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Jim Anderson's Predictions

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Summary: During his lifetime, James C. H. Anderson published many papers that contained predictions of the future. Many of his predictions were accurate, but, inevitably, others were incorrect to a greater or lesser extent.

Focusing on Anderson's predictions, the speaker reviews the limitations on the actuary's ability to predict the future. He discusses why predictions—even those made by knowledgeable students of the future—may not always be completely accurate. Was a trend overlooked? Was there an unanticipated event or "wild card"?

Mr. Albert E. Easton: As many of you probably know, the Futurism Section just completed a Delphi study. In the Delphi study, we had a series of 25 items and we asked people to make numerical predictions about things that would be taking place in 2010 and 2050.

As we analyzed the results of the Delphi study, it occurred to us to stop and think about what it is that leads people to make predictions and how they go about making them. We identified a series of things. First and most basic is the analysis of trends.

Actuaries do a pretty good job on the first two kinds of trends: economic trends and demographic trends. In fact, there are some who think that demographic trends, because they deal with people, really control almost everything else. As a society, we have limited control over birth and death, and very little control over most individual actions. But we have an understanding of the likely demographic outcomes and those have a marked influence on the economic, social, and political trends.

Actuaries are able to do a good job of projecting demographic trends, and usually a fairly good job of projecting economic trends, to the extent that they can be predicted. We probably don't do quite as good a job in predicting the interactions between people that lead to social trends. Political trends may be the most difficult of all to project because they sometimes are quixotic, like the weather. There are things that are just very difficult to project in terms of political trends.

Someone who is very good at making predictions will also try to analyze the interactions between trends. If he or she is aware of social trends and political trends that are headed in opposite directions, he or she will keep in mind that there will be a conflict there and try to see how that conflict will resolve itself.

A third item that someone might keep in mind, which is really a little different from trends, is “straws in the wind,” a metaphor from hurricane forecasting. If you see straws in the wind, you know a hurricane is coming. For actuaries, straws in the wind indicate that there might be a discontinuity coming, and if you're able to spot them and know what they are, then you'll be able to predict the discontinuity.

Finally, there are wild cards in discontinuities—things like a stock market crash or a major war—that really would be difficult for anybody to predict.

It takes an unusually perceptive thinker to put together the right analysis of trends and trend interactions to make a good prediction. It takes a real visionary to also be able to anticipate wild cards in discontinuities. Fortunately, Jim Anderson had those qualities. I'm going to read a page from Jim's biography so that those of you who don't know a lot about his background will know a little bit more about him.

"Jim Anderson was born in Winnipeg, Canada in 1931. He was a 1952 graduate of the University of Manitoba. His extraordinary abilities were evident at an early age, and his strong sense of values and fairness was well formed before he entered the business world. During his college years, Jim gathered experience with Great West Life, and Massachusetts Mutual. After graduation, he joined the staff of Northwestern Mutual in Milwaukee. In 1955, he accepted a position as actuary of Family Fund Life in Atlanta. In 1958, he entered the consulting field in Atlanta, with the firm of Bowles, Andrews, and Towne. While with Bowles, Andrews, and Towne, Jim wrote a paper that was to make him famous. And it is probably his best known and maybe one of the best known papers in actuarial literature. It was titled "Gross Premium Calculations and Profit Measurement for Non-Participating Insurance" and was published in the TSA in 1959. Jim was awarded the Society's triennial prize for that paper. "The approach presented in this paper serves as a basis for most of today's insurance pricing and appraisal work, both in the U.S. and abroad. In 1959, Jim became a vice president of Georgia International Life Insurance Company. Ten years later, he was elected president of Abbey International Corporation in Atlanta, which specialized in the design and marketing of equity-linked products in several countries. For part of this time, he was also managing director of Abbey Life in London, England.

"Jim returned to consulting in Atlanta in 1972 with the firm of Bowles and Tillinghast, and was named its president in 1974. The firm prospered under his leadership and grew from 2 offices in Atlanta and Dallas to 28 offices in 7 countries.

The firm underwent several name changes over the years, and finally became known as Tillinghast. During these years, Jim continued to enhance his reputation as an innovative thinker, and a pioneer in new products and marketing strategies.

"He was an early advocate of the universal life (UL) concept and became internationally renowned for his understanding of the changes that had taken place in the insurance industry. Jim was truly a giant in the insurance industry and the actuarial profession. He died on August 5, 1993 at his home in Atlanta."

What we hope to do is to read some selections from some of Jim's many papers, which have been published by the Actuarial Education and Research Fund. I'm sure you could, if you're interested, get a copy of this from the SOA. A CD-ROM is also available.

As we read these papers, I want you to think about what the trends were that Jim was observing, or what wild cards he was anticipating that led him to make the predictions that he did. Then we can briefly talk about whether what he predicted actually happened. As we found out in trying to interpret the results of the 1989 Delphi study, whose time horizon has now elapsed, it isn't always easy to tell whether a prediction actually happened.

