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Session 26IF
Small Company Issues

Moderator: Lori A. Truelove

Panelists: Stephen L. Marco
John R. Miller

Summary: With emerging regulatory and actuarial requirements, smaller companies are forced to find solutions with limited resources compared to those of larger companies. Dealing with the evolving regulatory environment often involves innovative and creative techniques. This session provides an opportunity to discuss issues of particular interest to participants along with new solutions and techniques. Several topics open for discussion are:

- *Section 7—changing cash-flow testing requirements*
- *C-3 risk-based capital requirements and methodologies*
- *Setting and resetting X factors for Regulation XXX*
- *Developing internal management systems*
- *Regulatory update*
- *Using outside consultants*

MS. LORI A. TRUELOVE: Our panelists are prepared to answer questions on various topics. We have Steve Marco, who is senior vice president and chief actuary of Citizen Security Life Insurance Company. John Miller is the "Miller" of Miller and Newberg, a consulting actuary firm.

I'll get started with a topic covered at another session. I thought the other session covered this topic fairly well. It dealt with the Section 7 changes to the cash-flow testing requirements. I'll ask one of our panelists to briefly describe the proposed changes and give an indication of the timing and impact to small companies.

MR. JOHN R. MILLER: The proposed changes give the ability to file an opinion with your domiciled state. The regulators have proposed elimination of the small company Section 7 exemption. How many people actually file a Section 7 Opinion? Quite a few people raised their hands.

As a consulting actuary, I have five client companies that are Section 8 and seven that are Section 7, so I kind of have a little of both. My smaller company clients with Section 7 opinions are not excited about having us do more detail. Maybe it's not cash-flow testing. Some of those other things are more involved than what we've done in the past. I believe the biggest issue in the change is it seems like we're making a trade-off for the larger companies to give them the ease of filing with their own states as opposed to filing for all states.

MS. TRUELOVE: Do any of you have a question with regard to any of the changes that might be coming your way?

FROM THE FLOOR: What's the timing on Section 7? Some of us have to get our small companies up to speed?

MR. MILLER: I don't think it will be done by this year-end, but the Life and Health Task Force is looking at it. Is there a September meeting coming up?

MR. STEPHEN L. MARCO: There's a September meeting, but I don't think it's going to be determined there. We think it's probably going to be settled sometime in December 2000. The Small Company Committee has tried to become more involved with it. What we've decided to do is try to send out some more material to small company members, so they have a better idea of what's going on. We think the final decision will be made in December, so knowing about it now gives enough time to make comments. If you have a problem with it, hopefully you'll have a chance to change it. My understanding is the regulators are very much in favor of it. So if you have strong feelings about it, you probably want to make them known as soon as possible.

MS. TRUELOVE: I have another question on that topic. Are there any perceived benefits to small companies if they lose the Section 7? Are they going to get any bang for their buck that they're going to be spending?

MR. MARCO: I'm from a small company and the only actuary there. We've done Section 8 testing since I've been there, and I find that it dovetails very nicely into a lot of other areas (for example corporate projections). We depend upon that heavily for financial analysis. Basically, we have a large model that is more detailed than you would need for cash-flow testing. In addition to corporate projections, we use it for profit testing and for loss recognition analysis for GAAP. There are a lot of benefits you can get from it. The question is, do you want to spend the money upfront to put it in place?

FROM THE FLOOR: Is this going to be as of December 31, or can we have it by September 30 and then do the work? As we turn in our final statement, should we submit our cash-flow testing certification, done as of September 30?

MR. MARCO: For cash-flow testing purposes, I've always done it as of September 30. I personally don't have the time to do it at year-end. I'm not aware that there's any talk about changing that. As a practical matter, it might not make sense. I do know that some regulators are not happy with September 30 because it's tougher to validate with actual values and because you have to do a reconciliation to the annual statement or to year-end numbers. Again, I've looked through the proposed changes, and I don't recall seeing anything where they would force you to use a year-end date.

FROM THE FLOOR: I know we use the term cash-flow testing with Section 8, but is it still going to be asset adequacy, which means that there are other methodologies, in addition to cash-flow testing, like gross premium valuations (GPVs).

MR. MILLER: That's correct. Your assumption is correct.

MS. TRUELOVE: Are there any other concerns on the Section 7 removal?

FROM THE FLOOR: To be exempt, you have to pass these ratio tests, and the ratio tests basically describe how risky your assets and your liabilities are. From where I'm coming from, if your assets and liabilities are not deemed risky because of these ratio tests, why should a company have to go through the additional expense for cash-flow testing? I don't see where the regulators are winning. I've seen large companies that, in theory, were doing cash-flow testing, and they still have problems. If the smaller companies that can't afford to do cash-flow testing did have problems, is there a macroeconomic effect? Where are the regulators winning?

MR. MILLER: When the first actuarial opinion and memorandum regulation came out, I don't think the regulators were excited about the small company exceptions. They gave it to us when we started, but eventually they're going to take it away. That seems to be my take on it. It's a trust thing, and we continue to lose that trust.

MR. MARCO: From a regulatory point of view, how small is small? I'm at a company with about $140 million of assets. Are we too small? Many folks our size would say there is no need to do cash-flow testing. In our case, I think we do. How does the regulator decide whether $2 million, $50 million, $100 million, or $200 million is large enough? I guess the simpler answer is let's just do it across the board. The extremes will always be obvious. In the case of a $2 million company, that's a fraternal, there probably is no need to do it whatsoever. I would think that the regulators would agree. Are they going to make a change to a regulation to accommodate 1% of the companies out there? Probably not.

MS. TRUELOVE: I think we'll go ahead and move onto a new topic. We can always come back. There was another session on the changes to the C-3 risk for risk-based capital, so would one of you briefly, describe the proposed changes to the C-3?

MR. MARCO: I'll try. My understanding is that the single pay life and annuity component of the risk-based capital calculation is going to be changing. Depending upon whether you pass an exemption test or not, you might be required to do a series of, essentially, cash-flow tests to determine what the level of that C-3 element is.

