RECORD OF SOCIETY OF ACTUARIES
1989 VOL. 15 NO. 2

THE U.S. REINSURANCE MARKET: VIEWS FROM ABROAD

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o A discussion on the state of the U.S. reinsurance marketplace as viewed by foreign reinsurers and consultants. Panel members will provide insight on the willingness of foreign companies to assume risks from the U.S. marketplace and key factors that enter into this decision. Some of the topics that will be covered include:
- -- General perspective on the marketplace
- -- Perceived profitability and rates of return
- -- AIDS risk
- -- Foreign tax and regulatory issues affecting marketplace
- -- Attractiveness of certain types and methods of reinsurance, e.g., financial versus risk and coinsurance versus modified-coinsurance

MS. SUE ANN COLLINS: Our objective is to provide insight into how foreign companies view various aspects of the U.S. reinsurance marketplace and factors that influence these companies' decisions to assume risks from the U.S. As background I've gathered some information that illustrates the extent to which foreign companies currently operate in the U.S. reinsurance market. These data are limited to ordinary, or conventional, reinsurance and financial reinsurance.

Over the last 10 years the number of companies writing conventional reinsurance in the U.S. has remained relatively constant: 26 in 1978 and 28 in 1988. However, the number of foreign companies has increased from 8 in 1978 to 16 in 1988. For purposes of this discussion, I have used foreign to mean either companies with non-U.S. parents or non-U.S. companies. Canadian companies also have been classified as foreign.

A number of domestic companies either withdrew from the conventional reinsurance market or merged with other reinsurers over the period 1978-1988. These included Centennial, INA/CIGNA, Republic and Manhattan Life. Over this same period, several new foreign companies entered the market: Frankona, Hamburg, Hudson, NRG American, and Scor/Optimum. Foreign countries represented in the U.S. reinsurance market, in addition to Canada, include the U.K., West Germany, Switzerland, Sweden, the Netherlands and France.

The amount and percentage of new conventional reinsurance written by foreign companies reached a peak in 1983 and has since declined. The following chart illustrates this:

Conventional Life Reinsurance
New Face Amount Issued
(In $Billions)

Type of Reinsurer	1978	1983	1988**
Foreign	6	64	49
Domestic	14	97	126
Total	20	161	175

**Estimated

* Mr. Taylor-Gooby, not a member of the Society, is a Principal of Tillinghast/Towers Perrin in London, England.

These amounts should be viewed as directionally correct as opposed to absolutely correct. Inaccuracies may exist due to reporting difficulties, e.g., new business, in some cases, may include retrocessions, which means that double counting has occurred. I would like to thank Munich American for providing me with copies of its historical reinsurance surveys. The statistics noted were derived from these surveys.

Moving to U.S. financial reinsurance, there are many companies operating in this market, foreign and domestic. Domestic companies include Alabama Re, Employers Re, General American, Guardian, J.C. Penney, Lincoln National, ITT Lyndon, Security Benefit, and others. Foreign players include Aachen Re, Crown, London Life, Manufacturers, NRG America, Winterthur, World-Wide and others.

I have not addressed foreign companies assuming other types of coverages: A&H, catastrophe, etc., nor those acting as retrocessionaires. There are many examples of foreign companies assuming these types of businesses as well.

MR. PETER JOHN SAVILL: I have a good deal of trepidation in approaching the subject at hand because, quite frankly, I am an amateur when it comes to the technical niceties of the U.S. reinsurance market. My amateurism has, therefore, along with other reasons basically made me refrain from taking any major active participation. That may actually have been my good fortune as it is my understanding that your market has over the past decade suffered considerable reversals at times. I know of many of my European friends in reinsurance who have toyed with the market in the U.S. much to their eventual regret. This brings me to the nub of my opening comment. Why should an offshore U.K. or other non-U.S. domesticated reinsurer be approached in the first place when there are in your territory a considerable number of prestigious, expert domestic companies, the leaders of which are among some of the largest life reinsurers in the world? My parent company has a local presence in both life and casualty reinsurance, and that is another reason why I am not much involved, but I nevertheless agree strongly with the company's rationale. The only way, it seems to me, that you can possibly hope to succeed long term in acquiring sound profitable business is to have a local presence with actuarial, underwriting, marketing and legal expertise capable of understanding and reacting to the problems and opportunities the market has. A nondomestic reinsurer sitting thousands of miles away cannot possibly hope to successfully compete and indeed runs a much higher risk of loss potential. Of course representatives can visit, meet companies, get local professional advice, etc., but I still contend that they cannot hope to have their fingers on the pulse of the market in the way the locals can. Therefore, my first thought is, if you want to make the U.S. market a serious profit center, set up locally, employ local talent and get to know the market in depth. If you do not do this, then you must play very carefully.

I do not want to suggest that there is no place whatsoever for the unlicensed player. There may be situations where serious study suggests opportunities. However, as I have suggested, great care is needed.

I would now like to amplify situations, which we in London have met. The first situation is a negative one: it is where normal treaty risk business is being offered to us for reinsurance where there does not appear to be any U.S. domestic reinsurer involved. A London broker comes into our office with the opening statement, "I have this contact in the United States, and I have this wonderful opportunity to write a large volume of U.S. business on attractive terms. I have selected your company as the ideal reinsurer, and I am sure you will appreciate the vast profit potential involved." He dumps, perhaps 100 pages of an actuarial report, complete with masses of computer projections incorporating a new business prognosis of which the largest companies in the land would be proud. He then asks for your definite answer by midday tomorrow at the latest. The broker seems quite hurt by our unwillingness to get excited and puzzled by our opening reply as to why, if it is so good, has the local U.S. market not stampeded to the ceder's door. He usually cites a special friendship with somebody in the ceding company, and if we still feel cynical about it, we offer to put him in touch with our sister company, Hudson Life, in the U.S. who we say can give much more valuable local advice. That, of course, immediately kills it. Occasionally he says his client does not wish to cede locally because of confidentiality, but we still give the same answer assuring him our sister company will be totally discreet. The same result normally occurs as the broker departs swiftly. He might say the life business is wrapped up with casualty business, and he must handle both; but we still insist we need local expertise.

If we are satisfied at that stage, we might look at it initially. We invariably find a number of common threads:

- o The company is very small with poor or no rating, and it could not possibly stand new business strain on its projections;
- o Despite the hundreds of pages of actuarial projections, there is usually little information about the underwriting capability of the company;
- o There is no information about administrative and computer capabilities of the company; and
- o For such exciting dynamic business it either keeps no or very little retention.