By the way, I'm sure there are many people here who knew Jim Anderson much better than I did. I only met him a few times in his lifetime. It seems clear though, from his writings, that some of his predictions may have been to make a point. I want to overlook that. I want to work on his predictions, as if what he was trying to say was really what he expected to happen. We'll work on it from that basis. If only it were possible, it would be great to have Jim do the reading himself. However, since it's not, I've had to ask some other people to do the reading in his place.

The first prediction we're going to read this morning is one of Jim's best known predictions. It was originally published in *Emphasis*, which is a publication of Tillinghast, in 1975 as a paper titled "The Universal Life Insurance Policy." I've asked Frank Hacker to read it for us. It's important to understand that there actually were no UL insurance policies in existence when this was published.

Mr. Frank A. Hacker: "What would be the impact on the life insurance industry of a successful introduction of the Universal Life Insurance Policy? What practical considerations would effect the manner of introduction of such a product, and its likely success? How would the industry respond? To suggest answers to these questions, the following scenario is offered.

"Cannibal Life is a medium-sized stock life insurance company, owned by a powerful non-financial company. Its management and that of its parent company are aggressive and non-traditional. Its agency organization is traditional and commission-oriented. At the urging of the parent company, Cannibal Life decides to adopt a completely new marketing strategy, designed to achieve major market penetration. It decides to withdraw all currently issued life insurance plans and to offer only the universal life insurance policy, not withstanding the risk of losing its entire agency organization.

"It decides that it will make a conversion offer to all existing policyholders. Furthermore, it decides to take the unprecedented step of offering to convert, without evidence of insurability, life insurance policies issued by other companies on the same terms as are being offered to its own policyholders. Although a no-load offer is to be made both to its own policyholders and to policyholders of other companies, Cannibal Life intends to pay commissions on such conversions at the usual rates. Existing policyholders are to be notified that they can consolidate all of their life insurance policies with all companies into one universal life insurance policy.

"Cannibal Life intends to support its marketing strategy through an aggressive public relations and advertising program, particularly including efforts to enlist the sympathy of activist consumer groups. This is a vital aspect of the marketing strategy, as will appear later.

"The new marketing strategy is unveiled to the agency organization, and launched with great public fanfare. Company representatives call press conferences, and appear with consumer advocates on television interview programs. Their comments regarding traditional life insurance products are not kind. Notwithstanding the radical reduction in commission rates, the agency organization is enthusiastic because of the income opportunities afforded by the conversion program and the confidence generated by the widespread publicity. The conversion program is highly successful and Cannibal Life's expectation that business would increase by 100% within 1 year, is surpassed. On average, each of its own policyholders converts one additional policy issued by another company, and many policyholders of other companies also convert their policies. Although the profitability of the new contract is significantly lower than that of existing business, Cannibal Life is able to increase its aggregate GAAP earnings on the increased line of business (previously capitalized acquisition expenses are charged off as an extraordinary item). Its agency organization also prospers and grows. Large statutory losses are incurred, but these are absorbed by tax recoveries and by a substantial infusion of capital from the parent company.

"Cannibal Life realizes that the conversion program is not a permanent source of new business. As a follow-up strategy, Cannibal Life decides to mount the major effort to capture a large share of the juvenile market by offering a special variation of the universal life insurance policy, specifically tailored to the needs of this market. The sales program promotes the product as 'The Only Life Insurance Policy Your Child Will Ever Need.' Because premiums in the juvenile plan are relatively low and commissions are relatively high, the reception by the agency organization is again enthusiastic and the customer base of Cannibal Life is greatly expanded, thus ensuring a future flow of business. Cannibal Life also decides to mass market its new contract through employers and associations and, for this purpose, undertakes to develop a specialized agency organization, which in the long term becomes its principal source of new customers. Eventually, its original agency organization will be disbanded and replaced by a new service-oriented organization designed to maintain its established customer relationships; this organization will be composed primarily of women. The new marketing strategy is a huge success, and Cannibal Life becomes a market leader in the individual insurance business.

"The activities of Cannibal Life do not go unnoticed. Through regulatory agencies, life insurance industry and agent associations attempt to block Cannibal Life's conversion program, but these effects are unsuccessful, due largely to the public outcry by activist consumer groups. A temporary injunction is obtained against Cannibal Life, but the request for permanent injunction is denied. In its opinion, the Court observes, 'To grant the relief sought would be tantamount to accepting the view that a class action suit on behalf of mousetrap makers against the maker of a better mousetrap is valid.' The court decision receives the attention of the national media, including network television. Cannibal Life receives large numbers of applications for employment from agents of other companies, many of whom are hired. Conversions of other company's policies increase dramatically.

