far as they can make it. We argued, as part of our lobbying on the legislative side, that if the unisex bill were passed, people would go across the state line to purchase their contracts and it would be very easy.

Massachusetts is not that large a state to go into Connecticut, to go into Rhode Island, to go into other states to purchase the contracts. Their solution for that was to base it on residency. That's one of those things where you think you're doing something that is going to be persuasive and in the end it comes back to haunt you.

There are some other pieces that I'm not sure exactly whether they will be carried over -- one having to do with the same ratio of male and female applied to each line, one ratio for life insurance and annuities. The interpretations here have some pieces that I think are going to leave the insurance industry extremely vulnerable to policyholder suits; not even in the next year, but possibly over a lifetime basis. For instance, if a CPI rider doesn't specifically state the premiums, they are not determinable by the policy. This could be interpreted as triggering a change.

The term conversion aspects of this may also be a problem -- premiums have to be determinable by the contract, and most term conversion riders or term conversion provisions are based upon the policies either at original issue age or at attained issue age, but they do not indicate the actual premiums. It's premiums for contracts then being issued.

Now, if it's a health contract where you have rate filings, it may be that it doesn't get unisexed, but where you don't have rate filings for life insurance, you could end up with an interpretation of the term contract having to be unisexed at time of conversion. And it's quite possible that some female who has purchased a rather large contract, wanting to convert a rider or a policy sometime out into the future, assuming everything is still okay, ends up having to buy a unisex policy at a significantly higher rate, sues the company and sues the Massachusetts Insurance Department.

In spite of the fact that the regulation has interpretations saying what the regulation means, it is not a law. It is a regulation. It is subject to interpretation and is subject to suit by policyholders. We get caught between a rock and a hard place. I don't know what we do about that, other than go back at time of suit and rely on the fact that the regulators said we had to do that, but it does leave us very vulnerable.

There are two court cases still pending in Massachusetts: one has to do with insurance companies saying that the commissioner did not have regulatory authority to do this, and another one of the suits has to do with impairment of contract created by the regulation. I do know there are some companies' contracts, for instance, that specifically define the class as being the gender, and so now, as these are changed, it says that mortality charges will be made within the same class, and then that class is changed by the Insurance Department. Again, it leaves it open for impairment of that contract. It will end up on the court scene with some decisions, but neither of those two court cases is moving at this point in time.

The next state which I will review is Pennsylvania. As you may know, the Pennsylvania case started actually with the opposite sex bringing it in the *Bartholomew* case. The parents of a young male argued that it was not fair under the Pennsylvania ERA that their son had to pay higher rates for his automobile insurance.

Legislation was passed through many struggles. The governor vetoed the legislation, but the legislature overrode the governor's veto. We went to the legislature to get legislation back in to say that the ERA could not be interpreted that way or should not be interpreted that way. It was taken to court again and now it's in front of the Supreme Court, has been heard, but there has been no decision as to whether or not that law that we got passed trying to clarify the ERA is unconstitutional under the ERA.

The Insurance Department had required that automobile rates be unisexed by March 15, 1989 and the Supreme Court chose not to rule prior to March 15, so those rates are, right now, out there being increased. There are complaints coming from policyholders because of those premium increases, but, as you know, automobile insurance is renewed on either a six-month or a yearly basis, so the complaints are spread out over Pennsylvania, not creating enough of a thrust to give

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us any kind of media attention to be able to bring this to the attention of legislators or the public. There's been some thrust to try and actually pass a resolution in the legislature about the economic disadvantages created by that, as well as on the life and health side, to see if we can develop some media attention, but we haven't been too successful in getting a sponsor for that legislation either.

When all of this started, the life and health industry did one of the things I think they shouldn't do. The lesson I thought we had learned at the federal level on unisex is the industry has to stay together. The life and health industry people said that this was a property/casualty problem. They didn't want their hands dirtied by the property/casualty issue and, lo and behold, we now have a regulation coming out of the Pennsylvania Insurance Department which, just as the Massachusetts regulation, comes out stronger than any legislation would and clearly is saying that it is necessary, under the ERA, to have unisex rates between men and women.

There are some additional pieces there as well. As Klaus indicated, there's been an interpretation in the Massachusetts regulation having to do with the utilization of tables, that you can't use build and blood pressure tables. The Pennsylvania regulation is very clear and says you cannot use build and blood pressure tables. The Pennsylvania regulation is also very clear and distinct on the fact that you have to treat pregnancy like any other sickness or illness. It is also very clear on the fact that you can't use any male or female ratio in determining the percentage for a group rate. You have to be sex blind in determining that rate. You don't even come up with a table, and I know exactly how you implement that. They just say you cannot determine the proportion of male or female in the group rate, nor can you deny coverage based upon a male or female proportion.

As best I read this, they're also being a bit sneaky in Pennsylvania because I think it reads that now not only are they requiring unisex rates and no distinction on marital status, but they are also requiring nonforfeiture benefits to be on a smoker/nonsmoker table as opposed to a smoker/non-smoker flat or blended table. So I think they've added one piece that none of us even thought about or looked into as of this regulation, or at least I was not aware of being in the prior regulation. So this is another one of those things that just kind of keep adding things on, and you get the opportunity to work at it.

Regulations are the worst to deal with for a couple of reasons. The only way you can challenge regulations are through the court system, and we have much more difficulty controlling it in a court environment than we have in a legislative environment. Many times it hinges upon law and how law is interpreted. For instance, the real thrust that is being used in Massachusetts on the ACLI and LIAM court case has to do with the regulatory authority. It has nothing to do with the substance of the issue, so we, as actuaries, get very, very frustrated that we never get to the substance of the issue and the real concerns that I have about solvency and equitable pricing because we're dealing in a legal environment that restricts how you can do that and what you ought to be doing on that. We also, in the regulations, end up with some things that are more unreasonable and need a lot more interpretation.

