SOCIETY OF ACTUARIES

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Letters

(Continued from page 3)

Mortality Fluctuation Reserve

Sir:

The September issue contains a "position paper" by Northwestern National which appears to confuse "margins for risks of adverse deviation" with "elimination of mortality fluctuations" under GAAP accounting. The paper suggests that unless mortality fluctuation reserves are established it will" . . . cause misunderstanding and possible apprehension on the part of users of the statements . . .", when in fact just the opposite is likely to occur.

The major reason, as I understand it, for the change to GAAP was that these same "users" were confused because in times of increased sales the statements showed increased losses. The same credibility gap will occur if in years of adverse fluctuations in mortality the company shows no adverse effect on earnings. What are the "true earnings" of life insurance companies if they do not include gains or losses due to mortality fluctuations? The "users" of our statements also use property and liability statements: in those statements adverse experience is reflected directly in the year's earnings.

Also, mortality results have generally been assumed to be independent from one year to another. If a company has experienced several "good years" (which would produce a large mortality fluctuation reserve) it has not increased its likelihood of producing several adverse years (the opposite is more likely).

Another reason for not having such a reserve is to avoid having to distinguish between "hard liabilities" and "soft liabilities" as we presently do under statutory earnings. If a mortality fluctuation reserve is used, disclosure would require a breakdown between the "formula" portion and the portion developed from prior random fluctuations, as well as distinguishing between mortality fluctuation reserves and GAAP benefit reserves.

Finally, I do not understand the concern over non-level insurance earnings. Insurance is an industry that deals with risks: as such, it is expected to have variations in earnings. If no variation in year-to-year earnings is the goal, management should set a zero retention level (which would properly eliminate the mortality fluctuation reserve under the stated formula), or else go into a business having no random fluctuations.

The solution to the interpretation of life insurance GAAP earnings should be the same as required in all industries. Annual earnings should be interpreted only after an in depth study of the industry. To assist such analysis, perhaps a footnote disclosure statement could display the expected mortality and the actual mortality (both after deduction of reinsurance recoveries) over a period of several years. In this way the "user" can see the "true earnings," as well as see the impact of random fluctuations on such earnings.

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4% MONETARY TABLES TO BE PUBLISHED

Over 30 states have enacted legislation permitting the use of an interest assumption as high as 4% in determining life insurance reserves. It is likely that the remaining states will enact similar legislation. A little over a year ago, the Society of Actuaries Committee on Preparation and Publication of Monetary Values conducted a survey of insurance companies, consulting actuaries, and regulatory authorities to determine whether this change in legal valuation standards would create a need for the publication of 1958 CSO Monetary Values volumes at 4% interest. After a review of the results of this survey and a study of the computing and printing costs of such a project, the Society's Board of Governors has authorized the Committee to solicit orders for such volumes.

The Society is now accepting advance orders at special prepublication prices in order to finance the computing and printing of these volumes. Orders received by November 15 will qualify for lower prices. After November 15 prices will be increased. Anyone interested in taking advantage of this prepublication offer should write to the Society office and ask for an order form which gives the details.

The new volumes will have the same format and quality as those previously printed by the Society for lower interest assumptions. The Committee is planning to offer volumes on an age-last-birthday as well as an age-nearest-birthday basis. The questionnaire responses did not show sufficient interest to justify printing 4% volumes based on the 1959 Accidental Death Benefit Table or on the 1952 Disability Study.

The Life Insurers Conference is preparing a set of 4% volumes based on the 1961 CSI Table. The Society Committee, chaired by Walter L. Grace, and the LIC Committee, chaired by John M. Bragg, have been working together to avoid duplication of effort and to achieve all possible economies in the computing and printing work. The special prepublication prices will also apply to these tables. Anyone interested in the 1961 CSI volumes should write to the Life Insurers Conference, P. O. Box 6856, 1004 North Thompson Street, Richmond, Virginia 23230.

The success of this venture will depend on receiving a sufficient volume of prepaid orders to finance the computing and printing costs. It is most important, therefore, that all potential users of these tables send their orders (and checks) to the respective offices as soon as possible. □

Closing the GAAPs

(Continued from page 1)

III. *Other*

A. Deferred acquisition cost asset as % of premium income and of statutory total assets

B. Ratio of GAAP to statutory stockholder equity

The wide range of responses to many questions indicates that GAAP results of different companies may be difficult to compare. For example, some companies amortize Field management compensation which is related to production, branch office operating expenses, maintenance costs and training allowances to new salesmen while others do not. The starting point for deferring acquisi-

(Continued on page 8)