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REGULATORY PROBLEMS OF LIFE INSURANCE COMPANIES vs. OTHER FINANCIAL INSTITUTIONS

by Richard V. Minck

The investment returns earned by life insurance companies over the past decade have permitted the sale of contracts guaranteeing relatively high rates of interest. The contracts have given rise to problems in the areas of the federal securities laws, of federal income taxes, and of state valuation requirements.

Traditionally, insurance contracts funding qualified pension and profit-sharing plans have not been regarded as securities to be regulated under the 1933 and 1934 acts. During the 1960's, insurance companies began to issue annuity contracts that provided for the allocation of contributions to separate accounts, thus enabling those contributions to be invested in common stocks. The SEC staff took the position that these separate account contracts came within the federal securities acts' definition of "securities." The issue was brought to the Congress which amended the securities laws so that participating interests in life insurance company separate accounts established in connection with qualified retirement plans were declared to be "exempted" securities. Recently, insurance companies have offered contracts to fund pension plans which *do not* utilize separate accounts and which provide for only minimum, if any, mortality guarantees. Questions have been raised by the SEC staff whether these contracts are entitled to exemption. However, on March 18, the SEC issued a "no-action" letter which set forth conditions which, if met, would lead the SEC not to recommend enforcement action if guaranteed interest contracts are sold by life insurance companies to corporate pension plans without registration of such contracts as securities. (*Continued on page 7*)

David Garrick Halmstad Memorial Fund

Contributions to the fund established to award annual prizes in memory of Dave Halmstad now total $4,000. The goal of $5,000 appears to be in sight. Tax-deductible contributions in the form of checks payable to the Society of Actuaries may be sent to the Chicago office.

SEX AND THE SINGLE TABLE REVISITED

by Barbara J. Lautzenheiser

Editor's Note: Barbara Lautzenheiser's excellent article "Sex and the Single Table" (see *The Actuary*, February 1977) indirectly gave rise to the following comment:

"The issue never was or is now whether women live longer than men. The issue is whether in a given group formed by common employment, benefits to one class within that group should differ because of race, sex, smoking, blood pressure — or eye color."

Miss Lautzenheiser decided to reply to this comment and her reply is well worth reprinting:

"Although I agree with you that the issue never should have been nor should be now whether women live longer than men, I'm afraid in some people's minds that *is* the issue. I constantly receive questions and doubts about the credibility of the current statistics. People always question things they haven't developed themselves, and particularly things they don't understand or things that don't give the results that they want. And people questioning longevity data on men and (*Continued on page 8*)

JIMMY CARTER AND SOCIAL SECURITY

by Ronald G. Harris

On the same day that the "1977 Trustees Reports" were issued, the Carter Administration unveiled its financing program for the Social Security trust funds. The Administration presented a series of proposed changes designed to alleviate at least partially the financial problems of the programs. The proposal in total is rather complex and defies a simple explanation but there are basically eight major provisions:

—The first is that it would institute a special "counter-cyclical" system of financing from general revenues which is intended to replace social security taxes that are lost when the unemployment rate exceeds 6%. There is a retroactive feature on this provision going back to 1975.

—A second major characteristic of the proposal is that it would remove the ceiling on the amount of an individual's wage or salary on which the employer would pay social security taxes. This is proposed to be accomplished in three annual steps beginning in 1979 and ending in 1981.

—The third point, related to the second, would impose an increase in the maximum amount of wages or salary on which an employee would pay social security taxes and, of course, on which his benefits normally would be based. The proposed increases would be $600 in each of the four years 1979, 1981, 1983, and 1985. These would be increases that are in addition to the automatic increases that would result from current provisions of the law.

—The fourth item is a shift of some taxes from the HI program to the (*Continued on page 7*)

PENSIONS AND THE U.S. SUPREME COURT

by Susan J. Velleman

In their recent decision in the case of *Alabama Power Co. vs. Davis,* the U.S. Supreme Court touched on a fundamental issue of employee benefits philosophy. The Court, in holding that defined benefit pension plans must grant benefit accrual credit for periods of military service, concluded that "pension payments are predominantly rewards for continuous employment with the same employer" as contrasted to "deferred compensation for a year of actual service."