Fortunately, the activity in other states has not been on a regulatory level. It has been on a legislative level. There are some who fear we might have a much larger thrust this year. There is some rumor of that at a legislative level. That has not occurred, by and large, on a yearly basis. We have had from eight to twelve states that have looked at unisex legislation. That has been the case this year. We've had around eight or nine. I was told eight, and when I counted them, it came out nine, so I'll give you your choice on that.

Kansas and Washington proposed legislation that really didn't go anywhere. Kansas had a hearing that seemed to be nothing more than an accommodation to National Organization of Women (NOW) because the sponsor of the legislation was about the only one at the hearing and didn't even seem too interested. It died in committee and legislature session has closed, so there's no real threat in Kansas or in the state of Washington. New York yearly proposes legislation which doesn't look like it's going anywhere. Those are always dangers because you make an assumption that it's just another year, another legislative issue that probably won't come up and then the legislations could spring up on you. We really don't think there's anything there. Rhode Island is technically alive, but not really alive.

Illinois had a hearing, and I understand that for the first time it was a real hearing where the proponents actually listened to the other side. That's deemed to be a positive, but we suspect

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nothing will happen in Illinois because Illinois is having its own political problems. It has had a change in the leadership. This is a partisan issue in most states. There are 38 Republicans and 41 Democrats, but two of these 41 Democrats are not liking what the Democrats are doing, so they're voting as Republicans, so they have a legislature that is 40-41 and everything is just sort of immobilized. So we are under the assumption that unisex will be immobilized in Illinois as well, so it's essentially dead there as well.

Massachusetts, as it always does every year, has legislation of different kinds. Massachusetts is like a volcano. You just sort of watch for it to erupt and then see what happens. Vermont legislated an interim study. There is some threat that it will, as a result of that study, have some legislation next year, but nothing this year. Minnesota is talking about such legislation, but has not yet done it. The two states where we had real activity this year were Oregon and Iowa; Iowa more severe than Oregon.

I'll start with Oregon. The reasons for Oregon were twofold. One was that it was backed by the Insurance Department. The second reason was that Commissioner Andrea Bennett of Montana, for some reason that I haven't been able to determine yet and I haven't heard anyone else has been able to determine yet, has taken up this issue and is literally going around the country talking about the unisex issue. If I have to guess correctly, she is looking for national visibility for some reason. What that reason is, I have no idea, but she was not that interested some time back. Suddenly she's very interested and, as I say, nationally going around the country talking about it; she was talking about it in Iowa, for instance, but she's up there in the northwest and it had a bigger impact in Oregon.

Additionally, as Dave Carpenter mentioned in the General Session, Proposition 103 is having its impact on life and health insurance companies across the U.S. as well. The very bad public relations that have come out from property and casualty companies is impacting us, and it makes it difficult then to talk about anything that you say isn't good for the policyholder, because the proponents just come back and indicate a mistrust.

There was also a change -- again, a bipartisan problem in Oregon -- of a heavier Democratic representation within both houses in Oregon. The person on the committee who had been our swing vote two years ago (Oregon is a two-year session) had moved over to another committee. So we were really quite concerned in Oregon about loss of the unisex issue. Fortunately, we were able to get another swing vote on that committee to agree with our position, so it was stopped in committee. One of the pluses in Oregon is there's a sense that the legislators are getting tired of hearing this issue and they're hoping that this is a watershed year, but if they get it resolved this year, it will not come up again for two years.

Iowa, the other state where there is a lot of activity, was even hotter. It had, much like Massachusetts had, a zealot in the legislature who was very much pro-unisex, did not care what arguments you used. It was an equal opportunity concept and it was the principle of the thing, having nothing to do with money. Her name was Nannette Doder and she was chair of the committee that handled all insurance issues. Nannette literally held all of the insurance bills the insurance industry wanted passed hostage in order to try and get the unisex bill passed. Our greatest argument in Iowa was that the governor in Iowa was wanting to encourage insurance companies, as well as other industry, to relocate in Iowa and one of the arguments they used was that having a unisex legislation there is not exactly going to be encouraging for companies to domicile themselves in Iowa. That did give us some help. Nonetheless, Nannette gave up on auto, gave up on life insurance, but brought up a health bill covering health policies and disability income; was pressing for that when, again, the argument that I just shared with you, that it would discourage companies from coming into the state, caused that bill to be killed in the Senate.

So we kind of sat back and thought everything was fine, and all of the sudden one Friday afternoon an amendment which required unisex came up to the Insurance Department Commissioner's budget appropriations bill. So now the insurance commissioner was not going to get his budget for the next year unless unisex was passed. So, once again, we began a lobbying campaign. And to give you some idea of how much fun it is to be a lobbyist on one of these things, the 7th of May, a Sunday, at four o'clock in the morning, the legislative session closed. Unisex was still an open issue between 3:30 in the morning and four o'clock in the morning. We finally won our battle, but by the time it was over, there had been trading on such critical issues as interstate

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banking and riverboat gambling. Nannette gave up her vote for riverboat gambling. One of those interesting things that happens!