"The activities at Cannibal Life also attract the attention of four national retail organizations, all of which are already engaged in financial service business; these companies decide to introduce similar products, and to market them on a non-agency basis through retail outlets. Similar action, based on a direct-mail approach, is taken by the sponsors of two nationally recognized credit cards. Several life insurance companies of various sizes, including one sponsored by a credit union association, adopt a marketing strategy similar to that of Cannibal Life. All of these entries are reasonably successful.

"The impact on the rest of the life insurance industry is now quite severe. A major decline in sales is experienced, accompanied by a substantial loss of agency manpower, leading to a further decline in sales. Surrenders increase to the extent of causing a negative cash flow. Investment losses are incurred on the liquidation of investments to meet cash-flow requirements; to minimize investment losses, higher yielding assets are sold, and portfolio investment returns decline. The loss of sales and business in force and the reduced investment returns cause an expense and earnings crisis, which is temporarily masked by large surrender profits under statutory accounting. Most stock life insurance companies report GAAP losses due to the write-off of unrecoverable, deferred acquisition costs. Mutual companies are forced to reduce dividends. Life insurance company share prices fall precipitously.

"Due to the decrease in business and the associated reversal of the effect of certain tax elections, most companies incur a substantial increase in federal income taxes on current income, and some companies are subject to Phase III taxes on prior year's income previously deferred. Some companies decide to suspend writing business to avoid insolvency, and there are numerous consolidations within the industry involving both stock and mutual companies.

"Eventually, the surviving companies also introduce similar products, and adopt similar marketing strategies. Gradually, stability returns to the industry, but market shares within the industry are substantially and permanently rearranged, and distribution systems are fundamentally altered. Following a period of adjustment, industry penetration of individual savings markets increases to record levels."

Mr. Easton: How many think that all of Cannibal Life actually happened? Nobody? Good. How many think that some parts of Cannibal Life actually happened? More than half. I'd be interested in people who would like to comment at this point on why they think parts of it did or didn't happen.

Mr. Hacker: Yes. I see that part of Cannibal Life did happen, especially if you consider this is a prediction made in 1975. UL has turned out to be a product of great influence in the marketplace. Some companies have adopted UL to the exclusion of other products. We have seen those types of conversion programs. I think that all in all, this was a remarkable vision of the future by somebody who made the prediction four years before there was even such a product.

From the Floor: A lot of it rang true. I actually worked with Jim on the development of some early UL products. One of the things that he was pushing was a much lower commission strategy. His idea was to make commission a low function of premium and face amount, plus sort of lump sum per policy. You'd get very attractive returns on big policies. However, the field force of the powers that be did not allow that to happen. If you look at what happened to commissions with UL coming in, in fact, they didn't change. If anything, they went up, so that one didn't work. We never really got into the juvenile policy. I don't know if any companies did do that, but a lot of that replacement activity did happen that was predicted.

Mr. Easton: Certainly there was a lot of replacement activity. I don't think that the juvenile policy as such took place, but the early UL policies were sold with the idea that they were the only policy that you'd ever need.

From the Floor: Right, and, in fact, the early ones were that flexible. They did become less flexible as you tried to fit traditional commissions into them. It was interesting.

Mr. Tom Bakos: I want to raise a question. It seems to me that UL took off, not so much because of its design or because it was the one product that anybody would ever need, but because interest rates were particularly high in the early 1980s. The design just happened to allow that feature to be emphasized, and that's what drove the replacement activity. I don't know whether Jim Anderson predicted the high interest-rate environment, or if anybody could have. It's one of those wild cards.

Mr. Easton: I do think that part of his thinking in the design of the UL policy was based on the fact that interest rates were going up, and the traditional product design was not flexible enough to recognize that.

I don't know how well he predicted this, but after interest rates went up, interest rates came back down. UL insurance policies were somewhat better at being able to deal with that than the traditional product design, because a tradition had grown up that dividend scales were carved in stone. It was only with great reluctance that dividend scales began to be cut when interest rates came down.

I'm going to move on to another paper. The next selection that we're going to read is from a paper called "The Alternative Futures of the Life Insurance Industry." This was presented at a Life Office Management Association seminar in 1978. John Yanko will read this, and he will pause in a couple of places, as he goes through it, so that we can discuss a couple of points.

Mr. John B. Yanko: "What are the alternative futures of the life insurance industry? To stimulate more than to instruct, this question will be addressed by presenting a series of five scenarios. To add an Orwellian touch, each of the scenarios has a setting in 1984. The scenarios have a common background:

"The decline of the traditional family as a basic unit of society has continued. The birth rate, which dropped from below the zero population growth level in the early 1970s, has gradually increased and stabilized at approximately the zero population growth rate. The generation gap has not closed.

"A coin telephone call now costs 25 cents. The rate of inflation, while still high, is down from the dizzying heights of the early years. And 5% inflation is considered an acceptable target. The widely followed prime interest rate, after touching 12%, has receded to 8% as inflation subsided. Talk about a pending energy crisis continues. But its expected arrival has been postponed several times.