Our suspicions are that the company wants to operate on a shoestring with vast reinsurance support and knows it will not get it from the locals. Hence, it tries an inexperienced, unlicensed reinsurer with little expertise. It also might be said that the small company may wish to off-load the increasing AIDS threat on the portfolio, and perhaps, the locals are unhappy with the underwriting.

It might not surprise you to know that following this route, we in the U.K. have never successfully completed one of these transactions.

Now I will be a little more positive. One of the major attractions of reinsurance is its ability to place capacity worldwide on large bona fide risks. For a risk, which has been carefully underwritten and controlled by a domestic U.S. reinsurer and for which the reinsurer is keeping a sizable retention in relation to its normal philosophy, it does happen, from time to time, that the company requires additional capacity, be it on a normal facultative surplus basis or in the form of a quota share pool. In those circumstances we are often willing to assist with the placement of such capacity. In fact the vast bulk of U.S. business that we are involved in entails support for domestic U.S. reinsurers in this way. Furthermore, it also can be the case that there is a reciprocal exchange, i.e., we may reinsure some of our European surplus reinsurance with a U.S. reinsurer in return for its own business. Such a reciprocal exchange is a natural consequence of international reinsurance cooperation. I don't want to pretend this market is vast because principally there are very high retentions in this market, but reciprocal exchanges do happen from time to time. The key point is that we, with our limited expertise in the U.K., are somewhat protected by the knowledge that a serious domestic player stands in front of us with the ability to examine the risk, to keep a fair share of it and to control the underwriting and computer problems I mentioned earlier. This, of course, is no guarantee of profitability but does at least give us some degree of comfort.

Occasionally it happens that support is required for special risk situations. Again, there is nearly always a domestic U.S. reinsurer involved in the first instance, but in this case the reinsurer may deliberately reduce its retention because of special parameters in the risk. Here, again, we know where we stand: for difficult or unusual risks the local U.S. reinsurer has reluctance in committing its full retention but nevertheless has explained its view internationally and will keep, in the final analysis, a fair share of the risk. Two examples of this type of reinsurance are:

- o special risk groups, e.g., sports teams; and
- o certain risky territories, e.g., Latin America.

As a third area, we have, from time to time, been involved in providing nonproportional support in the form of stop-loss reinsurance. Here, protection may be afforded on large group-type contracts in the area of overall excess deaths over those expected; for example, a claim may be precipitated if the overall exceeds 150% of the expected claims on the premium basis. Naturally this leads to large capacities for risk with a remote contingency of event and thus a small premium. These large capacities are sometimes handled by international cooperation.

I suspect that, at their origins in the U.S., the motivation for stop-loss may be to limit deficiency reserves on a block of business. To us it is quite appealing business, but I am not sure of the view the regulatory authorities take with this type of reinsurance vehicle. In Europe to be of any use you need to be a fairly big player to absorb high capacity, low risk business in any volume.

This brings me to the last point on business opportunities, namely, that of surplus relief. This seems to be the most discussed and utilized opportunity in this market, and here my knowledge is quite limited.

As I understand it, valuation strain is passed from companies which cannot afford it to companies which possess surplus and can thus absorb the strain. Prices paid are between 2% and 3% of the strain. Unlicensed reinsurers can get involved either by putting up a letter of credit or, following New York regulations in particular, by demonstrating "mirror" reserving. In the U.K. scenario there is the added attraction of our market not being liable to federal excise tax under reciprocal tax arrangements and also possibly because we possess tax regulations (I minus E) when I= investment income and realized gains and E= all expenses, which may sympathetically adjust to the risk.

However, having said that, there are serious problems for us, and the U.K. reinsurers have discussed such problems among themselves following various presentations from the U.S.:

1. In the U.K. we must establish a solvency margin, which equals one per thousand of the face amount at risk. Thus, we are ourselves involved in potentially high capital consumption.

2. We have in the past paid a stamp duty on policies of 0.5 per thousand of face amount if the agreement is three years or more. However, following our last budget, the stamp duty is to be abolished as of January 1990.

3. Our tax situation is now very dubious. From January 1990 the attractiveness of our expense offset in I minus E is to be considerably worsened until 1995 from when we can only take credit for some 14% of our acquisition expenses while taking 100% of the investment income. Therefore, there is a real long-range threat on the volume and availability of excess E for those transactions. Furthermore, at the present time, there is great debate concerning specialist tax treatment for reinsurance business. I fully expect measures to be taken in 1990 that could upset any tax advantages although at this time there is no quantification of this issue.

4. On the fourth point, virtually every reinsurance appointed actuary I know in the U.K. takes the view that, if you set up a letter of credit liability, you must, from a U.K. standpoint, fully back this with assets in your fund. You must ensure that, however remote the contingency associated with that letter of credit, you remain solvent to the extent of the liabilities you have assumed. This seems to be akin to the mirror-reserving requirements that New York has implemented.

Hence, to participate in that market, you must have the resources to support the surplus relief on offer, and generally this is so large as to outstrip any useful capacity.

We have considered stop-loss reinsurance as a solution to this since it overcomes the first problem listed because stop-loss reserves do not require solvency margins. It also helps with the third issued noted because the premium is fairly small and expenses would be fairly low. But the problem still remains unresolved on the letter of credit issue. Thus, as I understand it, at present little of this business has been done because U.K. reinsurers are not big enough and have limited free surplus.

I would like to close my presentation with a few remarks regarding the worldwide threat of AIDS. In the U.K. we have a working party on the subject of AIDS who has recommended minimum reserving standards that have been accepted by our regulators. Therefore, since 1988, offices with high mortality risk business profiles (including, of course, all life reinsurers) have had to set up substantial extra reserves consuming large amounts of free capital. All companies must set up extra reserves, but it is more minimal to those in the savings market, which distinguishes the U.K. market significantly from the U.S. market.

Because of this, the tendency has been to raise risk rates sharply on much of our term business at the critical ages of 25-40. Rates have gone up by 2 to 3 times. We also have removed guarantees and options and, in some cases, companies have experimented with an AIDS exclusion policy. We have also severely enhanced underwriting requirements with both HIV testing and lifestyle

questionnaires. I understand that in the U.S. testing is more detailed than ours and the questionnaire impossible.