I liken this to the fact that when you really deal with legislatures, it reminds me of when I was a child. I guess Dave Carpenter also said this. We go back to kindergarten principles. Remember when you traded baseball cards and marbles and jacks and Barbie doll clothes and all those things? That's the same kind of trading that goes on in a legislative arena late at night or early in the morning, depending on how you happen to look at four o'clock in the morning, but it's kind of fun. But we had won in Iowa. The problem of Iowa is that in that "win," it was only a battle we won. We did not win the war. There were lots of promises, we suspect, made to Nannette, which she will hold those people to who made those promises, so we're going to have to make a dramatic effort right now to keep the issue contained in Iowa for next year.

The final state I want to talk about is Montana. Again, with Commissioner Bennett talking across the U.S. about Montana, it's important to do so. Once again this year, we attempted to repeal the legislation, the unisex legislation on the books, which is by state of issue and not residency and is prospective, not retroactive. We really didn't think we were going to have as much difficulty. We thought it was a real shoo-in in the Senate and had started in the Senate to get the repeal. We went out, had the hearings, everything looked great and suddenly, overnight, it turned on us again and we lost the Senate vote, which meant the whole thing was over for two more years in Montana. So the bill stays on the books in Montana. Andrea Bennett, not trusting the prior commissioner's Montana study and not trusting an industry study, did her own study about the impact of unisex in Montana, because she also sensed that there may have been some changes that had to do with inflation and other things not unisexed, but the way she did it was to compare Montana rates and values with Idaho rates and values. Well, if you take a look at the results of Andrea Bennett's study, she indicates what we had told her was going to happen, and that is the term life rates for females were 10-32% greater in Montana than they are in Idaho and the male rates dropped by only 2%.

Under a whole life contract, the premiums are 10-19% lower for females. She argues that the cash values, however, were smaller, even though the premiums were less. She fails to point out that when you do a simple additional calculation, not even including the time value of money, the difference in cash values was nowhere near the increase in premiums that you had to pay over a ten-year period.

But she is quoted in the *Iowa Register* as saying that the unisex bill works fine. Now, I guess I ask, "Who does it work fine for?" It doesn't work fine in my estimation for a woman, I don't think it works fine for an actuary, and I don't think it works fine for an insurance executive. It may work fine for men; it created a slight decrease in the premiums, but it may work fine for Andrea Bennett who wants to talk about it.

What conclusions can we draw from this? Well, the one that is still most encouraging to me is that we're not seeing an increase in the number of states that are taking up the issue. We are able to contain the issue when we can do it at a legislative level and really talk to legislators about common sense. When we have an insurance department that is proposing regulations and we have to take it into a court system and play a different battle, we have more difficulty. But if we aren't working for systems, we continue to work on the issue. We seem to be successful. The discouraging part of that is that "it ain't over until it's over," literally until four o'clock in the morning some places.

I began this issue 20 years ago as a naive actuary (I was even young then), and I said I'd like to win this issue. If we could just get this information out there, we'd win the issue. I had to finally redefine success to mean we won't lose the issue because it's 20 years later and we are still dealing with it. So it is a political game and you have to keep playing it. The concept of political aspects is the second thing that I think is important for actuaries to remember. And that is that our actuarial tools, our ability to help with the solvency of a company or our ability to have equitable and fair pricing is being driven by political concerns, not by logical concerns. That's a very tough thing for most actuaries, including myself, to swallow. I accept it as real. I still don't think it is right, but I do recognize that it is real.

That is particularly disturbing to me because I am a firm believer, as a result of the kinds of contracts that we are developing -- interest-sensitive contracts and different designs, and

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particularly the AIDS issue which is impacting companies so differently company by company -- that we have to move toward a valuation actuary kind of reserving and pricing structure based on the judgment of the actuary. We have regulations and legislation which are prohibiting our best tools for determining what the real reserves and prices should be. We should be relying on our professional judgment. It is putting us, again, in a box where our liability is increasing, but our ability to actually predict those best estimates is being restricted. So we're getting put in a vise on that and that is extremely disturbing to me, because we should be using more of our professional judgment, standing up more and having better tools, not lesser tools, with which to do this.

The third conclusion is that you can't sit back and say it's all going to be okay because logic will prevail. It is not a logical concern. It is a political concern and you need to become active on these issues within your own state and help explain what insurance is about, that it's spread to the risk, and why this classification is necessary. Otherwise your tools are going to be lost, and you're going to be put into this box without the tools to fulfill that liability and responsibility that you need to do.

One final note in conclusion. For those of you who still say, "Well, somebody else will take care of this and it's not really this big an issue and unisex will probably go away and we've won on AIDS and it's all going to get better and I don't really need to worry about this," I'm going to once again talk about the domino effect I've been talking about for 20 years. I really do believe that this is just another step and a risk classification, and probably now even a socialization concern. Unisex was the first. AIDS was the second. And believe it or not, uni-age is the third.

How many of you are aware that there is a uni-age law on the books? March 20, 1989, the state of Arkansas passed a law saying that all premiums for Medicare supplement contracts had to be the same regardless of age. They call it Comprehensive Rating. They haven't called it uni-age. It is uni-age because regardless of your age above age 65, you have to have the same premium and in addition to that, you cannot deny coverage based on age. So if someone finally can afford it at age 100 and comes in and wants to buy Medicare supplement insurance at age 100, they will get a rate based on the premiums for ages 65 and above. This is on the books in Arkansas. It's being proposed by regulation in the state of Washington. It may be a single state, it may get changed, but I have to tell you it is being driven by the American Association of Retired Persons (AARP) and if you begin to look at those issues, insurance issues that are being lobbied and monitored by AARP, they are not just those issues above age 65. They are all life insurance issues because AARP is moving down in its target markets below age 65. I know it's down to age 50. I think it may even be down to age 45. The elderly are a very heavy driving force, and you are naive if you think uni-age is not a threat.