MS. TRUELOVE: What is the proposed effective date, and how soon should we start testing for an exemption?

MR. MILLER: I think it's December 31, 2000.

MR. MARCO: Yes.

FROM THE FLOOR: What is the first year they're going to get it?

MR. MARCO: 2000.

MR. MILLER: The first step is to see if you're exempted from it. I found out at another session that most companies will be exempted from it.

MR. MARCO: If you are not exempt, it would make sense to look at your year-end 1999 material and do some sample runs to see what effect, if any, it would have on you.

MR. MILLER: That seemed to be the expectation of the presenters, anyway. As a matter of fact, Section 7 small companies are very likely to be exempt. You would need to be concerned about it only if you're doing Section 8 opinions, cash-flow testing, or if you have a lot of annuities, which seem to be what's triggering this.

MR. MARCO: The nasty thing about it is when I said use cash-flow testing, I meant that you have to use a specific set of scenarios that are generated by a scenario generator that you can download if you go to the NAIC Website.

MR. MILLER: We looked at that a few months ago, and they seemed to be extreme scenarios, even on the outside bounds of the New York Seven. If you're struggling in your cash-flow testing about New York Seven rising scenarios passing, then, as an annuity company, you're going to have some very ugly scenarios when you're looking at some of these risk-based capital (RBC) scenarios.

FROM THE FLOOR: I'm just verifying that the companies are expected to utilize the new C-3 with their December 31, 2000 filing. The answer was affirmative.

MR. MARCO: We believe so.

MR. MILLER: Yes, that is our understanding.

FROM THE FLOOR: We are currently doing cash-flow testing. We have a lot of annuities, but we do it the old fashioned way with the C-3. Are we going to have to change the way we do the analysis with the cash flow with this new testing?

MR. MARCO: That's assuming you're not exempt.

MR. MILLER: You're looking at interim results in your cash-flow testing, and you might be looking at the end of 20 or 30 years and then decide whether they pass or fail.

FROM THE FLOOR: We're basing that on the end of 20 years.

MR. MILLER: This is going to be a little different because you're going to be looking at interim losses and discounting those back a present value and looking for the worst case number.

I haven't gone through the instructions, so I can't speak much more about it, but it sounds like you picked the worst case, and it became your risk-based capital for that component.

FROM THE FLOOR: Okay.

MR. MARCO: They have some fairly complicated rules as to which ones you look at, and you take certain averages of discounted values. If you go through the piece from the NAIC, I think you'll be surprised at how complicated we've made things.

FROM THE FLOOR: Thanks. So you recommend that we first check it if we are exempt?

MR. MARCO: I think your first step is to see if you're exempt. If you're exempt, then it's a problem you don't have to worry about.

FROM THE FLOOR: Okay. But we will continue to do cash-flow testing anyway.

MR. MILLER: Right.

MR. MARCO: It's not going to eliminate the need to do cash-flow testing.

MR. MILLER: They might be interesting scenarios for you to look at, even in your cash-flow testing (as a sensitivity) because you might not want to tell anybody the results.

FROM THE FLOOR: There are the model differences of the asset valuation reserve (AVR). You have to read the language about risk and the AVR and assets that might be added to the model regulation. I think it was the interest maintenance reserve (IMR), not the AVR.

MR. MILLER: That's correct.

FROM THE FLOOR: I have a question about the exemption. What are some of the criteria for becoming exempt or the test for exemption?

MR. MILLER: There was a session but I'm having trouble remembering what the criteria were.

MS. TRUELOVE: The first one is, your C-3 is over 40%.

MR. MARCO: Do you mean the sum total of all your C risks?

MS. TRUELOVE: Yes, it is the sum total of C risks. Then you will have to go through the new testing.

MR. MILLER: There was another test.

MS. TRUELOVE: There's another test, too. If you pass the first one, you go to the second one and see if you pass it, and then you're exempt. You have to pass both.

Here's the other one. I'll read it. It's very complicated. If the factor-based C-3A for your annuities and single premium life were 7.5 times as large, would the company's risk-based capital ratio be less than 100%?

MR. MILLER: The other thing I noticed in the proposal is there's a maximum and a minimum. It might be interesting just to ask what if the worst case was two times what the former component was? Maybe they don't want to go through the testing. They just use that number.

MR. MARCO: Right. That will be less than one-half and never more than two times the existing component.

FROM THE FLOOR: Forty percent applies only to the annuities and single premium life C-3 risk.

MR. MARCO: I think you're right.

MR. MILLER: That's right. What was the reference for that portion of the component?

MS. TRUELOVE: He said that the 40% number that we threw out earlier only applies to your annuities and single premium life. Any more questions or comments on the changes to C-3?

MR. MILLER: Even if you get the exemption, there's still an additional element of C-3 having to do with callable features on your assets, so that's something that, essentially, everybody will have to do.

MS. TRUELOVE: Anybody else? Okay. We'll move onto another topic that was addressed in another session. I think the sessions have covered these topics well. Let's discuss setting and resetting of X factors. We scurried to set our X factors, and now we have to scurry to reset them or check that they're adequate. What tools have people used to set X factors, and how do they demonstrate the reasonableness of their select X factors?

MR. MILLER: I know we're in the process of looking at that for about three clients that have situations for which we used X factors. We're using a Microsoft Access Routine doing Monte Carlo simulation. We are taking what we were doing in mortality studies and enhancing it, and then adding that to it. We're also using hypothesis testing. I'm not doing the crunching, but I've been talking to the guy that has, and I keep asking him what we are supposed to do with certain things. I think I'm going to have to figure it out by the end of the year. That's something we're doing.

Earlier this spring, I was at a Fraternal Actuary Session. There was a gentleman there that had done quite a bit of work in that area. Actually, that's where I got the idea of using Microsoft Access. He was doing his work there. I believe he was with Mennonite Mutual. So that's the approach we've taken. We are looking at whether we can come back after the fact and say, "Yes, our X factor was reasonable looking at our actual experience."

MS. TRUELOVE: How intricate have companies been in setting X factors? Have you seen mostly simplistic structures on X factors or have you seen really elaborate schemes?