"Supersonic travel is now fairly routine. Following the introduction of the more efficient, extended-range Concorde II and the success of the Russian built supersonic transport, dubbed Concordski, American aircraft makers are racing to catch up with the rocket-powered model, which will fly at altitudes that make supersonic overland travel practical.

"The U.S. is preparing for what looks like a hotly contested Presidential election, with Republicans bent on recapturing the White House on the basis of the pragmatic policy, 'If you can't beat them, join them.' In general, although old problems remain unsolved, these are peaceful and prosperous years. It may be that the 1980s will be judged by historians as a decade of toleration.

"In this environment, the life insurance industry continues to operate, but how? The following scenarios are intended to suggest various possibilities."

Mr. Easton: I wanted to pause here so that we can reflect on some of the predictions that he's made about society in general. Certainly phone calls did cost 25 cents, but he was wrong about inflation subsiding. It didn't subside right away. It continued even higher in the early 1980s, and finally began to subside after interest rates reached record levels. He mentioned a prime interest rate touching 12%. I think the prime interest rate finally got up to 17% before it started back down.

He was wrong in his analysis of the Soviet Union. People in 1978 thought that the Soviet Union was much more powerful and economically well provided for than it actually was. There was never a Concordski and the Soviet economy, as we all now know, probably never would have been able to support something like that.

The Republicans were not bent on recapturing the White House in 1984 because they already had it. They had succeeded in replacing Jimmy Carter, who looked like a very popular president, in 1978. By 1980, Jimmy Carter was a much less popular president. We had had an Iranian hostage crisis, a typical wild card. Also, the economic situation in 1980 led the American people to elect a president from another party.

Jim was not quite right in analyzing some of the trends. He didn't quite anticipate how extreme inflation and interest would become, and he wasn't able to follow a couple of other things, based on what the general knowledge was in 1978. Let's go on with the scenario, John.

Mr. Yanko: "Scenario 1: Business (Almost) As Usual. In defiance of all the prophecies, the life insurance industry continues to flourish and grow. The industry continues to receive the majority of its income from traditional, permanent insurance products, notwithstanding the continued rise in term insurance sales and the introduction of various "open track" policies, carrying significantly lower commissions. The industry continues to distribute its wares through the agency system, despite a continuing decline in the number of full-time agents, and the development of a scattering of non-agency distribution methods. Most agents now make extensive use of computer terminals as a point-of-sale aid. Recently, there has been a decrease in sales by number of policies.

"The number of free-standing stock life insurance companies has reduced and life insurance company shares continue to sell at substantial discounts from their intrinsic values, leading to a continuation of the trend for non-financial companies to acquire life insurance companies. Fears relating to the possible underpricing of individual life insurance products from the middle of the 1970s forward have proven to be unfounded. High interest rates and substantially improved mortality has resulted in higher than expected earnings and dividends.

"While prophecies of doom continue, the prophets themselves, not including one aging actuary in Atlanta, have largely been discredited.

"Scenario II: Big Brother Arrives. The date is Friday, June 29. In its race towards the summer recess for the July 4 holiday and the ensuing national conventions, Congress has just put the finishing touches on what will probably be the biggest watermelon cutting in history, the Financial Security Act of 1984.

"Together with existing legislation, the new act provides cradle-to-grave coverage on a heretofore unimagined scale. Social Security benefits have been increased well beyond the subsistence level, and the coverage is now universal. A feature of the new act is a variable retirement age, with a corresponding adjustment of retirement benefits. This feature, together with expansion of benefits, gives the program many of the aspects of private pension plans.

"Previous legislation mandating national health insurance has been scrapped in favor of a government-sponsored plan. A spokesman for the American Council of Life Insurance bitterly observed, 'This act marks the end of private health insurance, and may be the beginning of the end of private medical care, private pension plans, and private savings.

"Scenario III: Götterdämmerung. The date is Friday, April 15. The place is the Office of the Treasurer of the Preservation Mutual Life Insurance Company. The cash report for the week shows that the cash outflow for its benefits, expenses, surrenders, and policy allowance, partly due to the income tax deadline, has reached 300% of total cash in flow. As usual, many of the surrendering policies are assigned to Cannibal Life. Preservation Mutual has experienced negative cash flow for four consecutive years, and has already sold all investments realizable without incurring capital losses. Since long-term interest rates are now in excess of 10%, the company has a substantial, unrealized depreciation on its remaining portfolio of bonds and mortgages. To avoid recognizing losses, it has incurred substantial bank debt on which the interest differential is significantly adverse.

"The office is conspicuously empty. Two years ago, the investment department was disbanded, since the company had no funds to invest. The sales department has also been disbanded, since the company ceased writing new business to protect its solvency.