To my understanding you find it difficult to raise rates at present although you do restrict guarantees. Thus today, because of our reserving and, therefore, rate requirements, it would be difficult for us to accept long-term guarantees in the U.S. market, and we must feel restricted to the short-term end. The lack of questionnaires also would give us a problem. Therefore, U.S. business is likely to be much less attractive to us on this front in the future, particularly, as our perception is that the disease appears more advanced here, and you have not been successful in raising prices. This may seem critical, but of course, there is still severe debate about the future impact of AIDS on life insurance. There are many optimists in our market as well. The point is, regulation has forced our hand to be cautious to the point where it hurts -- capital consumption.

MR. ROBERT J. TIESSEN: Being from Toronto, which is seen as being only marginally abroad in Canada and hardly separate from the U.S. at all by some, my view may not appear to be quite as far-sighted as some of my other colleagues on the panel who at least have an ocean separating them from the U.S. market. But I'll try to give a foreign viewpoint nevertheless. I have structured my talk in three sections: Introduction; Characteristics of the market; and Conclusion.

My view is mainly a Canadian view and to some extent a U.K. view. My company, The Mercantile and General Reinsurance Company (M&G) was founded in Scotland in 1907. We are part of a U.K.-holding company and operate on a worldwide basis, opening an office in North America in 1959. We became licensed to do business in the U.S. in 1971.

Our original entry into the U.S. marketplace was as a branch of a U.K. company. This structure continued for approximately 10 years until 1982 when we also established a U.S. subsidiary company. Our branch and subsidiary currently operate with the same staff out of the same office.

Some of you may have heard of the recent Canada/U.S. free-trade agreement. As a result of this agreement, it might be argued that differences between the insurance marketplace in Canada and the U.S. will be eliminated. While this may occur in the future, the current situation is such that the U.S. reinsurance marketplace should be viewed as a separate and distinct market, both by Canadians and others.

Many general factors have made the U.S. reinsurance market attractive. One of the reasons why many foreign companies expand to the U.S. is the ease of entry as opposed to the curbs on companies in some Pacific Rim nations. The widespread use of English as a worldwide language of business and the strength and convertibility of U.S. currency make it easy to do business in the United States.

While much of the reinsurance interest in the U.S. from abroad has to do with surplus relief and other similar types of reinsurance, I will be limiting my discussion to what might be termed "regular reinsurance." With this introduction, a question we are still faced with is: "How do you decide whether to enter the U.S. reinsurance market?"

For a Canadian reinsurer one of the implications of entering the U.S. market is the relative size of the market. In recent years U.S. companies have sold approximately 10 times as much life insurance as Canadian companies. The differences in the sizes of the reinsurance markets are somewhat greater, influenced to an extent by the large amount of U.S. reinsured business from the A. L. Williams organization. U.S. reinsured new business was approximately 15 times as large as the Canadian marketplace for 1986 and 1987 and 10 times as large for 1988. The change in the 1988 figure is due to a significant increase in the Canadian reinsurance marketplace in that year based on preliminary figures. The proportion of business reinsured in the U.S. is higher than in Canada with a figure for 1987 being 12.5% of the market in the U.S. and 7% in Canada.

My figures also came from surveys produced by Munich American and reflect only recurring reinsurance, thereby excluding retrocessions and portfolio transactions. Canadian figures, also from the Munich, were developed in a comparable way.

Another way in which the two reinsurance markets may be measured is the market share of the various leading reinsurers. The market share of the top reinsurers is similar in each market and the top five reinsurers control a large share of the total in both markets. Not quite as significant

is the large number of reinsurers in each market: 18 in the U.S. and only 7 major reinsurers in Canada. The large number of reinsurers operating in the U.S. has had the expected impact on competition levels, another factor for new entrants to keep in mind.

Most of the reasons behind the dissimilarities in the Canadian and U.S. figures presented had to do with differences in the nature of the direct company markets in the two territories. The U.S. has more insurance companies in the medium-to-large category than Canada. By this I mean companies that have a large marketing force operate on a national basis and, therefore, have large volumes of placed business. However, the in-force blocks of business for these companies are not yet large or mature enough to allow for multimillion dollar retention, thereby resulting in large amounts of reinsurance.

As a result of this, the companies with the largest retention sell a smaller proportion of the business in the U.S. than they do in Canada. U.S. companies are also more likely to have a brokerage distribution system, which often encourages more shopping of business and results in larger amounts of reinsurance.

One of the most striking differences that distinguishes the U.S. reinsurance marketplace from other markets is the frequency of situations where the experience of the direct writer and the reinsurer need not be the same. This can arise from universal life expenses being covered by investment margins, from the income tax effect of reinsured graded premium whole life policies under a modified coinsurance agreement using the 818(c) election or from reinsuring medical claims on an excess basis instead of a first dollar basis.

In most territories, considerable effort is made to try to have both parties in the same position should an extreme development occur. This is less common in the U.S., especially for individual life situations, where reinsurance relationships are viewed with a much shorter perspective than they are in most other countries.

A U.S. client of ours recently introduced three different series of term products within 12 months, each series replacing the previous one. Each series was sent out for competitive bids; each series had a separate reinsurance administrative arrangement; and each series had a different group of reinsurers covering that risk. This is the expected way of handling reinsurance for many U.S. companies.

In other areas of the world, new products may just be added to the existing reinsurance agreement, which since it is often on a YRT basis, does not even require the calculation of product-specific coinsurance terms. This willingness by U.S. direct companies to be open to new, possibly foreign, reinsurers, for any new product has always made it easy for new reinsurers to enter the market. I see a small trend away from this openness, however, as the amount of administrative work involved in constantly evaluating and changing reinsurers has become excessive for some. This may well make it harder for foreign reinsurers to enter the U.S. market, as U.S. direct-writing companies reduce the number of reinsurers they solicit bids from and, also, the number of companies who ultimately share in the reinsurance.

Another feature of the U.S. reinsurance marketplace that is different from the Canadian marketplace is an increase in use of third parties, for example, consultants, brokers, intermediaries. This use of consultants and other advisers has frequently resulted in price being the main characteristic used to differentiate reinsurers in the U.S. Since many U.S. direct-writing companies do not look to their reinsurers for the same types of services that are often required of reinsurers in other countries, this may be a valid approach. Since the average size of ceding companies in other countries is often smaller than in the U.S., non-U.S. direct-writing companies often are more likely to look to their reinsurers for advice in areas such as underwriting, policy wording, product design, and response to industrywide issues. In such situations, a partnership approach is more likely to develop as opposed to the buyer/supplier approach that is more common in the U.S.