This characterization of pensions as a reward for continuous employment seems contrary to current attitudes, as exemplified by the requirements in the ERISA to fund and vest accrued pensions after fairly short periods of service and by the acceptance of negotiated pension costs as part of a cents-per-hour wage settlement. □

Jimmy Carter

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or methods of financing the programs in two key areas. One is the interjection of general revenue funds rather than relying solely on payroll taxes. The other is the treatment of the wage base—removing any limitation from the wage base on which the employer would make contributions. This latter item itself involves a couple of major departures. First, it's really the first time that the wage base has been used strictly as a financing tool. Normally, an ad hoc change in the wage base would affect both benefit computations and revenue to the program. Secondly, and I'm sure most of you are aware of this, professional firms such as actuarial consultants who have relatively high average wages would be affected rather strongly without any corresponding increase in the benefits that their employees would receive.

Editor's Note: We are indebted to the author for permission to excerpt these comments from his presentation at the "Open Forum One" session at Quebec City. □

Sex and the Single Table

(Continued from page 1)

woman are no exception. Since they feel the industry and our profession both have a vested interest in the results, there is the natural doubt in their minds as to whether or not that vested interest might have gotten in the way of the facts when we developed them. Fortunately, much of that data is census data and Social Security data, not developed by the industry, and therefore it's more credible.

Some of those who do accept the current data as credible, however, question whether or not the data will change with time. They're referring to the data equalizing, of course, rather than further separating as it has in the past. The beauty of the separate tables is that if they do change (hopefully the same way they have in the past, i.e. longer life for women, since in that respect I do have a vested interest) we can then reflect that in the rates in the future.

I sincerely wish that the issue you stated, i.e. "whether in a given group, formed by common employment, benefits to one class within that group should differ because of race, sex . . ." were the only real issue. If the issues were restricted only to this, I would have concern, but not nearly the concern I have for what I perceive the real issues to be. Unfortunately, the issues involve not only group insurance paid for by one employer, but also individual purchases for small groups paid for by many different buyers. In these latter cases equity and fair pricing, not just benefit structure, is absolutely necessary between different buyers.

It's also not just sex, but physical handicap and age as classifications, that are being challenged. It's the ability to assess the risk and charge a fair price for it, with no unfair overcharge for someone else's extra cost risk, that's being jeopardized. The proper assessment of the risk is a responsibility of the provider of the benefit, as well as a necessity, in a voluntary coverage system. Mandation of how to classify or rate policies, through unisex, or unihealth or uni-age tables, or just mandation of what benefits should be provided, reduces the options the public has because some insurers merely cease selling the coverage (as many have done in states where health benefits were mandated) and causes unfair charges to be made on the majority of the public — since low risks are forced to subsidize high risks. Ultimately this could cause elimination of the private insurance market with the necessity of a take-over by the government — a trend which is just the opposite of what the public and the President, appear to want.

It also involves not just annuities, but life insurance, health insurance and casualty insurance, where anti-selection is more prevalent. When an unlimited amount of insurance on a high risk coverage can be made at the same price as a low risk coverage, low risk coverage purchases will cease to be made. This will further spiral the costs and essentially make insurance unavailable at a price that's reasonable to the large majority of the population. This would just not be in the best interests of the public.

There's also the basic question of how to determine when benefits are equal. Paying one person $100 a month for 10 years provides the same monthly benefit as providing another person $100 a month for 20 years, but they don't have the same value. Providing one person a Cadillac to drive to work and another a VW gives them both equal transportation in terms of how long it will take the car to get them there too, but they don't have the same value. I've always measured equality and equity by cost, by value in dollars, because I don't have any other way to measure. And I use the same basis for annuities, i.e. the value of the benefits to be paid. And it's this present value of the payments to be made, not the payments individually, that should be equal.

I feel the profession's responsibility is to determine the facts, substitute them for appearances, and make sure those facts reach the persons responsible for making the decisions. If equality, not in terms of costs, and subsidization of one group by another is for the social good (and we have considered it so in cases such as cost of education for all children), that's for the public, through their representatives, to decide. But we, as professionals, as actuaries, have a responsibility to point out those consequences, costs and inequities (subsidization) that are caused by doing so, so that intelligent, informed decisions can be made." □