"Scenario IV: Doomsday. The date is Thursday, December 30. Since New Year's Day falls on Saturday, this is the last business day of the year. The Vice President for Sales is reviewing results for 1984. He knows that business is up 10% over the previous year, measured by face amounts of insurance. Company-wide sales have reached $1 billion for the first time in history, a milestone, which gives satisfaction to all. Aggregate new premium income, however, is only $5 million, a decline of 50% over the previous 5 years.

"A review of the sales results indicates that the company did business with 2000 brokers during the past year, each producing an average of 10 sales for a total of $2,500 of premium income and $1,000 of commission. Ninety-eight percent of new business was term insurance.

"Scenario V: Revolution. The scene is the employee's lounge at the Acme Manufacturing Company. In a semi-darkened room, a group of employees is watching a television screen on which a videotape presentation is playing. The film explains how proper planning, using the right tools, can provide a means of achieving personal financial goals. The film illustrates how a computer can assist in identifying the right tools to achieve particular goals.

"At the end of the presentation, the audience is invited to make use of self-operated computer terminals along the wall of the lounge to identify which tools are best suited to help achieve their financial goals. Personal advisors, they are told, are available to help with the operation of the computer terminals and to help interpret the results.

"The company sponsoring this personal financial planning seminar is a member of a financial complex offering a wide range of financial services, including innovative life insurance contracts, which provide complete flexibility to meet changing circumstances. Its sales representatives are salaried employees. The 1,000-man sales organization provides national coverage. For the year 1984, the company expects to sell more than 200,000 policies with a face amount in excess of $10 billion, along with a substantial volume of other financial security products.

"In addition to its sales organization, the company maintains a large service organization, which communicates regularly with customers. The system is customer-oriented, not sales-oriented. It is comprised primarily of women."

Mr. Easton: I'm not sure whether Jim intended these scenarios to be independent of each other. Quite often in scenario building, you try to put together a number of complete scenarios, only one of which can exist. I see elements in all five of these scenarios that actually did happen. I'm going to ask you to indicate which of these scenarios you think was closest to what happened in the mid 1980s.

Scenario I: Business (Almost) As Usual. How many think that that was what happened in the mid 1980s? One person.

Scenario II: Big Brother Arrives. The Financial Security Act of 1984 is passed. A spokesperson for the ACLI says that this act marks the end of private health insurance and maybe the beginning of the end of private medical care, private pension plans, and private savings. How many think any part of that happened? Nobody.

Scenario III: Götterdämmerung, which was a company running out funds. Cash flow was negative and they had already sold all the investments that they could without taking a capital loss. How many saw anything like that happening in the mid 1980s? We all saw that! It didn't happen in every company, but there were certainly some companies that ran out of cash because of the disintermediation in the mid 1980s. Jim was only thinking of a 10% interest rate.

Scenario IV: Doomsday. I guess this is doomsday because the sales organization has taken a walk. They're selling almost solely through brokers, and there are 2,000 brokers. Each has a premium income of about $2,500 and $1,000 of commissions. How many have seen something like that happen? That has happened to a few companies; not very many, but there certainly has been some increase in the amount of sales that take place that way.

Finally, Scenario V: Revolution—selling through computer terminals and selling what sounds like a UL insurance policy, although he doesn't call it that in his scenario. Anybody see anything like that happening? OK. I'd welcome any comments that anybody wants to make on these scenarios.

Mr. George L. Engel: I thought I might as well, since I was the only one voting for number one—at least defend it a little bit. You did say business as usual, and my company, Aid Association for Lutherans, was one of the companies that was the opposite of that. We increased from less than $10 billion in force to over $50 billion in force in the 1980s because of UL. When you look at that, number one doesn't look like the most obvious answer, but I guess I was focusing on the computer terminals as a sales aid. That was something we were getting into at about that time, and also the high interest hits and good mortality. Those two things, I thought, made that a relatively accurate scenario.

Mr. Easton: Jim did a good job of understanding effects that high interest rates and improving mortality would have on the insurance industry, and that's why he was able to predict some of the things that are in these scenarios.

There's another part of this paper that I think is worth reading. It has some of Jim's suggestions for the actions that a company should take to respond to what was coming.

Mr. Yanko: "If the appraisal of the current state of the industry is realistic, business (almost as usual) is not a reasonable hypothesis for the future. Accordingly, the industry must, if it wishes to control its own destiny, take positive steps to correct the fundamental problems addressed in this discussion. The following is a suggested list of action assignments:

