

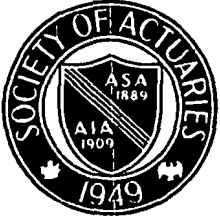


SOCIETY OF ACTUARIES

Article from:

The Actuary

September 1974 – Volume 8, No. 7



The Actuary

The Newsletter of the Society of Actuaries

VOLUME 8, No. 7

SEPTEMBER, 1974

APOSTLES vs. PROPHETS

by David S. Williams

No, this is not a report on last weekend's game in the Ecclesiastical Football League. Rather, it has to do with your appraisal of the "world problematique", the global complex of problems popularized through the "Limits to Growth" controversy. Are you basically a "prophet of doom", or do you count yourself as an "apostle of hope"? Whether you occupy one of the extreme positions or a point somewhere in between, you are assured of the support of numerous experts, e.g.,

"The battle to feed humanity is over. Unlike battles of military forces, it is possible to know the results of the population-food conflict while the armies are still in the field. Sometime between 1970 and 1985, the world will undergo vast famines—hundreds of millions of people are going to starve to death. That is, they will starve to death unless plague, thermo-nuclear war, or some other agent kills them first."

"Even if there were no new discoveries in food-growing technology from now on, and we continued to cultivate only the very small proportion of the earth's surface now used as farmland, a raising of all other countries' efficiency of cultivation to that of the Netherlands would already suffice to feed 60 billion people."

"We can and must commit ourselves to a lower rate of growth in the use of natural resources. In one decade, 1959 to 1968, the United States alone used more resources than all the world's people in all of previous history."

"It is not reasonable to assume that general resource exhaustion will reduce industrial output ever, let alone within a few hundred years."

(Continued on page 6)

VARIABLE LIFE INSURANCE

by Robert O. Dausman

At the Spring Meeting of the Southeastern Actuaries Club held on June 13 and 14, Mr. Walter S. Rugland discussed various aspects of Variable Life Insurance including the many problems still awaiting solution.

He began his address by stating that the viability of the VLI product depends upon favorable treatment of the product by various regulatory bodies. It appears that development work by the interested companies has ceased until the regulatory picture is cleared.

He noted some possible threats to VLI. Some of them were: (1) a commission rate at mutual fund rates, (2) investment gains taxed directly to the policyholder, (3) proceeds to beneficiaries could be taxed, and (4) insurance company taxes on VLI product line could be restrictively high.

His personal feelings are that VLI, as defined today, is a weak answer to inflationary problems inherent in permanent life insurance. Since the design of this product in 1968-1969, there has arisen a new dimension to inflation and to the equity market place.

Mr. Rugland then discussed the eight pertinent development issues other than the technical aspects. They are: alternative VLI approaches, agency officer commitment, proposed amendment to Rule 3c-4 — Marketing Implications, external influences, NAIC model, VLI investment vehicles, and finally, basic questions.

1. *Alternative VLI Approaches.* Mr. Rugland felt that product designs should be the creation of a product to fill a market need. Each company needs to evaluate its market and why people buy from it. His conclusion was that a company should not

(Continued on page 6)

SOLVENCY, THE INTERNATIONAL VIEW

Financial Guarantees Required from Life Assurance Concerns, Organization for Economic Cooperation and Development, Paris, 1971.

by James C. Hickman

Life insurance is a serious business. Through the political process, the public long ago made it clear that it expects a high degree of stability and continuity in the operation of life insurance companies. One of the principal obligations of the actuarial profession to the public it serves, is to design and manage life insurance systems that have a high probability of remaining solvent. Consequently, any discussion of solvency standards for life insurance companies is, in fact, a discussion of the foundations of actuarial science.

To honor the chairman of the committee that prepared the report, and in response to the imposing length of its title, this document is usually referred to as the Buol report. During the time that the report was being prepared, Mr. Buol was a member of the Swiss Insurance Supervisory Service.

The OECD, the organization that commissioned the Buol report, may not be well known to actuaries. It was created by an international convention signed in Paris in 1960. Twenty four countries, including the United States and Canada, are members. Yugoslavia has a special status, different from full membership. Member countries account for about 70% of world trade and 95% of all development aid. OECD sponsors a broad program of research and technical services with the objective of achieving the goals stated in its name.