MR. MILLER: I guess the things that we've seen have been fairly simple. We worked on one where we were going to be a little elaborate and decided that it was going to be a lot more difficult to justify at the end of the day. So we've kind of gone back to a simpler approach. What have other people done?

FROM THE FLOOR: I question how many people feel they have credible mortality experience from their own company alone. I consider myself a large/small company. We run at about 220 to 230 deaths a year. By accumulating a four-year rolling study, I can get up to around 900 deaths, which I feel is the minimum for justifying anything to the examiners.

We do not have a XXX product right now. We have nonguaranteed products. We are considering one. As far as the X factors go, I have substituted the 1980 CSO with the new select factors into my mortality study for the 1975–80 Table. In our case, our aggregate experience was something in the neighborhood of 60%; when we substituted the 1980 CSO, we were under 50%. I would be comfortable at this point going out with an overall X factor in the 50–60% range.

MR. MILLER: That fits with the factors that we've seen at 60%. It sounds consistent with other sources, and reinsurers will give you some input on that, also.

FROM THE FLOOR: We're pretty new into the resetting of the X factors. Can you briefly touch on what the ramifications would be for being too refined or too simplistic in your approach?

MR. MILLER: I guess being too refined would make it more difficult to justify. "Too simplistic" might mean your product is not as competitive as you or the marketing people might want it to be. It seems like there is probably a trade-off.

FROM THE FLOOR: If you stray from your X factor, is it chance fluctuation of one year or is it something that you have to correct immediately?

MR. MILLER: I think if you're convinced that you've strayed, I think you have to correct it right away. I think that some of the hypothesis testing doesn't always come back and say you have the right factor. It says that you're not rejecting the factor at this point. But as you're accumulating your data, you might get to that point, eventually, if it doesn't revert back, or if your results don't get closer to what you expected.

FROM THE FLOOR: If you're a half standard deviation away from your mean, does this mean you have to change it? There has to be some wiggle room in there.

MR. MARCO: That is particularly true with the credibility of the level of experience that we'd be using as a smaller company.

MR. MILLER: That's right. For a smaller company, you have more wiggle room than you do as a larger company. They're going to have a much narrower band to be able to either accept or reject the particular X factor that they've calculated.

MS. TRUELOVE: I had a question sent to me. I need to see a show of hands of how many companies have already set-up models for their liabilities and assets. Are they fully modeled liabilities and assets? Are they doing cash-flow testing?

MR. MILLER: Sure. I'd say half of our Section 7 opinion companies have liability models, but we don't do asset modeling for them. We have the tools, and it's fairly easy to do that. We get those "what if" questions, so we've tried to help our clients plan how much business they can write before they need more reinsurance, and we assist with questions that they have.

MS. TRUELOVE: Are there any more questions on X factors? You already have strategically placed your X factors correctly, so you don't have to mess with them for five years.

FROM THE FLOOR: With regard to X factors, one of the slides used at another session noted for reinsurance issues, coinsurance versus yearly renewable term (YRT). Of course, nothing was said about whether you use yours or the reinsurers. I didn't get a chance to ask a question on it.

Does anybody have any comments? What is the difference between YRT and coinsurance with regard to an XXX plan?

MS. TRUELOVE: I've worked in the reinsurance division for a good number of years, so I'll take that one. Basically, your term plans are heavily affected by your X factors, and they're usually under a coinsurance treaty. The reinsurers' X factors do not have to match the ceding company's X factors. Small companies often rely on a reinsurer that will spoon feed them X factors. The factors are based on the reinsurer's mortality studies, and what it thinks is appropriate for your company's underwriting standards, and so forth. YRT treaties have no impact on XXX because they use the 1/2cx reserve, so there is no impact on the YRT treaties.

FROM THE FLOOR: What can you take in credit?

MS. TRUELOVE: The ceding company can't take any more credit than what the reinsurer posts. If the reinsurer is holding reserves on a different basis, you have to make sure that you're not taking more credit than what the reinsurer is actually posting on its books. If you were audited and the discrepancy was found, you'd get slapped.

FROM THE FLOOR: So that's an important theory showing that reserving, with respect to X factors, now forces credit balance.

MS. TRUELOVE: Exactly. So it's very important that you look at your reinsurance treaties on a coinsurance basis, so you can see what X factors are being used. They're often being put into the treaties. What kind of guidelines has the reinsurer outlined for resetting the X factor?

MR. MILLER: Sometimes we have products where, even with X factors, we'll have deficiency reserves. So you'll want the reinsurer to be holding their share of that, so that they can take credit for it. Whereas, on the YRT side, you're going to hold all your deficiency reserves, and you're not going to get any relief from the reinsurer.

FROM THE FLOOR: You mentioned that you could get spoon fed X factors from a reinsurer, especially if it's a class that you've never had (like the super preferred), and you're going to reinsure it. How does the appointed actuary get comfortable with that number for their opinion?

MS. TRUELOVE: It's called the letter of reliance. Get one from your reinsurer. I gave out many.

MR. MILLER: That's what happened with our clients when they added the preferred class instead of having just one nonsmoking class. We've gone to two. You might look at it and think it looks reasonable. The reinsurer claims to have some experience. The reinsurer will give you a letter that you're relying on initially for setting your X factors, and over time, you're going to have to convince yourself that they are appropriate.

MS. TRUELOVE: Let's discuss internal management systems. What kind of analytics are being used on internal management systems and for what purposes?

MR. MARCO: When I saw the name of that topic, I felt it could mean different things to different people. What it means to me, and I would think for most of us who look at reserves doing what we might call reserve analytics, is simply trending factors and tracking them over time. You can either do it on a per policy basis, on a per 1,000 basis, or per unit basis to see if something is wrong with either the factor file or the in-force file.

We've gone so far with certain blocks as to actually graph the data. The idea is that we can have a less senior person do this. If something looks out of whack, it is very apparent. Of course, you can extend that. In my mind, you extend it to things like budgeting to see if your expenses or corporate projections are where they should be. I think that all of this is taken together as an internal management system.