The bottom line of all of that is we are moving, more and more, toward a socialization of insurance with one rate for all. That is very scary to me, particularly scary as an actuary, because it can cause elimination of the voluntary insurance market. So, there they are and it's fun. Get involved. Start learning how to not just react to what happens to you on a legislative front, but to be pro-active on that legislative front because you're going to have to live with whatever happens.

MR. DESROCHERS: Over the last year or so, since the Massachusetts regulation has become effective, we've seen in our consulting practice an increasing development of unisex versions of plans. What will typically happen is that while we're developing a product for countrywide distribution, once the product is designed and the rates and values are set for the sex distinct version, we will develop a unisex version of the plan -- usually for use in Massachusetts and Montana. This is the way, in practice, that companies are dealing with unisex. Those companies who want to sell in the Massachusetts market are "unisexing" their plans.

We recently completed a last-to-die plan sold primarily in the estate planning market and, in fact, we developed a unisex version. In filing the plan for approval in Massachusetts, we started with two unisex persons rather than one male and one female. As you might expect, although it started on a different basis, the rates for a male and female came out in about the same place as they would have in the sex-distinct version.

Before the Massachusetts regulation, the experience that we had in unisex was primarily in those markets that were payroll deduction markets or markets that were employer/employee driven, where there is more control over mix of business. What I'd like to do is share with you a very simplified pricing exercise, one that is typical of the development of unisex variations. The theme

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of the presentation is that unisex, in fact, adds an additional risk factor to pricing -- failure to achieve the target mix of males and females assumed in pricing.

One of the difficulties that we face in developing unisex plans is that we're giving away some of our ability to underwrite products -- at the same time that underwriting is becoming a much more important competitive issue. What I'll be doing is presenting the pricing dynamics of a sample UL plan. In preparing for the preparation, we took a sex distinct plan that we had developed and developed a unisex variation.

We tried to keep it simple and, at the same time, make a couple of specific points. In our product design, we've targeted a 50/50 male and female mix. In many companies, this is somewhat unrealistic. We've also kept it simple in the sense that we've run our model as consisting of a male and female, age 45. The analysis would normally be quite a bit more sophisticated.

The plan has been analyzed using what we call both macro and micro analysis techniques. The micro analysis measures cell-based profitability (Table 1). The goal in performing micro-profit studies is to look at product balance -- how the product performs on a cell-by-cell basis. We have measured a number of things for this product. We looked first at the individual cell profitability for each thousand dollars of insurance issued over a 20-year period. In the analysis, we calculated a number of profit measures typical of traditional pricing analysis: 1) internal rate of return or the return on invested surplus; 2) present value of book profits for each thousand issued; 3) the break-even year, which is a measure of the point in time at which surplus turns positive. We have also presented a couple of other things for comparison. One is the present value of book profit as percent of premium, and the second is a measure that I find quite interesting in this type of analysis -- what the present value of claims would be as a percentage of premium.

TABLE 1

MICRO ANALYSIS -- NEW ISSUE 7/89
PROFITABILITY STATISTICS

	<u>Male</u>	<u>Female</u>	<u>Difference</u>
IRR	11.65%	14.88%	-3.23%
PVBP*	0.0781	2.475	-2.397
BEY	11	10	
% Prem:PVBP	1.27%	4.02%	-2.75%
% Prem:CLMS	22.31%	17.74%	4.58%

* Per \$1,000 face issued.

We examined each of our two pricing cells to see on an individual basis what the pricing dynamics of that cell was. Although we have unisex rates, pricing is measured on a sex distinct basis -- we do not price with unisex tables. Let's look for a moment at what the results of these products are. The products have some specific differences in the pricing assumptions even though they have the same cost of insurance (COI) scales and the same expenses for male and female.

I'll review some of the key characteristics and make some comments on them. Obviously, as you'd expect, there are higher profits on virtually any measure for the business sold to females than for that sold to males. There is a significant difference in the present value of profits, where we're looking at about eight cents a thousand for males and about two dollars and fifty cents for females. Present value of profit as a percent of premium is about 1.3% for males and (after tax) about 4% for females. Finally, there is a fairly significant difference in the claim costs. The cost for males is 22.3% of premium. This measure is based on the present value of death claims over 20 years discounted back to issue and divided by the present value of premiums.

In these micro studies or in these cell-based studies, it's very clear we have a product that has a built in subsidy of the male rates by the females. I'd also point out there is something else which may or may not be true about a product that's priced on a unisex basis. This particular plan was heavily loaded toward expense. It's a front-end load product, and it derives a significant amount of its profitability through expense loads. In the pricing assumptions we used, I don't believe that the male and female mortality assumption is as extreme as it is in some cases. In the sample plan,

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whether we sell it to a male or whether we sell it to a female for these particular cells, it is profitable to some degree. This is not always true.

There are some product designs where the male profitability is negative and it's offset by higher female profitability. Some of the analysis that follows from this particular product is a function of the product itself. That is, when it's sold to males, there is some positive profit. This is a good idea for a unisex product -- that there should be, at least on some measure, a positive profit from the males.

After we have completed our micro analysis, which is really an analysis based upon individual cell profitability, the next step would be to look at what happens to the block of business as a whole. Although we're concerned about product balance and it helps us to know the individual cell profitability of the males and females, what we really do is sell business in its entirety as a block of business.