Another striking difference that is apparent in the U.S. reinsurance marketplace is in the types of products being reinsured. Many of the unusual product features currently in the U.S. market result from the existing valuation rules. For example, I know of no other jurisdiction in which it is advantageous to design a term product yet to call it a permanent policy. Reentry ART, the dominant reinsured policy of the 1980s, is a product that is sold primarily in the United States.

Only two major companies sell the product in Canada, both of whom have U.S. connections. To my knowledge, this product is not sold elsewhere. The reinsurance of the main permanent product, universal life, on strictly a mortality risk basis, has also essentially eliminated reinsurers from participation in the investment element of life insurance products in the U.S. Valuation rigidity also delayed the introduction of interest products which were available in many countries prior to their U.S. introduction.

An interesting side light from a Canadian viewpoint is the progress of level premium term-to-100 policies in the U.S. Term-to-100 policies have been sold in Canada for the past 10 years. These products have gone through various development stages, but initially they were level premium, level death benefit policies with no nonforfeiture values. Coverage was available until age 100 under these policies. As a result of not having any nonforfeiture values, pricing was very sensitive to the lapse assumption used. Naturally, this sensitivity was present in both direct company and reinsurance pricing.

The Canadian Institute of Actuaries established reserve standards, including lapse assumptions, for these products a few years ago, and now most products have some type of nonforfeiture option. This has reduced the sensitivity of the premium rates to lapse assumptions.

Several U.S. companies are now selling no cash value, level premium life products. Because of U.S. valuation laws, considerable gymnastics are needed in order to achieve this concept, but the use of a participating decreasing term policy can usually produce the desired result. Unfortunately, some of the problems encountered with term-to-100 in Canada may be repeating themselves in the U.S. While some reinsurers applied the experience they had gained with the product in Canada to their U.S. opportunities, it appears that not all reinsurers may have been aware of some of the Canadian experience.

A recent phenomenon, which has involved foreign reinsurers in the U.S. marketplace, is joint-life, last-survivor coverages. Joint-life, last-survivor coverages seem to be enjoying a bit of a renaissance as far as the number of new products go. Many of these newer policies have product features, which have made it difficult to obtain coverage in the U.S. marketplace for the desired amounts, resulting in recourse to Europe. Many of these joint-life, last-survivor products have been packaged in such a way that the reinsurer is asked to take a disproportionate amount of the more speculative risks, while the direct-writing company retains the more predictable risks. This has been a factor in the difficulty in obtaining reinsurance coverage.

The prevalence of many product differences between the U.S. and elsewhere and knowing the reasons behind them indicate that operating at a distance in the U.S. marketplace is operating at a disadvantage. As a result, many foreign companies have established offices in the U.S. and operate as subsidiaries.

Any foreign reinsurers must be quite surprised at the U.S. regulatory situation when they encounter it for the first time. The need to cope with up to 52 different sets of regulations (50 states plus the District of Columbia, and federal taxation regulations) is much higher than that required in most other territories, even when the territories are multinational, such as Europe or the Caribbean.

Reinsurance transactions, especially those providing surplus relief, have become the target of increasing regulatory scrutiny in the U.S. While most of this scrutiny is designed to eliminate perceived abuses, the methods used have inevitably made life more difficult for all concerned. Of course, many people feel that the innovative surplus relief arrangements are only necessary because the statutory reserve requirements are outmoded. Certainly, it is not hard to see how a valuation reserve basis, which changes only every 20 years or so, cannot keep up with the changes in the insurance marketplace.

Reinsurers familiar with the Canadian or the U.K. system are in fact surprised that a valuation assumption can be preset by regulatory authorities without giving consideration to individual company differences with respect to such items as expense levels, mortality rates or even lapse rates. Of course, the current U.S. valuation method does not permit the use of lapse rates at all which results in the reinsurance of a universal life plan (where only the mortality risk is being reinsured) being valued the same way as the reinsurance of a reentry term plan. I think many of us would agree that the reinsurance mortality on these two products is likely to be dissimilar.

The enactment of mirror-image reserving rules by New York will obviously reduce the attractiveness of reinsurance, which uses differences in reserve bases. The workload involved in full compliance with the New York regulation also reduces the attractiveness of operating in New York at all. These new complicating factors with respect to the regulation of reinsurance in the U.S. may discourage new entrants from the marketplace.

The U.S. view on antitrust activity and what this encompasses may appear to be a limiting factor to some foreign companies that are used to a freer flow of information. The antitrust situation is a point that is often raised at the Canadian Reinsurance Conference, an annual gathering of ceders and assumers of reinsurance to discuss problems and develop solutions. Many advantageous steps are being delayed or postponed due to antitrust fears.

I have become a bit more familiar with the U.S. antitrust laws in preparing for this panel, thanks to the information provided through the Society's counsel on what can and cannot be said. It has been suggested that the insurance industry could take a lead from the banking industry in this area.

When a leading bank announces an increase or decrease in its prime lending rate, other banks usually follow in short order. If they do not, the original bank usually moves back to its previous position. This does not appear to create any antitrust problems in the U.S. for banks. In many places insurance works the same way. Perhaps it could in the U.S. as well.

You may have all been waiting for this next section, or perhaps you came here hoping to avoid it. Alas, AIDS is a factor in all facets of life insurance. In the time I have available, I do not plan to provide any specific figures as to what the reaction to AIDS should be on either a valuation or pricing basis; other sessions are addressing that topic.

The insurance and reinsurance reaction to AIDS has been varied across the globe: Peter has already mentioned that in the United Kingdom, where the number of AIDS cases per 1,000 of the population is 0.02, most companies have increased prices because of AIDS. This was as a result of reserve increases being required.

In Canada, the number of AIDS cases per thousand population is 0.06, three times as high as the U.K. figure. Several companies have acted to increase prices because of AIDS in the Canadian market. Here again, reserve increases have been required by the regulatory authorities.

In the U.S., the number of AIDS cases per thousand population is 0.19, three times as high as the Canadian figure and nine times as high as the U.K. figure. To my knowledge, no companies in U.S. have changed their prices because of AIDS, certainly not to the same extent as Canadian and U.K. companies. This is possibly due to the fact that no reserve changes have yet been required. This is a substantial difference in approach.

From the U.S. view, it would appear that many foreign companies are crying wolf, trying to get people exercised about a risk that does not exist. From the foreign viewpoint, however, U.S. companies appear to be the crowd watching the emperor's parade, everyone knowing that the risk is there and that something has to be done, but no one willing to admit it. What is my opinion on the matter? I would just like to say that there really is a wolf.