At the beginning of every year, we do a corporate projection, track it during the year, and make refinements as we see fit. Every time there's a variation, it becomes necessary to explain why.

Because we're a small company, at least the mortality part of that is usually easy and is attributed to normal variation. That sometimes, but not always, satisfies our CEO.

MS. TRUELOVE: Are these analytics tied to our cash-flow testing, or are they completely separate?

MR. MARCO: The corporate projection part is essentially an offshoot of the cash-flow testing. We put together a fairly complex cash-flow testing model because we use it for corporate projections. We found it very useful. We don't do projections like this with the assets. It's basically a liability model; however, it is in enough detail that you can run it on a quarterly basis. Most of you who do Section 8 opinions realize that your model probably isn't suitable for quarterly models. Basically, you're lucky if it gives you good information annually. We feel we have computer toys at the office where we can put together something sophisticated without worrying about processing time.

FROM THE FLOOR: Steve, I'm wondering if one of the offshoots of doing these kind of models is to value your company from year to year, using economic value added. I'm wondering how much it's worth. I guess that question is for anybody else in the room. One of the uses of cash-flow testing is for appraisal purposes. I'm just wondering how proactive small companies are when putting together a value of their company.

MR. MARCO: One of the things I normally do in May, after the cash-flow testing is put to rest, is assign a value to the company based upon the results of the cash-flow testing. I've always believed that a typical cash-flow testing model is probably not quite detailed enough for a good appraisal. Some folks would disagree with that, but I think you need something a little bit more than the typical cash-flow model. I think you're right in that it is a very useful offshoot of the process.

FROM THE FLOOR: Can you describe the size of the cash-flow testing models?

MR. MARCO: I guess it depends upon how many lines of business you have. In our case, we probably have a dozen in the cash-flow model. If a company our size had a dozen small blocks of business, I can't see them putting the effort into the model that we do for cash-flow testing. That is especially true if it's a type of business where you're pretty comfortable that it's going to pass all the scenarios and you're not going to have much of a problem with it.

FROM THE FLOOR: Could you describe the content of your model cells for a typical line of business?

MR. MARCO: I guess I can start with a traditional block of home service business, roughly 60,000 or 70,000 policies. The model contains about 3,000 cells, which is a lot more than what you need for cash-flow testing.

On the annuity side, we tend to have fewer cells. We have approximately 1,000 policies, and we might have something short of 100 cells. As you can see, it is a fairly detailed model. The good part is once you set it up, it's not too difficult to continue it. You just dread adding new blocks to the company, because you know you'll have to go through the process over again.

FROM THE FLOOR: This is backing up a little bit to the reporting for a small company. Oftentimes, if you do annual reporting, you're not really finding out enough. If you do quarterly reporting, you find out more. At what point do you draw the line and decide whether it's worth doing that monthly reporting of everything? Let's discuss what the best thing is. I mean if you're going to do only one thing monthly, what should it be? Or, if you're going to three things, what should they be?

MR. MARCO: In our case, we do monthly financials. I personally think quarterly is probably as far as you need to go. I don't think it's easy to spot emerging trends on a monthly basis. Or, if you see a trend, it's hard to believe that it's real, especially if it's not to your liking. We go through this analysis, show it to the CEO, and the CEO will say that it can't be real. It's kind of hard to argue that it is. So you end up giving it another month or two anyway and do a quarterly financial.

I think if you wait and do it annually, that will be a problem. We do a fair amount of dental, which is a short-tail type of business. If you look at that only once or twice a year, you can get yourself in trouble very easily. So I guess the answer is, it depends on how stable the business is and what your aims are. I feel comfortable doing it quarterly. My reserve analytics are done quarterly, even though we do monthly financials.

MR. MILLER: We've been through periods of doing monthlies and quarterlies. Unless you have something that's going to have an awful lot of variability, I can't ever see the benefit of doing anything more often than quarterly, except for looking at mortality and morbidity experience monthly. That seems to be far more dynamic in causing changes on a monthly basis than anything else can be. If you think about a life insurance company's statement, unless you're going to have some big fluctuation in investment income, what can cause it to change on a monthly basis other than experience? There's just nothing else that can happen. So doing all the extra work to get the exact reserves and the exact impact of surrenders, endowments, or whatever, seems to have very little added benefit. Knowing your experience, you could probably come pretty darn close to predicting the bottom line on a monthly basis. You know whether it was a good or bad month.

MR. MARCO: One thing I've found as a direct offshoot of doing cash-flow testing is that, in most systems (we use the Tillinghast TAS System), you have a set of assumptions that you assume as standard assumptions. Then you have to do your dynamic valuation, which is basically where you true up the projection to actual results to make sure you feel it's realistic. In doing that, you apply mortality and lapse scalars. So you can tell pretty quickly, according to your model, where your mortality is (and where it is compared to your assumptions). For example, if you had a scale of 1.1, it's telling you that your mortality is roughly 10% higher than you thought it was originally. I depend on this approach very heavily for my repricing processes.

MS. TRUELOVE: Any other questions?

FROM THE FLOOR: Let's go back to the model in your experience studies on mortality experience and lapse. You have this factor of 1.1 that might show up. How often do you update your experience studies and then feed them into your model?

MR. MARCO: If we're developing a new product, we'll start with a new set of assumptions. But this dynamic validation process sort of updates itself every year. So I tend to be a little lax on doing formal mortality studies because I can get a read on how our mortality is compared to actual as a result of this process.

FROM THE FLOOR: Another comment on those lines. What I've found is it sounds like you have a model that has a large number of cells, so you might have been able to deal with males, females, smokers, nonsmokers, and preferred standards. When you start combining those, it seems to be a lot more difficult to get that validation. There are so many things that come into play if you try to move everything to standard, nonsmoker, or everything to male. It's a lot more difficult to do that type of validation on a gross basis and easily reach a conclusion.