Our next step was to assemble a model office assuming that the company would sell one hundred million of face and about a million of premium of this plan. We want to measure the financial effect to the company issuing this block of business. We would typically measure financial effect not only in terms of the profitability measures that I discussed before -- the internal rate of return, present value of profit as percent of premium -- but we'd also focus on what the block of business might be worth in terms of the present value of book profit. This is similar to the value we were to appraise that block of business or to attempt to sell it to another carrier. Another way to view this measure is as the "value-added" or the discounted value of the 20-year profits. We would use that measure to look not only at the profit that arises from that hundred million of issues, but also to see what might happen to the company under alternative distribution scenarios.

If the product were extremely competitive as a result of assuming that we had a 50% male and female mix, we would need to look not only at unit profit but also at what happens in terms of market share. I believe that price is a function not only of unit-profit, but it's also a function of demand.

We've used the macro analysis to look at two things: what is that block of business worth and what might happen to us in a competitive environment from having a product that had, in effect, more of a subsidy of one class by the other because of our expected distribution of sales? For the first step, having looked at the cell profitability, we built a series of model offices and we looked at what happens: 1) if we achieve our target mix of business and 2) if, as a result of the competitive positioning of the product, we sell larger percentages to males than we had expected.

I'd like to look at some of the profit measures and see how profitability changes in a way that's beyond our original pricing (Table 2). When we priced this on a sex distinct basis, if we achieved balance in the male and female rates, we didn't have to worry about this distribution mix. But now that we have a subsidy of the males by the females, we need to be concerned that we sell enough female business to achieve our original target objective. As we move from a distribution of 50% male, 50% female, as we expected, to a distribution of 90% male, we see that all of our profit measures fall off quite dramatically. In fact, the rate of return drops from 13.3% to about 12%. Present value of book profit drops from \$162,000 to about \$95,000; about a 40% drop. Our break-even year moves up a year. The present value of profits drops from 2.5% to 1.5% and the claims as a percent of premium, as you'd expect, increase from 20% to about 22%.

TABLE 2
MACRO ANALYSIS -- NEW ISSUE 7/89
PROFITABILITY STATISTICS -- % MALES

	<u>50%</u>	<u>60%</u>	<u>75%</u>	<u>90%</u>
IRR	13.31%	12.98%	12.49%	11.99%
PVBP*	162.83	145.89	120.48	95.07
BEY	10	11	11	11
% Prem:PVBP	2.47%	2.37%	1.96%	1.55%
% Prem:CLMS	20.02%	20.48%	21.17%	21.86%

* Per \$100 million face issued; amounts in \$1,000s.

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So what we're dealing with here is a situation in which, as we move away from the distribution that we expected, profit is impaired as compared to our objective.

This leads to the second part of the analysis -- what can be done if this is occurring in a block of business. If your profit goal was 2.5% of premium after tax, and again that's a very thin profit goal, you would have, by moving to a 90% male distribution, considerably missed your profit objective. The problem is that price is subject to the marketplace, and having assumed a distribution of 50% females makes the rates look very attractive to the subsidized class, in this case the males.

If we assume that our goal is to maximize the present value of profit for a particular block of business, we can look at the change in mix of business in a positive light. If our intent is to develop as much profit as we can, we can also look at the effect on the company of producing additional business. A result of having a very competitive product might be an increase in market share. If our intent here was to maximize the value of the company, we can determine the increase in market share which would be required to give us that same present value of profit as would have occurred had we sold the original volume to the target mix of males and females.

That is, we can chart how much additional production we would need to produce, on a present value basis, the same profit for that block of business (Graph 1). This would be a "marginal value added" analysis. If we were dealing here with marginal costs, then we could argue that we can either achieve our target profitability by selling the same mix of business or, as an alternative, selling more business that is more heavily oriented toward the subsidized class. The analysis shows, however, there would need to be a tremendous amount of elasticity of demand as you move to a 90% male distribution, so this may or may not be a good strategy -- it may or may not prove to make sense financially.

As we moved from a 50% male distribution to a 70% male distribution, we would need to sell 30% more business to have the same equivalent value. If your distribution system, as a result of any price advantage to males, was not able to deliver that much more additional production, then you would conclude that you were losing more from the change in business mix than you were gaining in additional production. Our analysis indicates that you'd have to achieve 70% more in sales to break even on 90% males.

This type of approach shows that there really are two ways to deal with the mix of business. The first way is obviously to attain your target mix. The second way is, if you're looking at the marginal value that would be added to your company, then it may make sense to justify a more aggressive price structure if you were able to sell more business. In many cases, however, distribution systems are not that elastic. Over a period of time you would still have to sustain that increase in production to be in the same position.

Having looked at pricing at issue of the policies, we also tried to look at what might happen if, two years after issue we decided that we were not achieving our target mix and that, in fact, we were going to reprice the business as a result of not achieving the target mix.

