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Update on Preferred and PreNeed Valuation Mortality Tables

By Roger K. Annin

Two committees continue work on experience studies that will provide a basis for new valuation mortality tables. The first committee is the Preferred Mortality Project Oversight Group and the second is the PreNeed Valuation Project Oversight Group. This article summarizes activity to date for these committees.

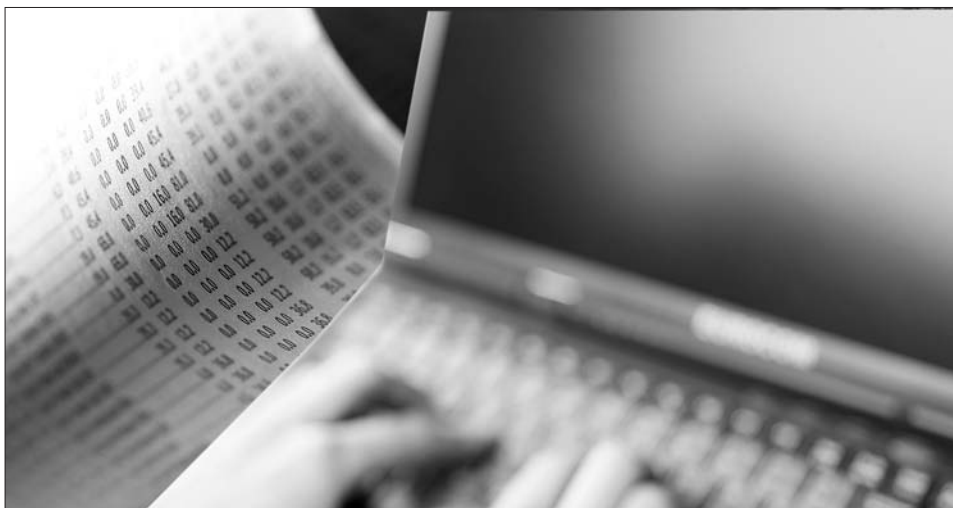
Preferred Mortality Project Oversight Group

This is a joint committee of the Society of Actuaries (SOA) and the American Academy of Actuaries. The committee was formed to respond to requests from the NAIC for the development of preferred mortality valuation tables. The need for such tables is actively supported by industry groups such as the ACLI and will form a foundation for Principle-Based Reserves (PBR).

A number of “teams” have been formed to address specific aspects of the project. The list includes:

- Data Validation Team—validates company contributions and resolves questions related to data quality.
- Underwriting Criteria Team—evaluate underwriting guidelines used by companies in determining preferred risk classifications.
- Experience Analysis Team—develop initial experience tables.
- Valuation Basic Tables Team—develop basic tables from experience analysis results.

Data Contribution. To date, approximately 50 companies have contributed data for this experience study. This compares to 21 contributing companies for the 2001 VBT. However, this project calls for more than just experience contributions.



In order to evaluate experience by underwriting class, each contributing company is also asked to submit their underwriting criteria. The underwriting criteria team has developed an algorithm that will enable the POG to combine data for similarly classified policies. This effort requires a combination of data analysis and actuarial judgment. The algorithm will be tested initially against a subset of data, hopefully during April.

Funding and Timing. A project of this scope requires a dedicated effort on the part of many volunteers. It also requires funding to support hard costs for data tabulation and various levels of analysis.

The costs for this special study fall outside the SOA’s normal life experience study budget. Therefore, a special assessment is needed to raise funds to complete the project. The POG has been actively involved with the SOA in addressing approaches to fund the cost. The objective is to spread the cost across the industry in a fashion that reflects the benefits companies will realize from the new tables. For example, this implies a higher expectation for writers of term insurance and universal life where preferred classes are more common.

The project timeline will undoubtedly undergo revisions as the project moves forward. However, the goal is to present results and recommendations to LHATF in the last quarter of 2006, with expected adoption of the tables in 2007.

ACLI Interim Proposal. Because of the time needed to formulate, present and adopt new preferred risk valuation tables, the ACLI has offered an interim proposal. Although not directly linked to the POG’s efforts, it is interesting to examine the ACLI proposal. This proposal was initially presented to LHATF in December and LHATF has referred the proposed factors recommended by the ACLI to the SOA for review.

Under the ACLI proposal, there would be three Nonsmoker valuation classes—Super Preferred, Preferred and Standard. There would be two classes for Smokers, Preferred and Standard. The table below provides a brief overview of the mortality ratios proposed by the ACLI.