MR. MARCO: There is a certain amount of judgment involved. There's no doubt about that. What you're really looking at is how it progresses from year to year. As I said before, we're a small company. Our normal annual variation in death claims could be as much as 15%, depending on the blocks. But I'm not necessarily going to change my scalars by 15% every year. But if you look at it over a three-, four-, or five-year period, you get a pretty good feel as to whether things are changing. If you draw a line through it, you'll see that it goes exactly where you want it to, even though you might have highs and lows during that period. I believe that you either take this approach or be forced to do a mortality study for every piece of my business every year. We just don't have enough in-force business for many blocks to justify that amount of time and expense.

MR. MILLER: I think the detail of your model makes it possible to do it that way.

MR. MARCO: It was intended to be that way.

MR. MILLER: Yes, it was deliberate. In a lot of the cash-flow testing we do, my tendency has been to overbuild the liability model just because we're comfortable with that. We do differentiate smokers and nonsmokers. The same thing that Steve was saying is, we use that as a way to corroborate our pricing assumptions and to make sure everything is going in the right direction.

I communicate to clients that we've put in our pricing mortality, but we had to put in a 75% scaling factor so that it matched up with last year's statements. We've done those things for several years. That has also been helpful. I sign off as illustration actuary for a lot of those clients too, so you need some comfort that your illustration actuary testing assumptions are reasonable when you say, "Yes, this passes the self-support test, and it passes the lapse-support test." So I found that we could use that model in lot of other areas.

MR. MARCO: I mean the important thing is to make sure you look at the scalars over an extended period of time and not merely change them from year to year. If you did your results, it wouldn't make sense, historically.

MS. TRUELOVE: I'm curious about how many in the audience have internal management systems in place and are doing a value-added approach to your company? How many have those in place already? Just a few. How many would like to have them? Just a few more.

MR. MILLER: I have several clients that are fraternals and their board members are not insurance people. I use some back-of-the-envelope, value-added numbers to show the value of the organization. They can do it. We come up with factors, a multiple to premium, a multiple of reserve, depending on the line of business. The accounting people and financial people at the Society can calculate this and tell the board whether we are going in the right direction or being successful. Several of them have decided they need to get back into the insurance business. They start writing new business and they lose money. Board members don't understand that. You want to be able to communicate to them that we're really doing the right thing by writing more business, even though we've shown a statutory loss. You must overcome some of those hurdles and educate them on statutory accounting. We found that those kinds of things can be very helpful on that side. The management appreciates that assistance because they don't have to deal with the board members all the time and ask them why they're losing money. That's probably different for a lot of your companies. Actuaries understand that. We found that to be valuable.

MR. MARCO: We found that our board is more forgiving as long as the GAAP numbers look good.

MR. MILLER: Most of the Societies don't do GAAP, so we don't have that to fall back on.

MS. TRUELOVE: Anyone with a question? Let's move on to the regulatory environment. What's looming out there that we don't know about?

MR. MARCO: One thing that would probably scare most folks is solvency testing. That's the next evolution in cash-flow testing. I suppose that if the Section 7 exemption is lifted, when the time comes for solvency testing, small companies would probably be affected by it, since there would be no grandfathering, if you want to call it that, for the exemption.

MR. MILLER: I think they'll probably find some of that C-3 testing, too. It sounded like they initially wanted more companies to do that testing, but a lot of companies complained. The exemption was made fairly large, and only a few people are going to have to do it this year, but they're going to change that. They're going to broaden it. I mean this just helps them to get their foot in the door. It's kind of like taking the Section 7 away. They gave it to us to start with, but it's going to be taken away.

MS. TRUELOVE: Your comment just reminded me of something else that was said at another session: even though companies are exempt from that, the rating agencies might require it. So if you're concerned about your ratings, then you still might have to go through that testing anyway.

MR. MARCO: That was the gist of the discussion. It was Duff and Phelps.

FROM THE FLOOR: Yes, it was Duff and Phelps. It wasn't A.M. Best.

MR. MILLER: That's correct. Best wasn't mentioned at all in the discussions.

MR. MARCO: Best has its own method of calculating RBC, which is only loosely related to what you do in the blue book. We call it a blue book.

FROM THE FLOOR: By Blue Book, do you mean the Blank?

MR. MARCO: Yes. I must remember not everybody has a blue book.

MS. TRUELOVE: Any more regulatory information?

MR. MARCO: Other than codification?

MS. TRUELOVE: Go into the codification.

FROM THE FLOOR: You say there's a session on that.

MR. MARCO: There was a session on that, and it appeared to me that most of the issues were more accounting oriented. Probably one offshoot of the whole thing is that the end result will be that if the NAIC adopts a rule, whether your state adopts it or not, you might end up stuck with it.

MR. MILLER: You certainly have to deal with it or you might have to calculate reserves according to that standard in addition to what your statement requires.

MR. MARCO: Right. Then justify or explain the difference.

MR. MARCO: Realistically, most of us aren't going to file separate statements in various states to satisfy individual requirements.

MR. MARCO: We do something like that now with the universal life model regulation. I don't believe Kentucky, which is our domiciliary state, has ever adopted it. But a number of states have adopted, and it effectively becomes extraterritorial. So I could see that happening on a much larger scale.

MR. MILLER: That's a good example.

FROM THE FLOOR: Is anybody besides me concerned about what we'll do if we come up with a new standard valuation law without having formula reserves with safe harbors?

MR. MARCO: I didn't hear any mention of it.

MR. MILLER: Wasn't there a component about peer reviews? I guess I don't know what that means. That sounds like an expense that you're going to have to face.

MR. MARCO: In another session, the speakers said that the unified valuation system (UVS) will have some formula reserves. Did I hear that wrong?

FROM THE FLOOR: It's still an open issue. That's what I heard. Right now, they're talking about adding it in, but they held out the possibilities that they might do away with it.

MR. MARCO: That concerns me, too. I mean it's hard to believe that the regulators would allow a system that doesn't have some sort of formula reserve as a safe harbor. I don't know that that would make much sense. We would hope.

MS. TRUELOVE: Other issues on regulatory?