On a more practical basis, foreign reinsurers operating in the U.S. as branch operations must set up additional reserves on the business that they write in the U.S. because of AIDS. This is true now for U.K. and Canadian companies.

At the M&G, in our U.S. Branch operations, we have made a provision of $20 million for AIDS claims, about one-third of our statutory basis reserves of $58 million at the end of 1988. While such reserves are not necessary for foreign reinsurers operating as U.S. subsidiaries, it might be difficult for some actuaries, especially those operating under the valuation actuary concept, to ignore the potential impact of AIDS. Our valuation actuary has felt it necessary to set up additional provisions, in excess of our statutory levels, for our U.S. subsidiary. The level is similar to our U.S. branch, about one-third more.

Why invest in the U.S. reinsurance market? There are many reasons for a foreign company to do so. You might have a long-term view of the market, and you expect any current unsatisfactory

practices to end, as their impact becomes known and that, by being a long-term participant in the market, your skills and services would be recognized and rewarded.

Another reason might be the desire of your company to protect itself on a worldwide basis against fluctuations in experience in any one territory. If Europe or Asia are having poor experience, the North American experience can be used to provide a greater distribution of risk, and therefore, less fluctuation in overall company accounts.

The ability to service your current clients, as they expand from their home base into the United States, is another reason to expand there. Offering service worldwide can have advantages in being able to apply developments from one territory to another. For example, dread disease coverage moved from one area of the globe to another assisted by reinsurance companies operating worldwide.

If assets are being held by a company in the U.S., a matching liability may be desired. Since it is easier to generate reinsurance liabilities than other kinds, an investment reason may be the driving force for entering the U.S. reinsurance market. Another consideration, especially if you have a shorter-term viewpoint, would be to invest now since the life cycle may be on an upswing now that AIDS testing is in place, persistency seems to be improving, and other factors seem positive. However, the main reason why people invest in the U.S. reinsurance marketplace is that the U.S. is where the worldwide reinsurance market is centered. I would like to end with a Russian proverb concerning reinsurers I encountered a few years ago. A reinsurer is someone who wants to avoid risk but whose position requires him to accept it. The U.S. reinsurance marketplace certainly requires the acceptance of risk. The market is large and generally open to new entrants. New investors should not expect a continuation of current practices or products. There are opportunities for wise and patient participants. Others should stay away.

MR. STEPHEN PAUL TAYLOR-GOOBY: I'm going to run through a number of issues and questions that U.K. and continental European reinsurers look at when considering venturing into the U.S. market. The first things that people look at are the superficial reasons why the U.S. might be attractive. There are a number of them. The first of these is not a very deeply reasoned argument for entry into the U.S. market. The size of the market is always mentioned as a reason. Let me give some background to the position of some of the continental European reinsurers as to why size is an attractive reason for coming to the U.S. In Europe, a large proportion of business has been savings oriented with short-term endowments and deferred annuity contracts being especially popular, mostly for tax reasons. A large amount of this business is reinsured, partly to manage the emergence of profit in the light of highly restrictive rules governing the distribution of profit to shareholders in some European countries. Hence, we have some European reinsurers that have grown very strong and very big. Tax considerations also have driven them to retain large amounts of profit within the business, which has resulted in enormous capital bases. A lot of the barriers to entry that have kept competitors out of Europe are now being brought down by the European Economic Community (EEC) and considerations such as 1992. A lot of these companies are now looking to their stock price and wondering what's going to happen to them. There is now a powerful reason why this excess capital should be put to work. And the first place that you look to is the biggest market in the world. The chart below provides an indication of the size of the U.S. market compared to the European market.

European Direct Market
1987 Life Premiums

	U.S. $Billions
U.K.	$40
Germany	26
France	22
Switzerland	9
Netherlands	7
Other Europe	14
U.S.	181

Direct life premiums are shown because it is difficult to obtain meaningful statistics on reinsurance premiums; the risks get shared and retroceded around the world, and it is difficult to

tell what is U.S. and what's not. Another factor to bear in mind when reviewing these premium income figures, is that I would estimate that the share of business going into protection (term insurance and whole life contracts) in the U.S. is double the share in the U.K. So, in fact, the U.S. protection market is very much bigger.

The second reason why European reinsurers might wish to move into the U.S. is the great difference in sophistication between the two markets. I'm going to take a few minutes to explain why the markets are different.

To look at product design in the different areas let us distinguish between the U.K. and continental Europe because the U.K. is very different. Traditional products, i.e., traditional whole life and endowments, seem to be worldwide. Universal life is relatively strong in the U.S. and very strong in the U.K. There have been one or two companies which tried to introduce these products in Europe, but with little success. Variable products, unit-linked products as they're called in the U.K., now comprise about 40% of new business in the U.K. I understand that the market penetration is a lot weaker in the U.S.

In the U.K. we're seeing one other development which is the development of integrated financial services groups. We heard Dave Carpenter talk in the general session about the threat from banks and other financial service institutions. In the U.K. we actually have far more flexibility to get around these problems. Insurance companies can buy banks and other financial services institutions. It's common to see mortgage lenders, unit trusts, mutual funds, banks and insurance companies within the same financial services group so that the group itself is protected against changes in legislation that can cause one product to suddenly become more attractive than the other.

I do not want to leave you with the impression that continental Europe is just one big market. In fact, it is several markets within the one. We will look at a few of the characteristics of the different markets. First, the German market is the most regressive of all. It's heavily dominated by a cartel of insurers which have very close links with the governing and supervisory authorities who tend to behave and act in their interest. It has a very insular attitude, a fear of foreigners, and it has been protected from foreign entry. This protection has, in my view, contributed to the lack of sophistication in the products and the lack of competition. We generally find that sophistication is inversely proportional to regulation.

We can move across the spectrum. France was very similar to the German market in the past. But it is beginning to loosen up. The French have heard of "1992" and want to start preparing for it. We also see the banks beginning to compete strongly with insurance companies.

Italy is another exciting market, where life insurance still has tax privileges. People are developing an awareness of this, and that awareness has the obvious consequences for new business.

The Netherlands is the most free market in continental Europe. Many companies go there wanting to get into continental Europe, but few manage to compete successfully. The market is still dominated by the big Dutch insurers with whom some of you are familiar.