Preferred Mortality Ratios ACLI Proposed to 2001 VBT, ANB, Select/Ultimate

Super Preferred Male Nonsmoker

Age	Dur 1	Dur 5	Dur 10	Dur 15	Dur 20
25	51%	51%	50%	50%	50%
35	52%	51%	50%	50%	53%
45	50%	50%	50%	50%	50%
55	50%	50%	50%	50%	55%

Preferred Male Nonsmoker

Age	Dur 1	Dur 5	Dur 10	Dur 15	Dur 20
25	71%	70%	70%	70%	70%
35	71%	70%	70%	70%	72%
45	70%	70%	70%	70%	70%
55	70%	70%	70%	70%	73%

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It might be noted that one goal of the ACLI proposal is to apply factors to the 2001 Table so that effectively, the preferred tables will not represent a new valuation table...

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Residual Standard Male Nonsmoker

Age	Dur 1	Dur 5	Dur 10	Dur 15	Dur 20
25	117%	117%	117%	117%	117%
35	116%	118%	117%	117%	116%
45	117%	117%	117%	117%	117%
55	117%	117%	117%	117%	116%

Ratios for female lives are very similar to males for Nonsmokers. Smoker ratios are about 70 percent for all durations for preferred risks and 113 percent for residual standard.

It might be noted that one goal of the ACLI proposal is to apply factors to the 2001 Table so that effectively, the preferred tables will not represent a new valuation table, but rather a breakdown of the existing table. Under the ACLI proposal, super preferred risks are assumed to account for 15 percent of business, preferred risks account for 15 percent and standard account for 70 percent. Mathematically, these ratios applied to the table ratios above add back to 100 percent of the 2001 Table.

PreNeed Valuation Table

A PreNeed Valuation Table Project Oversight Group also exists to examine mortality experience of companies in this market. PreNeed plans are sold as funding vehicles for pre-paid funeral arrangements. Policies in this market are sold directly through funeral homes and have very limited underwriting. Most business is single premium, but some multi-pay plans exist as well.

Concern exists that the 2001 Table does not adequately represent experience for this market. In fact, most company studies show the 2001 Table mortality falling well below levels seen in the PreNeed market. In addition, the slope of the mortality curve for PreNeed business may be quite different from underwritten business. A reverse select period has been identified in preliminary data analyzed by the POG.

Data Contributions. In this study, 10 companies have contributed data with adequate deaths to provide credibility.

Credibility is more easily obtained for this market due to the high average issue age and higher frequency rates experienced.

The POG is currently tabulating and reviewing data and expects to make a formal report to LHATF at their June meeting. It is anticipated that a proposed valuation table may be offered as early as the September LHATF meeting for this market.

Coordination with Principle-Based Reserves

As stated earlier, these new valuation tables will provide a foundation for PBR. As such, the co-chair of the American Academy of Actuaries Life Reserves Working Group has discussed with the Preferred Mortality POG expectations of that group in regard to new valuation tables.

The general philosophy is that under PBR, companies will look to their own mortality experience, but then blend such experience with industry (NAIC approved) tables to gain credibility. Under this approach, industry tables will need to reflect the mortality expectations for the risk class. As such, industry tables will need to span a range of mortality experience based on underwriting and market guidelines. Tables that are both more aggressive and more conservative than current tables will be needed.

Companies would not be limited to a specific valuation table. Multiple tables might be used depending on the spread of risk and markets addressed by the company's products. Indications from the LRWG are that as many as 10 tables may be needed to properly address the spread of risks envisioned. This implies multiple levels of preferred underwriting and more conservative tables for simplified issue and PreNeed markets.

Summary

Work is moving forward at a fairly rapid pace in the valuation area. Substantial time at LHATF meetings is devoted to PBR and the mortality tables needed to form a foundation for more dynamic reserves.

Over the remainder of this year, we expect to see experience data from both the Preferred Mortality study and the PreNeed Mortality study. Undoubtedly, the ACLI proposal will continue to garner attention as an interim solution to conservative valuation mortality for the preferred risk classifications.

Much of the activity of these groups can be easily tracked through www.soa.org and www.actuary.org. ●



Roger K. Annin, FSA, MAAA, is senior vice president and principal with Lewis & Ellis, Inc., Actuaries and Consultants in Overland Park, Kan. He can be reached at RAnnin@lewisellis.com.