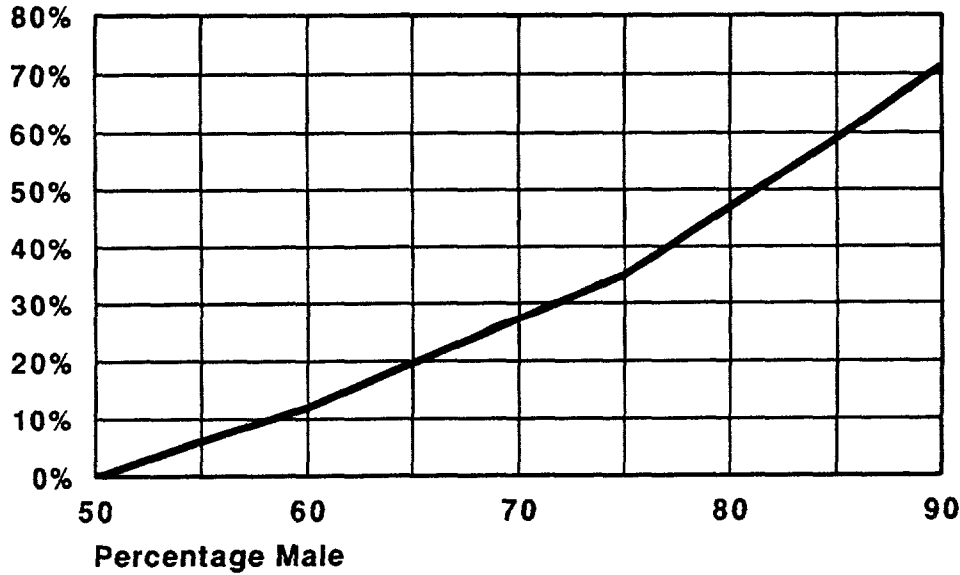
Our analytical technique was to determine the value of the business. What is the in-force profitability two years after issue? And then let's look, as an example, at a 10% increase in the cost of insurance (COI) to see how that would affect the profitability and to judge from that how much we would have to increase the COI to cover the additional mix of business. Our approach is similar to what many states require for repricing indeterminate premium products and that's that we cannot recoup any past losses, but what we can do is set the COI such that our expectation of future profits is the same as our expectation would have been had we achieved our target mix of business.

The first part of our exercise was to go through and appraise the block of business to determine what the present value of profits would be, in July 1991, under the original pricing assumptions, but looking at different mixes of business (Table 3). What we effectively did was an in-force appraisal. Table 3 indicates a fairly high value per unit in-force. The value declines from \$926,000 for that hundred million dollars issued to \$850,000 if our distribution were 90% male. What we would do in practice is to evaluate the actual distribution and determine what the block of business is worth -- what would it be worth on an appraisal basis, what might it be worth if we took it to a reinsurer. We would determine the expected value and compare it with the amount as

UNISEX PRICING STUDIES:

Required Addl.
Production

Macro Analysis
Production v. Mix of Business



PRICING ON A UNISEX BASIS -- CONSIDERATIONS
GRAPH 1

PANEL DISCUSSION

TABLE 3

MACRO ANALYSIS -- IN-FORCE 7/91
PROFITABILITY STATISTICS -- % MALE

	<u>50%</u>	<u>60%</u>	<u>75%</u>	<u>90%</u>
PVBP *	926.11	907.48	879.54	851.59
%Prem:PB*P	17.34%	16.70%	16.48%	15.97%
%Prem:CLMS	26.37%	26.97%	27.87%	28.76%

* Per \$100 million face issued; amounts in \$1,000s.

it actually emerged. We then would change the COI scale in such a way that we would end up with equivalent present values.

In this case, we ran the same model office as we did for the original issues, but we increased the COI on a prospective basis after the second year by 10% (Table 4). As a result, the present value of profits has increased -- in fact, it's increased by somewhat more than the difference between what we would expect from a 90% block of business and what we would have expected from a 50% block.

TABLE 4

MACRO ANALYSIS -- IN-FORCE 7/91 (+ 10% COI)
PROFITABILITY STATISTICS -- % MALE

	<u>50%</u>	<u>60%</u>	<u>75%</u>	<u>90%</u>
PVBP*		1,097.98	1,069.52	1,041.08
% Prem:PVBP		20.57%	20.04%	19.52%
% Prem:CLMS		26.97%	27.87%	28.76%
Required COI Increase for Equal Profitability				4.00%

* Per \$100 million face issued; amounts in \$1,000s.

We next determined what we felt the equivalent increase in COI would be for an actual mix of business that was 90% male. We would need to increase the COI by about 4% prospectively to have the same prospective value of profits. Now, there are couple of things that I should say about the analysis. One is that, as I mentioned earlier, this product is not heavily dependent on the COI for profit so that a great deal of its profitability comes from other sources. In other products, we might in fact find that there would be a higher COI rate.

The second is also an important phenomenon -- that although we were getting reduced profitability for the males, we were not in a position where we were losing money on males. Had the product been structured somewhat differently, we could very well have found that the required increase in the COI was higher or even unattainable as a result of the guarantees that we made.

One needs to be very careful in pricing unisex products; some provision should be made for sensitivity testing on changes in the mix of business. From the example that we put together, I think we can generalize some things, but there are many situations where it would not come out as simply or easily in practice as has come out in our simple example.

What I'd like to do now is just share some thoughts on the unisex pricing dilemma. Clearly the examples indicate that on a micro basis or on an individual cell basis, the plans lack balance by cell. Product balance occurs when the expected profits for each of the cells are similar.

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What we're able to do by balancing a product is minimize the distribution of business risk. In pricing a flexible premium plan we minimize the risk on different premium patterns so that we can't be selected against with certain premium patterns.

On unisex we cannot really balance our products in such a way that this male-female subsidy will never occur. It is, in my judgment, becoming a fact in the market, particularly for companies that don't have captive distribution systems, that products are increasingly subject to analysis by spread sheet. With personal computers and a little bit of diligence, it's very easy for an agent to pick out your pricing mistakes. It's very easy for an agent to find those cells and those products that are very favorable to their clients. To counter this we attempt to achieve as much balance as we can in our pricing. The unisex area is one where we really cannot achieve that balance because of regulatory constraints.

The second comment I'd like to make is the greater the male-female subsidy, the more attractive the product is to the subsidized class. If you assume a 50/50 mix, as we did in our example, obviously that product is going to look much more attractive to the subsidized class, who in this case are males, than it would be had you assumed a 90/10 distribution. The more you subsidize, the more that you should sell to the class you're subsidizing. It seems to be a fairly basic economic principle. As a result, it may be very difficult to achieve the pricing targets. In a competitive market, it may be almost impossible to attain your target mix by anything except some inelasticity of distribution or very strong control of a distribution system.