And finally there is the U.K. where there is complete freedom of product design. Another interesting feature is the strong actuarial profession. Other characteristics include total freedom of investment and an open market for foreign people to enter. All this has led to a deregulated and healthy market for the consumer.

I'll now come back to the original subject which is reinsurance. My view is that the regulation in the U.S. market with valuation laws, nonforfeiture laws etc., which has so closely controlled the direct market, has led to a greater sophistication in the reinsurance market and the development of a very highly sophisticated secondary market.

My next comments illustrate the variation of reinsurance products found in the U.S., the U.K. and continental Europe. I've divided the products into a few broad categories. Risk premium reinsurance and coinsurance are available in all three markets. I include modified coinsurance (modco) with coinsurance. Modco is very strong in continental Europe, for some of the reasons I mentioned earlier for profit management. And, typically, all financing, which may be called

surplus relief here but really is a totally different product, is done by straight coinsurance with risk.

Tax-motivated reinsurance in the U.S. has developed, and as far as I can see, is largely undeveloped, although I believe there are still some opportunities. It's still not developed in Europe.

Surplus relief, as you know it in the U.S., does not really exist in continental Europe and is very limited in the U.K. although there are one or two new products that have emerged in the last 5 years or so.

Many reinsurance companies and continental reinsurance companies see the sophistication of the U.S. market as a very powerful reason for entering that market. There is actually a chance to gain access to the technology of the market and to transfer it back to the continent. Frequently you'll see continental actuaries going to the U.S. for their training, and then problems arise when the companies try to get the actuaries back to Europe again.

While we're on superficial reasons for entering the U.S. market, there is one final reason. It is just that the market is different, and this is a fascinating reason why companies want to enter the U.S. Until relatively recently the European reinsurers have not competed vigorously with each other. There were few major reinsurers, and they tended to avoid each other by keeping strictly to their own territories. In the last 15 years we have seen the position change radically with new entrants to the market and the old noncompete agreements of the established reinsurers falling apart. Profit margins have fallen dramatically. The old way of pricing some coinsurance treaties was the "10 and 5" pricing method whereby the reinsurer pays the same commission to the direct writer as the direct writer is paying plus a 10% initial expense allowance and a 5% renewal expense allowance. This is dramatically changed. Today we see sophisticated profit testing of reinsurance quotes, and companies looking for a 15% after-tax return on capital invested. Companies then knock another 1% off that rate because they know they will not win the business unless they do.

This leads to the "brown grass" syndrome. It's fairly simple logic: "The grass is brown here so it must be greener everywhere else. Let's diversify overseas." This doesn't sound very logical, but you would be surprised how often this argument is used.

There's one other reason why U.K. and European reinsurers want to get into the U.S. market, and it's one that is often not mentioned. It is the attraction of trips for senior executives to go to the U.S. to monitor the business and keep up contacts.

Despite these superficial attractions, at a closer look, the market does not look so appealing, particularly the market for traditional risk reinsurance. This becomes readily apparent if you try to analyze the competitive strategies a new entrant might adopt.

The market appears to me to divide into two parts. In one part treaties are placed with reinsurers with strong historical and personal relationships with the ceding company, competing by reputation and relationships. This part of the market is still relatively strong in the U.K. and in Europe where many of these loyal relationships with reinsurers are quite hard to break into for a new company. Companies tended to take the attitude in the past that reinsurance was only 4% of the business and the rest was hugely profitable, so why worry too much about the reinsurance terms?

The other part of the market is heavily price competitive, and I believe that this comprises a much larger proportion of the U.S. reinsurance market. My impression is that price is about the only significant competitive factor.

The first segment is closed to newcomers by definition. The second is expensive to get into.

It seems to me that a reinsurer aiming to gain market share by competing on price will always lose money because the market is relatively perfect. It only takes a small number of competitors to create a perfect market. In such a market you might expect all reinsurance quotes to be close to the minimum return on capital. It then only takes one reinsurer to be a bit overoptimistic or perhaps take a better view of the company's underwriting and feel that it can undercut the others, driving the market down.

It's difficult to see any other grounds on which a new entrant can compete. Some companies will tell you that they're reinsurance service is better than others. Many times I've seen claims made, such as XYZ company will turn your substandard cases around much more quickly, will give you a quick decision on facultative cases and will provide smooth administration. I think most companies are cynical about this. What usually happens is that, when the marketing actuary is in town, the service is wonderful. But when the marketing man's gone, the treaty placed and you are dealing with the administration people, the service is a bit different.

One final method of competition, which is heavily used on the Continent and in the U.K., is competing by offering additional services, usually without charge. Services that would typically be provided are product-development services, including profit-testing facilities and rate making; tax advice; underwriting assistance; and, in some cases, direct-marketing assistance at no charge, although given the expense, this is becoming rare. Trying to compete by offering these types of services, I think, must be expensive for a small company.

There are two other reasons why the decision to enter the U.S. market is not one that you should take lightly. One is American actuaries and the other is American lawyers. I put these under the heading of "cultural differences."

In selling reinsurance you have to negotiate with experts rather than with the public. European reinsurers are used to negotiating with European actuaries who tend to have strong loyalty to their reinsurer and don't particularly want to upset the reinsurer when they know it will be back. My impression of U.S. actuaries is that they know their business well, are more profit oriented, and would not hesitate to capitalize on any sign of naivete in a foreign reinsurer. U.S. lawyers can come as a shock to Europeans. Traditionally the reinsurance market has been based on the principal of utmost good faith, and many reinsurance treaties are very loosely worded. The reinsurer will always rely on the arbitration clause and know that it company will be dealt with fairly in the end. I get the impression that the U.S. environment is more legalistic, and I would not expect a U.S. court to be all that sympathetic to a foreign reinsurer pleading that it thought that it had entered into a gentleman's agreement.

These last two considerations just serve to reinforce Peter's and Bob's messages that it is unwise to write risk reinsurance business on a casual basis without establishing a branch or a subsidiary. I believe it is vital to build up local expertise and to know and understand your clients. Otherwise, you will be selected against.

There are other obstacles that make life difficult for a nonestablished reinsurer, for example, the U.S. reserving requirements, excise and withholding taxes and requirements to hold localized assets backing reserves. Each of these considerations adds to the complexity of any reinsurance agreement and reduces the margins that are available to the reinsurer.