MR. MARCO: How could a regulator not want some sort of formula reserve in there. I mean judgment can take them only so far in getting comfortable with reserve adequacy.

FROM THE FLOOR: My opinion as a regulator is that you are correct. The more sophisticated the product, the more the UVS would come into play. I think the formula reserves would work better for the less sophisticated product (for example, traditional life).

MR. MILLER: Isn't that really what has driven some of the work on the UVS, the universal life, and some of the new products? People aren't concerned about that.

MR. MARCO: The universal life model regulation reserve isn't anything to brag about either.

FROM THE FLOOR: You're correct. Let's go back to the codification question. What are some of the reserve implications? I've seen a lot of the accounting ones, and I haven't seen a lot of reserve implications with codification.

MR. MARCO: The only one I'm really worried about personally is the extraterritorial piece. If a particular state adopts a reserving requirement or the NAIC adopts it, you're effectively stuck with it. They're going to incorporate guidelines as part of this whole process. In many cases, you'll be stuck doing it and paying the difference.

MR. MILLER: I think XXX is going to be one of those, too. I mean if you're a Wyoming only company or something, you might not be holding XXX reserves.

FROM THE FLOOR: There are bigger states than Wyoming that haven't adopted XXX.

MR. MILLER: Michigan is an example.

FROM THE FLOOR: There's a disadvantage there with not having XXX if you want to use it on your own life products.

MR. MILLER: You don't have any X factors either. I think that's what Bob's getting at when he talks about not having XXX.

MR. MARCO: The bottom line is you'll be doing a lot of work, whether you really want to or not for other reasons.

MR. MILLER: That's right. You'll have to deal with XXX, even if you're only in Michigan.

MS. TRUELOVE: Any more questions on regulatory issues?

FROM THE FLOOR: I've not heard anything at this session about small policies. We've become sort of afraid of the small policy issues and how some regulators have confused the race-based issue with the small-policy-size issue. They're calling them low-value policies and all sorts of things. As a company that writes a lot of final expense and has a lot of burial policies, we're sort of worried about it. I haven't heard anything on this session. Is anybody else worried about that? How are they trying to deal with it?

MR. MARCO: We sell a lot of final expense and low-face-amount policies. My personal take on it is that I think it's more of a political issue than an actuarial issue. For some reason, it's not reported that way in the press. There might be issues involved on an actuarial side, but those of us who price products realize that a small face amount is going to have a much higher expense per 1,000 factor than a larger policy. There's no way around that if you're going to charge a premium that makes it work. The only other element would be commissions; obviously, you pay what the market requires to sell the product. I don't know how you get away from that.

FROM THE FLOOR: Please address the upside-down problem. Are you familiar with that term?

MR. MARCO: No.

FROM THE FLOOR: That's when the premium paid exceeds the face amount. When you're selling your house, you don't get your fire premiums back.

MR. MARCO: I guess my only argument is you are providing protection, and you only know whether you're going to pay more than the face amount after the person has died.

FROM THE FLOOR: The upside-down problem is the hot topic at this time.

MR. MARCO: I'm assuming that if you go through an actuarially proper pricing process, and that's the way it turns out, then it's not fair to say it isn't equitable. It is equitable because you've used the proper techniques.

FROM THE FLOOR: I beg to differ. Your company might be doing it right, but I've seen some that aren't.

MR. MARCO: We don't have many products where that's true.

FROM THE FLOOR: We have run into that.

MR. MILLER: My experience with those things, as far as pricing, is if you don't start grading back the commissions at the older ages, you're going to get into situations. For example, if they don't die between years three and seven, then it would have been better for them to have put their money in a savings account instead. I talk to my clients about that and ask them if they realize what they are selling. I tell them it doesn't look very good. We need to grade starting at age 70 and start reducing that commission. It is almost like a target premium on a universal life. When you get to a certain age on universal life, the target premium usually flattens because of your surrender charges and nonforfeiture law. I believe we really need to be looking at that on the final expense or something like that, so that you can get a premium at 80 or 85 that doesn't cause an upside-down problem in the first five years. In ten years, at age 85, that might be reasonable.

FROM THE FLOOR: It doesn't happen in the first five years?

MR. MARCO: No.

FROM THE FLOOR: But it could happen in the first ten. I have seen situations where that has happened, and it is unfortunate.

MR. MILLER: Yeah.

MR. MARCO: That's not the case in the final expense products I've looked at, at least in terms of what we consider our competition to be. If you issue it to a 15-year-old, and you add 85 years worth of premium, does it exceed the face amount? I haven't looked at that. For the most part, the premiums seemed reasonable and in line with what you might expect. There might be some types of business, and possibly pre-need is one of them, where you might find those kinds of situations. That becomes a little more complicated because you have to build in death benefit increases in most pre-need products during the pricing process.

FROM THE FLOOR: I think the solution is to not bring in actuarial issues, but the solution is that the companies must examine their book of business. After a number of years, they'll get a voluntary basis on what's happening. It will probably keep everybody happy.

MR. MILLER: It is based on duration or something like that.

MR. MARCO: That might be a solution, but that's still a political solution and not an actuarial one.

FROM THE FLOOR: That's correct, yes. This is a hot topic, and we might see more of those things in the future.

MR. MILLER: The fraternals look at it that way and they say, "We can't really do this to our members." They'll change the product to be more reasonable. I know that the National Fraternal Congress is giving some input to that lobbying process and working with the regulators to let them know about what some smaller societies sell.

FROM THE FLOOR: What was that potential solution?

MR. MARCO: The proposed solution was that, at some period in the future, after certain amounts of premium had been paid, there would be some sort of dividend or an increase in face amount.

FROM THE FLOOR: I didn't sit in on the NAIC meeting when this was discussed. My understanding of what happened is it is looking at anything below $15,000 as a small amount policy. Based on what I heard secondhand, disclosure did not come up. It seems to me that a rather simple, straightforward solution would be disclosure.

That will require providing more information at the time of sale, but if a customer knows what can happen in five or ten years, then it seems to me that regulation should step back from it. I'm saying that as a regulator, by the way. We shouldn't play a role in that if there's sufficient disclosure.