The Buol report was written by representatives from ten European countries. Consequently, North American actuaries may find some of the actuarial terms

(Continued on page 7)

Variable Life Insurance

(Continued from page 1)

- plunge right into VLI without considering the other approaches available to protect against inflation or to provide growth through equity investments.
2. *Agency Officer Commitment.* The Marketing Department's reaction, feelings, and commitment toward the marketing of VLI is essential to its success. There is no benefit for a company to build a beautiful "Edsel" insurance policy.
 3. *Proposed Amendment to Rule 3c-4—Marketing Implications.* The current SEC proposal is to give the SEC direct control of how to regulate VLI in order to provide the investor protection "substantially equivalent" to the 1940 Act. Some of the implications from this are that this Amendment may result in restricting the sales load, necessitating a free-look provision, offering high early cash values, and disclosure of fees and asset charges. The SEC wants protection against "excessive management, administrative and sales charges."
 4. *Your Representatives.* The life insurance industry is very active in the VLI discussion scene. Much effort is being extended by the industry in order to obtain a favorable and equitable treatment from the various regulatory bodies. As of the present time, 51 companies have representatives on either the Variable Contracts Committee, Sub-Committee for Federal Regulation, and the Sub-Committee for State Regulation.
 5. *External Influences.* A complex sequence of events must occur before VLI can become a reality. There are a number of interested parties, all of whom have their fingers in the pie and all having different views, i.e. the insurance industry, NAIC, SEC, IRS, and the mutual fund industry. The interplay of thoughts and actions of these various groups may eventually be resolved only through legislation (both state and federal) and litigation.
 6. *NAIC Model VLI Regulation.* Mr. Rugland listed 23 unique features of the Model Regulation. Most of these are additional requirements other than those currently existing for fix-

ed benefit policies. This Model Regulation affects the marketing of the product, the product design, and the administration of the product.

7. *VLI Investment Vehicles.* It appears that VLI separate accounts will be exempt from the 1940 Act registration, although the states may adopt new regulations affecting them. There are two basic VLI separate account approaches which may be followed by insurance companies:

- (a) Fully managed separate account — a separate account which directly owns a diversified portfolio of common stocks.
- (b) Flow-through separate account — a separate account which directly owns shares of only one stock, such as, a mutual fund.

Mr. Rugland listed the advantages of each of these separate account approaches. The performance of the separate account and its consequent effect and the consequent effect of VLI may very well affect other very important areas of the company, such as agency morale, competitiveness of company products, etc.

8. *Basic Questions.* Mr. Rugland pointed out the many questions which need to be individually answered by each company before the development of a VLI product. These questions revolve around the following topics: (a) corporate structure, (b) issues—pricing and product design, (c) investments, (d) sales, (e) administration, (f) broker/dealer, (g) underwriting and policy issue, (h) legal, (i) systems, (j) accounting, (k) federal and state taxation. □

Apostles vs. Prophets

(Continued from page 1)

"There is no longer any excuse to pretend ignorance of the menace (of global collapse of human affairs) ahead of us, of the profound wrongness of the present direction in which humanity persists in moving, by inertia or by narrow motivation."

"Even if the balance of the probabilities were on (the side of the *Limits to Growth* report) with respect to the imminence of disaster there would still be an overwhelming argument for further delay . . . we can afford to waste another decade even if we

Deaths

Harold Garabedian
Ralph Keffer
Robert C. Morrow
G. Robert Mullans
Gary Olson
Samuel Winn

only have another century . . . simply because the consequences of a mistake would be so grave if 'Limits' were wrong."

The extraordinary divergent opinions exemplified above suggest that some of the alleged experts in this field are perverting Ruskin's dictum by manipulating facts so as to create misleading impressions. The debate has therefore been counter-productive in that it has furnished a superficial reason for government inactivity and created a range of attitudes among the populace ranging from frustration to boredom. In view of this, can a study of the "world problematique" by the actuarial profession serve a useful purpose?

To find the answer to this question, we need not look beyond our professional responsibility, i.e., to assist our employers and clients in making w. decisions in the face of long-term future uncertainty. Does this not require us to be well-informed in this general area, and to have some appreciation of the socio-economic restructuring of our society that may prove necessary?

Consider also the tools of our trade—projections, probabilities, and correlations (not to mention the more advanced Operations Research techniques utilized by our technically more proficient colleagues). Do these not specially qualify actuaries to develop a reasoned appraisal of and response to the "problematique"?

Because of your unavoidable responsibilities as a forecaster, these questions deserve your careful consideration. Whether you speak as an apostle of hope or a prophet of doom, your comments and opinions will be welcomed.

The topic will be further explored in a panel session at the annual Society meeting in New Orleans. Some excellent background reading is available, e.g., *Toward a Steady-State Economy*, a book of essays edited by Herman E. Daly, published in 1973 by W. H. Freeman and Company, and available at most University bookstores. □