1. Premium rates for term insurance should be increased to make it less attractive to package these products with other savings media. Commission rates for the term insurance should also be increased to the highest levels offered on any products.
2. Premium rates for permanent insurance should be reduced or dividends increased and cash-value structures appropriately modified so that the marginal costs associated with a savings element of these products becomes competitive with other savings media. This implies a radical reduction of commission rates on permanent insurance and the probable elimination of the front-end load associated with the savings elements of these products.
3. New products, affording much increased flexibility, should be developed. This will be much more easily accomplished if commissions on the savings element are reduced.
4. To the extent that agency distribution methods are expected to continue, it follows that productivity must be substantially increased from present levels to support the income expectations of agents. This will require sophisticated marketing support.
5. The industry should lobby for modifications in the present federal income tax legislation, which imposes a large and growing burden on the investment

earnings of policyholders. The industry should also lobby for an elimination of premium taxes, at least to the extent that they apply to savings accumulations.
6. The industry should abandon its dependence on artificial tax avoidance, such as minimum deposit, and concentrate on serving more efficiently the family market of the mainstream population. To have realistic expectations of success in lobbying for a reduction in taxes, it will probably be necessary to sacrifice some existing tax concessions.
7. The industry should concentrate on conserving its existing business and perhaps, more importantly, its existing customer base. The truism of the future may be: 'Our customers are our most valuable assets.' Conservation efforts may include the need to pay voluntarily interest profits on policies, a practice adopted several years ago in the Netherlands.

"I'm not suggesting that it will be easy to implement any of the foregoing action assignments. How, for example, can one company take the lead in increasing term insurance premiums without losing a substantial portion of its market share? Nevertheless, solutions must be found. Perhaps a form of adjustable life, hopefully simpler than the existing forms, will be the key to the restructuring of the relative cost of term and permanent insurance, and perhaps some variation of this product will afford the necessary increase in flexibility. Perhaps such a product, supported by point-of-sale computer terminals, will lead to the necessary increase in agent productivity. Perhaps such products can be designed to mitigate the effect of federal income taxes on investment earnings of policyholders.

"I'm not suggesting that adjustable life is the all-encompassing panacea, the long sought Holy Grail. Obviously, it does not address several of the problems and there may be other and better solutions.

"I am, however, expressing the view that the most likely and the most attractive solution to the various problems I noted will be found in a new product form."

Mr. Easton: Some of the things that he recommended happened. Number one, increasing rates for term insurance definitely did not happen. In fact, the opposite happened. Term insurance rates went down. Jim Anderson was not alone in calling for increases in term insurance rates in those days. And there have been others since. But in spite of all that, term insurance rates were low and have continued to be low. They may be bouncing up a little bit now because of Regulation XXX, but, in general, term insurance rates did not and probably will not go down.

Premium rates for permanent insurance were reduced, and, as he suggests, the marginal cost of the savings element has become somewhat consistent with other savings media. New products with increased flexibility have certainly come about. I'm not sure that productivity for agency distribution has really been increased in any sense.
The industry did lobby, to some degree successfully, for modifications in the federal income tax. At least insurance companies are no longer taxed directly on investment income as they were in 1978. On the other hand, I'm not sure that

most would agree that the burden of federal income tax is any easier to bear now than it was at that time.

And I'm not sure that the industry has completely abandoned its dependence on artificial tax avoidance. Although some of the gimmicks that were available at that time, such as minimum deposit, are no longer available under current tax law, deferred annuities continue to be sold primarily for tax deferral.

And finally, I think most companies would agree that this slogan, "Our customers are our most valuable asset," has actually been adopted.

The next selection is from a somewhat later time, 1985. By this time, Jim was, I'm sure, looking back on his predictions and his five scenarios for 1984. He was realizing that the distribution system was going to be a little tougher to reform than had first been apparent. Frank Hacker will read this selection from 1985, dealing with distribution systems.

Mr. Hacker: This one is titled "How To Get Ready."

"From the viewpoint of the distributor of life insurance products, the real revolution is only now beginning. How can he or she prepare for the coming of the revolution? Some suggestions:

"The producer should seek ways to lock in his existing customer base, and seek ways to expand it. Insurance companies, banks, and others will be striving for exactly the same objective, even at the expense of the intermediary. Each participant will be trying to stake out as protected territory, a controlled customer base, and will attempt to make it as difficult as possible for any competitor to encroach upon his territory. If the independent intermediary is to be an important participant in the future, it will be because he alone is seen as having access to a defined customer base. Part of the process of protecting the customer base is to minimize the opportunity for encroachment by others, by providing the widest practical range of services.

"The independent intermediary must be prepared for a world in which compensation may no longer be exclusively or even primarily based on sales commissions. Negotiated commissions and fees are a likely development in the immediate future. And signs of this change are already apparent in the recent Florida appeals court decision concerning rebating and in scattered signs of the appearance of no-load products in the individual life insurance business. Plans for this change should be formulated now, and should include decisions as to the appropriate fee levels which will be charged and advice as to the circumstances under which fees and commissions may be legally charged.

"In addition to his customer base, the strength of the independent intermediary rests importantly on his abilities and motivation as an individual entrepreneur. The distribution of life insurance and allied products is not an activity easily supervised, and life insurance companies and other participants in the financial services business will be reluctant to move toward some of the fixed-cost distribution alternatives, such as those involving salaried representatives. Except for those engaged in location selling, few have the skills and personnel necessary to adequately supervise a noncommissioned distribution system. If the independent intermediary is prepared to price his services at a level at which he will not be driven out of the marketplace by consumer-oriented competitors, he still will enjoy and occupy an important position in the future distribution of life insurance and related products.