I just found it interesting that nobody brought that up. If you want to protect the small market business or the pre-need business, that might be something that needs to be supported. Somebody's going to have to go to the NAIC meetings and represent a position like that, if they think it's worthwhile. What is your reaction?

MR. MILLER: That reminds me of something we might see in a sophisticated illustration for a universal life. They're looking at your rate of return at death. It is something along those lines that uses that kind of a calculation.

FROM THE FLOOR: You better develop it rather than let the NAIC develop it or we'll have at least 15 pages. West Virginia already requires such disclosure on policies of $25,000 or less. It is a bit onerous in this regard. The disclosure simply says you have to show the cash value at the end of 5, 10, 15, or 20 years, and at age 65. You have to show the amount of premiums paid at that point. If the amount of premiums could ever exceed the face amount, what year would that occur?

I say it's onerous because they go up to $25,000, and it's $25,000 or less. They don't define what a premium is for a universal life plan. We sell universal life down to $20,000. By fiat, we have told our agents the minimum policy you can sell in West Virginia is $25,001.

FROM THE FLOOR: I just wanted to comment on the statement about disclosure. It has been a very hot topic in New York. What has been happening is that companies that write pre-need and home-service-type products charge a very high premium, and within a ten-year or a seven-year period, their premiums are exceeding the face amounts of the policy. New York was not allowing those premium rates. They were considering it excessive. Many of the companies were having problems by saying that New York doesn't have the right to regulate what the premium rates actually turn out to be.

So one of the solutions was to put in disclosure language that would say New York would permit the premium rates, whatever they turned out to be, even if they were thought to be excessive. You'd have to put language in the marketing material. This is for all policies under $25,000 and less. The marketing material would have to say that this policy might have premiums that exceed the death benefits, and it could be an excessive policy. You might want to look elsewhere. That's the kind of language they were thinking of. You might want to shop around.

The problem that was happening was they wanted to do this across the board. Any policy less than $25,000 had to have this material, and this marketing disclosure. The problem is there are certain companies, including mine, and a lot of other companies, that are not in the pre-need or home service market and that do not fail this seven-year or ten-year test. They're trying to require us to put that language in when it's really not relevant to our particular products.

That has been a very hot topic because some of the small companies have been battling against each other. Because of the pre-need and home service market, they don't mind that disclosure because they don't think it will really affect their sales. They just don't want New York to regulate the rates. The other companies don't want that language because it's not applicable, and it would scare the prospective customer off from purchasing the policy to begin with. It has been a very hot topic in New York.

MS. TRUELOVE: Understandably so. Any more comments on small policies?

MR. MARCO: If companies are not allowed to sell small face amount policies, then there will be a large market that will go unserved. So some solution has to be found, whether it's increasing the face amount or refunding premiums after a certain point. The product has to be viable from a company's perspective or else it isn't going to be offered.

FROM THE FLOOR: Just remember that if regulators try to retroactively make companies increase the face amount, it will take a lot of companies down.

MR. MARCO: That's true.

FROM THE FLOOR: This is especially true of older, small companies and not necessarily true of home service companies. They have a lot of that type of business on their books.

MR. MARCO: At that point, that's the more profitable block of business, too. Most of us would love to have a seasoned block of traditional business.

MR. MILLER: I don't think the recommendation is onerous to enhance the face amount. It's a voluntary exercise when any reasonable person would look at it and say this is ridiculous.

FROM THE FLOOR: I think that any reasonable person would look at it and say it's ridiculous, but they would also say it was ridiculous if it was a very legitimate pricing situation (such as if a 20-paid plan wound up with more at a higher age or wound up with more premiums being paid on a very normal pricing basis).

FROM THE FLOOR: The situation you're describing is more reasonable. I've seen outrageous situations.

FROM THE FLOOR: I know. You're right. You mentioned everybody in the same brush and this is the thing that worries me. I know there are bad situations there and I agree with you.

Something ought to be done. But the press doesn't know the difference between a legitimate spreading of the risk and sharing of the risk and what you're talking about.

FROM THE FLOOR: You are correct.

MS. TRUELOVE: Let's move on to our last topic, which is the use of outside consultants. My first question would be, how do you find the right one?

MR. MARCO: Because I am with a very small company, we have to use outside consultants fairly often. Realistically, you use word of mouth, sun spots, or do anything to try to find someone who has the expertise you're looking for. When we first got into the pre-need market, we were looking for someone with very specific pre-need experience on a large scale. We spoke to a few people. Everybody was an expert. It became difficult to determine who was the right person, so we ended up using three different people.

MS. TRUELOVE: All at the same time?

MR. MARCO: No, at various stages. It could have turned out that way. The big problem is you can either pay the price to go to a very large firm, which will have some expertise in everything, or go to a much more reasonably priced smaller one. It is tough to know whether they have the background you're looking for, and it becomes less likely in a smaller firm. There are folks out there who know it. The trick is, how do you find out who they are?

MR. MILLER: You might know who the consultant is for your competition. That might be one approach.

MR. MARCO: It's tough to try to use them.

MR. MILLER: You can get the referral.

MR. MARCO: It's kind of hard to say what are they doing. They can't tell you.

MR. MILLER: Yeah.

FROM THE FLOOR: My question associated with that is how do you make sure the consultant is doing everything that he is supposed to be doing?

MR. MARCO: I can tell you what I do, and we can see where we go from there. Basically, keep in constant touch with the consultant and try to stick your nose into as much as possible without, obviously, interfering with the work. We have some folks that we deal with through e-mail, because it becomes a lot easier than playing telephone tag. We ask for weekly updates and try to get to the point where there is something to be looked at. Make a point of setting aside time in your schedule to look at it. The last thing you would want would be for a person to take the ball and run with it and then find out three months later that they missed the point. You also don't want to have to go back and ask them to change what they were doing. They'll be glad to do it, but it's going to cost a lot more money.