To summarize, although there are reasons why European reinsurers are anxious to expand into new territories, especially the U.S., the traditional risk market is perceived as a difficult one. In my view, an entrant is unlikely to have much success in attracting serious business as a non-established reinsurer. In order to make any impression on the market, a company must establish and meet the competition head on. This is likely to be a long and expensive task, only worthwhile for the very large companies. Even for the large companies, this route is probably only possible for those with patient shareholders.

My fairly gloomy view of the prospects for European reinsurers in the U.S. risk market is probably welcome to you -- it indicates less competition in the future. However, I believe the prospects in the U.S. financial reinsurance market are much brighter. The differences between the different markets, i.e., European and U.S., that give outsiders a competitive disadvantage in traditional markets actually turn into opportunities for arbitrage in financial reinsurance. I see three areas where the different regulatory regimes present such opportunities: tax, reserving, and accounting.

The first area, tax, has been known for a long time but is fraught with difficulties. The main opportunity has existed between the U.K. and the U.S. where life companies are taxed on totally different bases. In the U.K. tax is based on I minus E, investment income and realized gains less all expenses. Unused expenses get carried forward, hence the phrase "excess E," because most companies tend to have more expenses than investment income.

A company operating in both the U.S. and the U.K. would naturally wish to arrange for all its profit to arise in the U.K. and all its investment income to arise in the U.S. This is somewhat simplified, but it is something that can quite easily be arranged. The problem with this neat scheme is, oddly enough, resistance from the tax authorities. Successive tightening of U.S. regulations now means that, in theory, it should not be possible for a U.S. company to reduce its tax bill by reinsuring. However, it is still possible for a U.S. company to profit by reducing the tax bill of a U.K. company through reinsurance.

Given what I have just said, why haven't all U.K. life companies simply reinsured out all their investment income to the U.S. and reinsured in expenses on terms that are profitable both for the U.S. and the U.K. companies involved? The answer lies in the peculiar nature of the U.K. tax system, which like many other things in the U.K., relies on trust and good faith. Reasonably large parts of the tax bills of U.K. companies depend on precedents and discretion on the part of the tax authorities rather than the letter of the law. If a company abuses the good faith of the authorities to save tax in one area, it can easily end up paying more in other areas. Thus, many companies have not wished to be adventurous. Having said that, there are always a few companies, usually the smaller and the younger ones that have very little to lose. They don't have the old relationships with the tax inspector and are willing to pursue this opportunity more aggressively.

The position is changing now. The U.K. tax authorities have long recognized the weak position that exists when they have a totally different tax base from continental Europe and also the U.S. They are aware of opportunities that exist for companies to totally wipe out their U.K. tax bill. So far, the discretionary system has worked in keeping the tax leakage to fairly small numbers. But the worry remains. We recently had a complete review of the tax system in the U.K. Some measures already have been announced, and the warning is left that reinsurance is a topic still on the agenda. It will be addressed later this year.

The reason why the rules haven't been published is that the U.K. authorities still don't know exactly what they're going to do about reinsurance. I think there's danger for the U.K. authorities, which may turn into an opportunity for financial reinsurers. This is that if the U.K. authorities abandon the old system whereby they in fact had quite a lot of power over companies and move to a more legalistic system whereby companies are much less frightened to operate strictly on the letter of the law, then the opportunities for arbitrage may just increase. It would only be a short window I'm sure, but it may appear soon.

Tax-motivated reinsurance is an example of the way that a free-arbitrage market puts pressure on governments that introduce regulations which are out of line with other countries. There are other examples of this. The only way to stop this is to close up the market and put up the barriers in the way the U.S. government has with its antireinsurance legislation. Another example is the different reserving requirements.

In the U.K. the reserving regime does have some regulations about minimum reserves that you have to hold. But largely, the reserving rules rely on the integrity and the judgment of the actuary. This presents an opportunity if rules in the U.S. demand unreasonably heavy reserves. It should be possible to find a U.K. actuary who'll take on the same risk with lower reserves. Assuming the cost of capital is the same in both territories, it will pay to reinsure those reserves across to the U.K. U.S. regulators have tried to prevent this free market by establishing barriers, such as denying reserve credit unless funds are withheld or letters of credit are provided, and now New York has mirror-reserving requirements. I believe that these regulations tend to act as a spur for innovative minds and that, if there is sufficient benefit in reinsuring overseas to escape burdensome reserving requirements, it will happen nevertheless. I have to stress here that the point is not to escape from fair reserving requirements but from ones that are unfair.

There are still some problems with reinsuring into the U.K. You must pay a stamp duty of 0.5 per $1,000 of face amount reinsured. This has been fairly easy to avoid by putting a stop loss on the treaty and reducing the total face amount reinsured. And, in fact, it is possible to not transfer any risk but to lose the reserves, or to not transfer any risks that the U.K. actuary would call a risk, then there would be no solvency margin or no stamp duty because there's no risk.

One area where it seemed likely that a transatlantic reinsurance market would develop arose through the nondeductibility of AIDS reserves for U.S. taxes. In the U.K. we still have the

position that any reserves that the actuary wants to set up are deductible for tax, although that may not last for too many more years. However, we have not seen a significant market in AIDS reserves being transferred across the Atlantic. The main reason is the culture of the European market where surplus relief has always meant a transfer of risk. I think U.K. actuaries were particularly worried that they were actually going to assume real U.S. AIDS risks. They have looked at the U.S. market and believe that it has not reacted properly to the increased risk of AIDS. We may be wrong, but it has been a good excuse to put the prices up.

One final area that may produce an interesting market in transatlantic reinsurance is that of accounting. Many U.S. companies seem to be finding that Financial Accounting Standard (FAS) 97 is having an adverse effect on their profits. Most U.K. companies do not report under GAAP. We actually have an interesting concept that governs statutory accounting in the U.K., which is that of true and fair, i.e., the accounts should actually present a true and fair picture of what the company has earned in the period under consideration. The value of an asset should always be what you can sell it for, and the value of an insurance contract should never be less than what you can sell it to a reinsurer for. So, it strikes me that there's an opportunity for U.S. companies to gain immediate assets in their statutory accounts by reinsuring the contract overseas. In the U.K. a company can take full credit for the present value of future profits in its accounts. I have to distinguish here between the published accounts and the statutory accounts that are used for looking at capital and solvency. But, it may still be profitable to reinsure as a way of managing your profit emergence, only, of course, if you think that your profit emergence is unfair under the current rules.

