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Description of the Development Process for the 2003 GRET Factors

by Timothy Harris

Timothy Harris

Once a year the Committee on Life Insurance Company Expenses of the Society of Actuaries at the request of the NAIC reviews the prior year's life insurance company expense data in order to determine if a new GRET table should be established.

This year we started by acquiring 2001 annual statement data for the 200 largest life companies as measured by life insurance expenses. The companies were grouped into the four categories of distribution systems: branch office, direct marketing, home service and all other. Companies were placed in the appropriate category based on research performed by Conning and Co. supplemented by public information (e.g. Bests Reports) for our analysis.

This total expense information for each group was used to modify the LOMA expense factors that have been the seed factors in all prior GRET calculations. This modification was accomplished by multiplying the LOMA expense factors by the appropriate total units from each group of companies. An adjustment factor was calculated as the ratio of the total group of companies' expenses to the totals produced from the LOMA factors. This ratio when applied to the LOMA factors and multiplied by the appropriate units will then reproduce the total expenses for the group.

Actual to expected ratios are then calculated using each companies units and the adjusted LOMA factors and the companies are sorted by their actual to expected ratios.

To lessen the effect of reinsurance on the analysis, companies were removed if life reinsurance commissions and allowances were at least 25 percent of the sum of life general expenses and life commissions. Additional companies were added to replace those that were dropped. Companies were then excluded if they were considered to be "outliers". Outliers were generally determined to be those companies with expenses that were less than 20 percent or greater than 300 percent of the expenses produced by the median factors applied to that company's units. New companies were selected to bring the number back up to 200.

The final expense factors for each group are then derived by applying the A/E ratio of the resulting median company to the modified LOMA seed factors.

Finally, the factors were rounded in the following manner: "Per Policy" expenses and "Maint" expenses were rounded to the nearest dollar, "Per Unit" expenses were rounded to the nearest $0.05 and "% of Prem" expenses were rounded to the nearest percent.

The results of the calculations for the 2003 based on 2001 published Statutory information are shown in Exhibit 1 (2003 GRET Factor Comparison) on the following page.

When the results were presented to the NAIC members of the Life and Health Actuarial Task Force (LHATF), questions were raised about the decrease in branch office company expenses versus the increase in "Other" company expenses. The latter category is a group that includes many stock life insurance companies.

Further analysis of expenses for the two categories showed that when compared the base LOMA expense factors that are used to allocate expenses by function in the study, showed that the branch office expenses had held fairly steady of the past two years when compared to the base expense factors while the other Company category showed an increase. See Exhibit II. (GRET Comp Charts) on page 13. This may be due at least in part to the reduction in expenses following the numerous demutualizations that have taken place and should not be viewed as a negative commentary on other company expenses.

In New Orleans, the LHATF voted to recommend adoption of the revised GRET, and that recommendation was approved by the Life Insurance and Annuities (A) Committee. The final step is consideration of this recommendation by the full NAIC membership in San Diego in December.

GRET Factor Comparison

		2001 Factors	2003 Factors	Percent of 2001 Factors
Branch Office	**Acq**			
	Per Policy	$70.00	$66.00	94%
	Per Unit	$1.25	$1.15	92%
	% of Prem	78%	73%	94%
	Maint			
	Per Policy	$35.00	$33.00	94%
Direct Marketing	**Acq**			
	Per Policy	$87.00	$80.00	92%
	Per Unit	$1.55	$1.40	90%
	% of Prem	48%	44%	92%
	Maint			
	Per Policy	$43.00	$40.00	93%
Home Service	**Acq**			
	Per Policy	$60.00	$61.00	102%
	Per Unit	$1.05	$1.40	105%
	% of Prem	33%	44%	103%
	Maint			
	Per Policy	$43.00	$40.00	103%
Other	**Acq**			
	Per Policy	$78.00	$85.00	109%
	Per Unit	$1.40	$1.50	107%
	% of Prem	43%	47%	109%
	Maint			
	Per Policy	$39.00	$39.00	110%
Total–Weighted by Actual Expenses	**Acq**			
	Per Policy	$73.09	$73.74	101%
	Per Unit	$1.31	$1.29	99%
	% of Prem	$0.63	$0.60	95%
	Maint			
	Per Policy	$36.53	$37.10	102%

Comparison of Actual to Expected Using Unadjusted LOMA Seed Factors