Another way that one could argue that you can achieve your pricing targets is by increasing market share. If, as a result of the subsidy, you are able to increase your market share on a permanent basis, then that may be an alternative for the target mix. It seems apparent, however, that any increase in market share is going to be, by its very nature, temporary. If your initial pricing assumption is that you'd achieve a 50/50 mix and you achieve more like a 90/10 mix, then when you do your next product, it's going to be very difficult to have that same 50/50 assumption.

The other alternative may be to raise prices for the in-force business. In our example where we did raise the prices, we made a couple of fairly critical assumptions. The first was that we would not, as a result of raising prices, have a significant impact on the future lapses. Were we actually to price the product for other than a simple example, we would obviously want to also increase our lapse rates. I think increasing COI rates on in-force business also has a negative impact on the distribution system. It has a negative impact on customers and overall may have a detrimental effect on the block of business. So for the unisex product, one of the dilemmas is that it may be, over a long period of time, very difficult to achieve the pricing target that you're looking for.

With respect to the targeted mix, if you assume that there is too much of the underpriced class, if you expect that you'll sell 90-95% males, then you may find yourself in a competitive disadvantage with a company that assumes a different mix or that perhaps even expects that it will sell more like 60/40 or 50/50. And so even if your pricing is right on and even if your target mix is attained, you may find yourself in a competitive environment having a price disadvantage because you don't have enough subsidy.

I mentioned earlier that raising prices may have a marketing disadvantage because what you're doing is effectively reducing expected policyholder values. It's a very difficult decision to reduce dividends or to increase COI charges because you made illustrations on a certain basis and now you're reducing expected values. I would conclude from all of this that unisex pricing leads to higher overall prices; that, in fact, by introducing the subsidy, by introducing the risk in mix of business, that, by its very nature, by taking on this additional risk, it's something that the insurance companies ought to be compensated for. So while it may change the distribution of who pays in the aggregate, unisex pricing should, by its very nature, lead to higher overall prices.

I also believe that it is a very significant issue that we lose the right to underwrite. The life insurance market is moving very definitely toward more underwriting as a response to pressure on prices and profits. We've certainly seen this in response to AIDS. If we look at the market now, blood is taken usually at a \$100,000 level for most companies; it may even be lower in some cases. Preferred risk with build requirements and blood pressure requirements is a phenomenon that we saw in the term marketplace over the last few years and we'll see increasingly in the UL market. It is unfortunate that at the same time that the industry is trying to produce good consumer values

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and good returns for its owners through more selective underwriting, we're also fighting this battle against its loss of ability to underwrite.

I would like to close by saying that, as you are pricing, it's important that this mix of business risk be recognized. It's important that the products just not be taken in their sex-distinct form and quickly changed to unisex basis, because there is additional risk and it's risk that should be recognized in pricing.

MS. LAUTZENHEISER: Chris has really articulated very well some of the concerns that we also had on the unisex issue having to do with the impact on insurance companies that are lobbying. We did not discuss this because it gets to be rather complicated, but I think that concern about the competitive environment was as much a concern as the ability to do the underwriting. There are companies whose total marketplace does not drive toward the female population. For instance, the small business owners. There is still a significantly smaller percentage of females buying those business policies than there are males, and when you try to create a premium pricing that shows 90% male and 10% female, you look noncompetitive on the unisex issue compared to someone whose current distribution allows that to be at a 50/50 level.

You also have a problem in Massachusetts of not being able to vary the percentage by product -- that you have a product that is being targeted towards a business market where it may be 90/10 and another product that is targeted towards the female market where it may be more 50/50. You're going to have to decide which of those two products you want to sell most and come up with the ratio that represents that and then work from there, and one of those is going to have its premiums increased.

One of the things that we have discussed and will continue to discuss in the Actuarial Standards Board is cash flow testing. The cash flow testing issue became a critical issue because of investments. It is now also probably a critical issue based on AIDS, because each company (the way they've written business, the kinds of business they have) may require some scenario cash flow testing for AIDS. In unisex states, this is one more reason for cash flow testing or scenario testing because you're going to need to see what happens if they run in one direction or the other. There's never going to be a lack of need for the actuary in this coming environment.

MR. JOHN W. HADLEY: Do you see much chance of Massachusetts attempting to expand its scope to say that changes in credited interest rates might also be considered to be changes that cause the policy to go unisex, or possibly guarantees as to future credited interest rates either by rider or by administrative liberalization?

MR. SHIGLEY: No, I think the regulation is pretty clear that what triggers the retroactive application of unisex is changing premium for traditional products and then changing in the schedule for non-traditional products. With respect to interest, it does require that the same interest rate be paid to males and females, but I don't see an extension of retroactivity to policies merely because an interest rate is being changed.

MS. LAUTZENHEISER: An additional comment in that regard. Because, again, these are interpretations of the insurance department, I think it could be changed. My guess is if the department people thought they could have done that in the beginning, they would have, so the probability is pretty small.

MR. MICHAEL J. ROSCOE: If there were no threat towards movement away from the ability to do risk classification at all, if we had a perfect environment that allowed the industry to approve any kind of change or else it just didn't apply, what would be your viewpoint towards the unisex rating? It's not likely that you're selected against by the individual based on his or her sex. It's not something he or she can control and without the threat of the removal of risk classification, what would your opinions be?