In conclusion, I see some opportunities for European reinsurers in the U.S. financial reinsurance market, not for companies to establish and compete in the surplus relief market since many Europeans would regard the prices paid for surplus relief as an inadequate return on capital for the risk involved, despite the fact that the deals are risk free. The opportunities for European reinsurers lie instead in exploiting the differences between the markets, and for this it is essential to remain offshore.

This will never be a secure existence because opportunities come and go with time and changes in legislation. It presumably does not present a threat of increased competition to local reinsurers since the opportunities are additional to rather than replacements for opportunities in the local market.

MS. COLLINS: Mutual Life of Canada has several U.S. subsidiaries, and it has recently made a decision to enter the U.S. reinsurance marketplace. Phil Brooks from Mutual of Canada is in the audience, and Phil has agreed to share with us some of Mutual of Canada's thoughts.

MR. PHILIP D. BROOKS: My comments are more general and not necessarily specific about Mutual Life of Canada. I think Mutual is representative of a number of large Canadian companies, which have been active for some time or are becoming active in the retrocession marketplace. The first reason, as has been stated, is the size of the market. These large Canadian companies generally have surplus that is not being used efficiently in Canada, and with the U.S. market being extremely large it is enticing because it is so close. From a profit point of view, recently the profit in certain areas, for example, special risk reinsurance, has been very strong.

I would like to ask a question with regard to AIDS, one of the major concerns that all these companies have. It has been addressed by each panelist and all have made references to the differences between the U.K., Canada and the U.S. The problem is presumably recognized. The Canadian companies look at the U.S. and question whether anybody will take any action from a pricing point of view. Mutual's position in the U.S. currently is that we are evaluating how AIDS should effect our pricing and our product development from a new business point of view. For current business that is being written today, is it being tested sufficiently so that there is no need to take any action on price?

MR. DENIS W. LORING: A number of companies in the United States seem to be constantly lowering their blood testing limits. We believe that the additional information that results from blood testing at lower limits, not simply Human Immunodeficiency Virus (HIV) information, but liver function tests, glucose, and other blood information, provides you with underwriting margins that compensate for people who are zero negative on issue and then will be converting to zero

positive later. On balance, the lower blood testing limits make up for possible conversions after issue because they pick up the HIV people with lower levels and provide other useful information.

MS. COLLINS: Bob, how did M&G react to New York's recent enactment of the mirror-reserving regulations at the end of 1988, and what are its plans for 1989?

MR. TIESSEN: There were some features in the New York regulation that indicated that it would not apply to agreements that did not assume any additional new business. Hence, one of the first steps taken was to close off all our existing agreements with New York companies and set up new ones, effective January 1, 1989. This meant that we did not have to apply the mirror reserving standards to the existing in-force business and merely had to worry about it for new 1989 issues. We have not filed any 1989 statements yet, and I'm not exactly sure what we'll be doing in this area. However, we had been simplifying some of our reinsurance arrangements in light of increased scrutiny, and I think we closed off some of the more complex arrangements we had in the past. We will be able to handle the mirror-reserving requirements for new business now, and when year-end comes, we will see how much work it is. We want to avoid having to follow too far down the line, which is required by the law. In many arrangements it would be impractical to follow the law to the full extent, especially if you've placed business into pools that might get ceded off again.

MR. STEPHEN F. KRAYSLER: There seems to be a sense of the panel that U.S. actuaries have not recognized the threat of AIDS. I'd like to address this issue from a valuation standpoint. I think it's fair to say that compared to pricing assumptions, excluding the AIDS risk, that valuation mortality is orders of magnitude greater than expected mortality. Therefore, there is a huge contingency reserve built into the valuation basis. Although, I would rather see a series of explicit reserves for this risk, we do have a major difference in reserving. In the U.K. and Canada there is a valuation concept and a lower statutory base reserve. AIDS adjustments were made on the valuation basis in the U.K. and in Canada, but they were made on a much lower valuation base. Even with the higher incidence in the U.S., is it not possible that there's still quite a bit of protection in the U.S. in the valuation basis?

MR. SAVILL: I'm not really familiar with the U.S. valuation basis. The additional reserves that we put up are very similar to what Bob mentioned, about 25% of reserves. It does rather strike me that from what you say, that nobody yet is quite clear what the severity of this problem is and just how much margin we have got. I've heard this argument used in the European market, that U.S. companies start with much higher statutory reserves than we do. We originally worked off of our published assured lives basis and molded a number of projections on top of it, basically of the Cowell-Hoskins type. You may well be right. But at the end of the day we're in a period of considerable uncertainty as I see it. We in the U.K. feel that we ought to start, go out and meet that uncertainty head-on, at least for the solvency of our companies, and talk to shareholders, and say to them "Look, this problems looms." Because it's the next generation of actuaries, our sons and daughters, who are going to pick up the bill if we don't.

MR. TIESSEN: One other comment I'd like to make is that the margin in the valuation basis is relatively small at the younger ages and then expands as you get into the older ages. The AIDS risk is exactly the other way around, large at the younger ages and less at the older ages. Trying to offset these two areas can be quite difficult. It depends on your AIDS distribution, your age distribution, and other things of that nature. I think it might be difficult to offset that one additional expense against that one additional margin for this reason.

MR. TAYLOR-GOOBY: Steve, you're right, regarding valuation standards. An appointed actuary in the U.K. would be justified in reserving on say 90% of the assured lives table if he could demonstrate that experience was below 80. This is not much of a margin. However, I think the pricing side is more interesting where term rates in the U.K. had already dropped to a suicidal state and something needed to happen. It's fairly easy to demonstrate that all the companies at the top of the market, unless their underwriting was absolutely superb and very significantly better than the average, must have been losing money on their term lives. The industry took it as a good marketing excuse to put the prices up, sometimes by double and more.

MR. JOHN E. TILLER, JR.: I would like to pick up on Bob's comment about the margins and the valuation table being greater at the high ages. That's absolutely correct. If we try to adjust a mortality table to reflect modern mortality with AIDS, we would probably get a flatter mortality

table, and the slope, therefore, would cause maybe even a lessening of reserves. Some work that Dave Holland and others have done has shown that the current 1980 CSO is adequate on an overall basis for reserves at a normal company's distribution of business, whatever that may be. But, if you look at a high proportion of low average age policies or a high proportion of term policies, then the reserves become very inadequate. Increasing premium policies in particular may have inadequate reserves. I would point out that even companies that are selling YRT reinsurance are generally selling an increasing-in-premium, term-type product. Therefore, the reinsurers may have more of a problem vis-a-vis reserves than would a direct writer.