"Will the independent intermediary of the future be tied more or less to a primary company than he is today? With a few notable exceptions, the existing distribution system seems, more likely than not, to move towards multicompany representation, and away from single or primary company representation. In competing for the business of independent intermediaries, insurance companies are likely to expand their salaried staffs and other activities supporting such intermediaries to better secure the continuing services of such intermediaries.

"The future role of the independent entrepreneur, as a distribution of financial products, will stress 'advising' rather than 'selling.' The premium value of product knowledge is likely to increase at the expense of selling skills. Most distributors will find SEC registration a necessity.

And now, let the real revolution begin."

Mr. Easton: I'd be interested in your comments on how much of Jim's prediction on the distribution system you think has taken place.

Mr. Bakos: Again, I think he was pretty accurate. Obviously, it depends on what level of sale you're looking at. In the higher-income, more sophisticated markets, agents and producers feel they have to represent more than one company or have products available from more than one company. That multicompany representation is certainly there. And with variable life products becoming a very significant part of the product mix, the producer needs to be SEC-registered. In those respects he was right on.

From the Floor: Again I agree with Tom. I think he got more right in this one than he normally did. I took down five points, and the first one about the importance of locking in existing customers because every other financial institution will be after the customer base is true nowadays. It was interesting to hear a Wells Fargo guy saying they're looking for 100% of the customer's wallet nowadays. They're going for every financial product they can.

Jim was always keen on getting rid of commissions. And that has never really happened. He was always a no-load and fee-for-service guy, and that really hasn't happened.

About the agent as the individual entrepreneur, and not easily supervised, he was right on. I'm not sure if he was forecasting the market conduct stuff that eventually developed, but he did point out that to survive they were not to be too greedy. It was very true, but not many of them took his word.

Oh, yes, and the forecast that we're really going to go to multicompany representation is clearly coming to pass now, but took some time. And the last one I took down, advice rather than selling is very much the catchphrase nowadays, but it took 20-odd years to get here.

Mr. David N. Wakely: I'd like to paraphrase a statement that Bobbie Kennedy made in a speech one time, when he said, "Others see things as they are and say why. I see things as they should be and say, why not?" I think of that often when I read Jim's statements or listen to them today. I think Jim had a clear view of the way he thought things should be and how they could solve certain existing problems. I think he tends to understate the general lethargy in any group—the reluctance to change and the existing forces that like the status quo, and will resist change. I think of Jim as looking at things as he would like them to be, and as maybe they should be, but tending to understate how often or how soon we can get there.

Mr. Easton: It's interesting that sometimes things are done before their time and nothing comes of them, but other times, if you catch things when the tide is just right, they will bear fruit. There have been some experiments with salaried field force, and there have been some experiments with low-load or no-load insurance, but so far they really haven't caught on to any great extent. I think that some day, somebody is going to try one or the other of those and it's going to catch fire suddenly, and there will be a revolution. But it hasn't happened yet.

There's one more paper that I would like to have John Yanko read for us. It's from 1987 and it's a subject dear to all our hearts—the future of the actuarial profession.

Mr. Yanko: "Now let's move closer to home. Let's talk for a moment about users of actuarial services, circa the year 2000. I've identified three users of actuarial services, beginning first with insurers. I would tell you that I expect insurers will no longer be the largest users of actuaries in the year 2000. Mainly I foresee insurance companies becoming parts of large consolidated financial and perhaps financial and industrial groups, resembling what might be described as a new zaibatsu. In these enlarged groups, I foresee that there will be no clear senior role for actuaries as such, as actuaries are now trained.

"Instead I see, as was mentioned yesterday during a panel discussion, other individuals taking on senior responsibilities in these kinds of expanded organizations. I would predict that actuaries who are involved in areas of health and casualty insurance are likely to experience considerable gain in the importance of what they do, as contrasted to those who are active in the field of life insurance.

"The second user of actuarial services is retirement plan sponsors. Here, too, I foresee considerable change. I see that the whole process of retirement plan sponsorship will become a part of a wider set of issues, the wider set of issues being labor costs and human resource issues. These are compartmentalized solutions that we have been accustomed to in the past. Solutions, for example, that separate employee benefits from direct compensation will be less appropriate in the world I foresee in the future.

"Finally, among the users of actuarial services, I would mention the consulting firms. By the year 2000, the consulting firms may, in fact, employ significantly more than 50% of the actuaries in North America. A couple of weeks ago, I attended the meeting of the Conference of Actuaries in Public Practice, and using the preregistration list that was published in the program, I was able to classify the individuals in attendance at that meeting into one of three categories. In the first category were individuals who were involved in a monoline actuarial firm, an actuary or single practitioner. This is a firm, in other words, in which there was only one area of practice—perhaps the employee benefits field, perhaps the casualty field, or whatever.