MS. LAUTZENHEISER: I think it's probably clear what my opinion is. I happen to believe in cost-based pricing. I happen to believe in an additional concern: I don't want the insurance industry to end up where the savings and loan industry ended up and that is in an insolvency basis. And any time we don't consider actual costs, I think we run some risks of not being able to determine, even from a solvency standpoint, what our real risks are. I also believe, as Chris has

PRICING ON A UNISEX BASIS -- CONSIDERATIONS

indicated, that the attitudes of the public are even more "what's in it for me" and "what's it going to cost me" in moving toward preferential risks.

At the same time, we've got a social policy that's going the other way. Given we didn't have that social policy that was trying to push for equal benefits and premiums, we would, in fact, move toward more preferential underwriting over time. People just don't want to pay more than they have to pay. Anyone who can identify yet another risk factor that is going to reduce those costs for one segment of the population will move in that direction.

MR. SHIGLEY: Let me give you the views of the chairman in my company. The view of Jim Morton at John Hancock is that it's a political issue and we're better off working with the politicians to get the kind of regulation, the kind of legislation, that we can live with rather than fighting them and eventually losing the battle by getting the kind of regulation that we have in Massachusetts. It would be good for our public image to start working with the legislature, with consumer groups, to get the right kind of legislation.

MR. DESROCHERS: I see it as a pricing and marketing issue to a great degree -- that companies should have the ability to underwrite to the extent that they wish. If they feel that they can develop a market niche for themselves by being an underwriting company, by having very tight underwriting, and as a result of that, by having competitive price, then they should be allowed to do that. If they believe that there is a market advantage to a unisex type of product, then they should have the right to do that. In a perfect world, a company's pricing decisions would be based on market demand and a company's view of the marketplace.

MS. LAUTZENHEISER: I'm going to make one more prediction: In those states where we have that unisex pricing mandated either by regulation or by legislation, at some point in time, it's going to reverse. The women are going to come back and complain that they are subsidizing the men and there will be a reverse political situation. That has already happened, even on the preferential underwriting. It was not more than ten years ago when people said that they didn't want to be treated by their own individual characteristics and now it's moving toward wanting to be on their own individual characteristics. So, if you follow the political climate, you have to then keep moving with it.

MR. DESROCHERS: With some of the discussion, preferential underwriting is an issue which should be of concern. I'm not sure what a unisex build and blood pressure table looks like, although it certainly might be interesting to put one together. Clearly if you can't make meaningful underwriting differentiation based on the standards that you're allowed, then there's no sense using your standards. So I would be very concerned not only about the effect of the uni-age pricing, but also by the restriction on preferred underwriting, which has become, I think, a critical strategic issue for a number of companies that are increasingly trying to meet their competitive issues and the profitability issues through stricter underwriting and preferred risk plans.

MS. LAUTZENHEISER: I've actually wanted to see if we couldn't use build, in particular, as a surrogate for all of this. Being five foot tall, I think the shorter you are, the lower your premium ought to be.

MR. JOSEPH D. AUSTIN: On the issue of residence, perhaps the producer can contrive to get around the law say by way of trust in Rhode Island or wherever, and that is the only source of business or any way of contact can it be governed by Rhode Island or is it a Massachusetts policy? Secondly, if it is clearly contrived, is there any liability for the company to allow this or how would it interpret the law?

MR. DESROCHERS: It's becoming increasingly difficult to use the trust approach because the states have tended more and more to look through it. There are any number of states now that say even if you're using an out-of-state trust, the fact that the trust is writing policies in the state, then it's subject to regulation. Over the last ten years or so, it's become increasingly difficult to use the trust approach to avoid state regulation and, clearly, I think you would have a liability where you're trying to do that, because the states have not been shy about enforcing their will on people writing business in their state, whether through a trust or directly.

PANEL DISCUSSION

MR. SHIGLEY: The only thing in the regulation itself, in the interpretive bulletin, is that the buyer or the owner of the policy has the right to select the site. I think it also says that the owner has to reside in another state, so I'm not sure how that applies to a situation of a trust. It's hard to know where the trust lives.

MR. STEVEN I. SCHREIBER: I think Barbara has reemphasized the importance of the legislators as opposed to the regulators. I want to know your perceptions as to what any regulators need to be concerned about and second, the concern that, as Klaus pointed out, where we thought we were successful with dealing with the Massachusetts legislators, we ended up having to deal with the regulators afterwards.

MS. LAUTZENHEISER: The Massachusetts situation is unique in and of itself in that the regulators had a zealous drive to do what they needed to do. I'm not sure any legislation that we could have gotten passed would have actually been a plus. Maybe it would have been. We still would have ended up with prospective, maybe not retrospective, but I don't think that stopped the Massachusetts regulators from coming back in and reinterpreting what they wanted to do anyway. They could have done the legislation plus this.

The commissioner that I am concerned about is Andrea Bennett in Montana and any other commissioner who may agree with her. Based on my conversations with the commissioner in Vermont, that may be one problem. They are doing a study and it may stop at a study, but those are things that are difficult to tell.

The best solution to all of this, in my opinion, is to go talk with your state insurance commissioner in the state in which you're domiciled, before it becomes an issue. If you do that on a pro-active basis before it becomes critical, there's not a lot of mistrust. What you really are talking about is how the principles work and you can get your ideas across ahead of time.

We did that, for instance, on AIDS in Maine. They were very concerned in Maine that the groups would continue to drive that, so we held a mini-seminar in Maine and explained it to the legislators, as well as the regulatory people, thereby giving them the facts that they can use to argue against the people who are coming in on the other side. You have to help provide them with the information that they need, so a lot of it has to do with being pro-active, but predicting in advance is a little difficult to do and those commissioners change.