"The second group consisted of multiline actuarial firms, which practice in more than one actuarial field, and where the firms are controlled by actuaries. The third category was those who were involved in mixed professional practices that were not controlled by actuaries. I won't go into all the statistics, and there's one very striking one. Category three, the mixed professional practice, not controlled by actuaries, represent 54% of the people who are preregistered to attend the meeting. What I'm leading up to, of course, is the issue that was discussed yesterday: the future of the actuary.

"Harking back to what I said at the very outset, it's my belief that the future of the actuary is something that we can control. I think that the future of the actuary is entirely within the bounds of being dictated by the current profession, but we are going to have to face some decisions. One is whether we are going to continue to be traditional specialists in the field, which I think is going to decline in a period as short as the next 12 years, or are we going to become problem solvers who act on a larger stage. I think that not only is the choice ours to make, but the choice is very clear. I think this profession must move towards becoming problem solvers, acting on a larger stage. I have several times made this suggestion that life contingencies may no longer remain part of the core curriculum of the actuarial profession, and it's something that I sincerely believe. I think we have got to separate ourselves from the narrow specialties on which this profession has been built for so many years. The future is within our control, provided we make appropriate modifications to our educational process, our training process, and our qualification process."

Mr. Easton: One of the things we need to keep in mind about the future is that, as Jim says, it is within our control. We will be the ones who will decide the future. I'm interested to get your reaction to what Jim was predicting 12 years ago now, in 1987. To what extent do you see that his predictions for the actuarial profession have actually taken place?

I happen to know that we do not have over 50% of the actuaries working for consulting firms. Anybody want to comment on why they think that that is true? Why there hasn't been the growth in consulting actuaries that Jim was predicting? I don't know myself. I would welcome any answers.

Mr. Bakos: Just a wild guess, but is there a quota maybe?

Mr. Easton: No, there's no quota.

Mr. Bakos: But isn't it awfully close to 50%?

Mr. Easton: No, I think it's about 40%.

Mr. Bakos: That's awfully close. Whom did the other 60% work for then?

Mr. Easton: Still about half work for insurance companies and the remaining 10% or so work in academia, for government, and for other financial services organizations.

Mr. Bakos: Isn't that kind of a surprising thing? That 10% work for somebody other than an insurance company or consulting firm?

Mr. Easton: I think that might be the biggest surprise.

Mr. Stuart Klugman: The one that really struck me in my role as an academic as interesting was the comment that actuarial mathematics and life contingencies would become less important. Ironically, in our year 2000 examination system, the proportion of that exam system that's devoted to life contingencies is considerably smaller than it's ever been at any time previously. And I suspect that if you look inside the software packages that are for sale at every other booth in the exhibit hall, that very little of the work being done inside those packages would relate to the formulas of Jordan. The calculations that are in them would not be classified as traditional-life-contingencies-type calculations. I think the timing was remarkable in that prediction for the turn of the century.

Mr. Easton: When the new life contingencies book replaced Jordan, there were those of us diehards who hated to see the abandonment of the old commutation functions that we knew how to deal with so well. We all felt that we would never reach a point where we were not using commutation functions. Nowadays, though, when we do spreadsheets and so forth, we really don't use commutation functions at all. We use probabilities and interest rates. I'm sure that there will be further developments.

Mr. Neil J. Davidson: One thing in the non-actuarial part of the predictions that we heard is a constant hope or prediction that sales compensation would go down. Maybe it has at the margins somewhere, but I've seen it go up and stay up, and the products are as fully loaded as they ever were in the majority of sales. I think that prediction is a long way from coming true.

Mr. Easton: When I used to work for a life insurance company, I was always interested to observe that it costs almost as much to sell insurance in any other way—by direct marketing, for example, or by marketing in banks—as traditional agent selling does. Almost any way that you do it, it costs the same amount to market life insurance. I'm not sure that I would have agreed with Jim's hope that you could ever get the distribution costs of life insurance down. It may be too bad for the future of life insurance that it costs so much to market and distribute.

A consequence may be that buyers will focus on term insurance only, and choose other ways to do their savings accumulation. I see some of that happening already. One of the questions in the Delphi study was a prediction of the growth of life insurance in force, and the growth of the assets of life insurance companies. We found that respondents were actually predicting a larger and more rapid growth in assets of life insurance companies than they were in life insurance in force. That seemed like a strange prediction until we looked back at what happened over the past 10 years and found that that was actually the trend over the last 10 years. Assets have been growing faster than life insurance in force. We're all aware of the fact that life insurance companies are now developing savings products such as variable annuities that have caused their assets to grow more rapidly than their insurance products. Too bad for actuaries, maybe, but good for the life insurance industry.