MR. MILLER: There was an article several years ago in the *Actuarial Digest*, written by Ed Cowman, who had experience on both sides. He had been with a smaller mutual company for several years, and then got into consulting for a few years. At that point, he wrote an article. I thought it was very helpful and very good. I've always been a consultant, so I've never been on the other side.

FROM THE FLOOR: We had an experience where we needed to bring in an outside consultant with some expertise in a particular area. We found that consultant by talking to our reinsurer. In fact, at that time, we were actually interviewing several reinsurers and taking bids, so we probably got more than one opinion. I think talking to your reinsurer is a good way to find out who is out there in the consulting area who actually can provide the services needed.

MR. MILLER: That is a good way. We've gotten referrals that way from people because their reinsurer knows we have some expertise.

MS. TRUELOVE: I'll just add that, as a reinsurer, if you get a recommendation from one, it's usually a very good one, because they are very hesitant to recommend anybody that might burn you. They want to keep your relationship solid, and they don't want to recommend somebody who they don't fully trust. If you get a recommendation from a reinsurer, it's usually a very good one. Any questions on the use of consultants? I thought this might be a really lively one.

MR. MILLER: I think you'll have some different options, depending on what you want them to do. If you want them to put the model together and do all the crunching, you want to look for a firm that has some people that aren't going to be billing at the top rate. Maybe that's obvious, but some firms have more finders, minders, and grinders. But if they have more grinders on their staff, you can count on them to do that. For example, our firm does a lot for our clients. We are their actuarial department, so we have a mix of personnel and experience. Some firms have a lead consultant and some people that keep track of the projects and people that are crunching the numbers, like you would have in your actuarial department. You have firms like that or you have the larger ones at which somebody comes in for a day and tells you everything you need to know to do the project. Then you start doing it. You need to decide what you need and what you want, and what your management team is looking for.

MR. MARCO: Another point is, how quickly do you need it done?

MR. MILLER: That's true.

MR. MARCO: We've had some situations. When I first joined my company, we were looking at a possible acquisition, and we needed something done in ten days. One person's not going to set-up a model to appraise a company in ten days. So we were forced to use one of the big guys who threw plenty of folks at it in order to get the appraisal done. Obviously, if you have plenty of time, you can use a smaller operation. Most consulting firms could do something like that in a ten-week period.

MR. MILLER: It depends upon what time of year it is.

MR. MARCO: That's true. Never ask consulting actuaries to do anything at year-end. That would probably depend upon what the job at hand is and how time pressured you are.

MS. TRUELOVE: Maybe you can explain some of the differences between large and small consulting firms, and what kind of expertise you can expect from each of those. Our consulting firm might be small in number, but the spread of the different areas of focus are quite varied.

MR. MILLER: The mix in the smaller firms is driven by the clients that you have. It reminds me of the typical four box diagram where you have your existing clients and new clients. You have projects you know how to do and things you don't know how to do. Box number one is working on things you know how to do with clients you already have. Then you expand in the other direction. You might be getting new clients, but you're doing projects for them that you already know how to do, or existing clients are telling you what direction they want to go. They might want to learn about equity-indexed annuities. You have a relationship there, and you're expanding your expertise.

You want to stay away from that box that includes clients you don't have and things you don't know how to do. You can get a really bad reputation quickly by getting in that area. Maybe we can continue to work on things we know how to do with clients we already have. Maybe this client isn't active in this particular product line. The client might ask you for ideas and you can say, "We've done something like this several times, and we think this is a good fit."

You have more experts in the larger firms, and they present it that way. They can find somebody in the firm that has done quite a bit of work in a particular area. As for the smaller firms, you just need to get to know them and look at it from that standpoint.

There are the one-man shops that do certain things, the medium-sized firms, and the large firms. I'm not sure where you draw the line in determining what those look like. I've always been in what I call small-to-medium-sized organizations. At times, we've had very aggressive clients, and we have been working on some very interesting projects.

FROM THE FLOOR: I've been on both sides of the shop, too, and I'd just like to suggest that if you do go to a large firm, you want to find somebody who specializes in small companies. Otherwise, you might be getting a large company solution for a small company problem.

MR. MILLER: That's a good point.

FROM THE FLOOR: New York Regulation 126 has a requirement. If you have significant reinsurance, you're supposed to demonstrate that assets and liabilities are matched gross of the reinsurance in order to take the reserve credit for it. I'm wondering how companies are dealing with that.

FROM THE FLOOR: We tend to take a simplistic view that the cash flows from the reinsurer match the liability exactly, so it's really just a reinsurer stability question. I know that's simplistic, but I think it's realistic, too.

FROM THE FLOOR: I'm revisiting the issue of X factors. With the Monte Carlo simulation and hypothesis testing, the end result of this is a regulation that wants you to say that your valuation mortality is greater than your anticipated or pricing mortality. From a statistical point of view, you can have a result that the mean valuation deaths, or at least standard deviation, are smaller than your mean anticipated deaths, and I find this perverse. It just doesn't seem to fit with the goals of valuation that one can use a mortality table smaller than the pricing table. That is one reason the whole idea of hypothesis testing doesn't sit well with me. I have a hard time telling my appointed actuary to use an X factor when the result is smaller. That's just a comment on the whole idea of using simulation and hypothesis testing.

You asked earlier what kind of risks you have for setting X factor structures. If you use a general structure of X factors, like one X for all your plans or all your smoker/nonsmoker combined, you'll probably get more credible information. However, if you start issuing more preferred risk over what you assumed, you're going to start getting a far different deficiency structure, and it's going to hit your bottom line differently than what you expect. Those are my two comments on X factors and XXX.

MS. TRUELOVE: That's very true of the impact of the X factor, especially on resetting reserves. A more refined approach might be quite a shock when you have to adjust and find that those deficiency reserves really shoot up if you go by age or those kinds of things.

FROM THE FLOOR: Let's go back to the Actuarial Opinion Memorandum Regulation (AOMR) which they've been talking about revising for ten or twelve years. It has been ongoing. In the past, the National Association of Life Companies (NALC) and the American Council of Life Insurers (ACLI) have been successful, on behalf of the small companies, at keeping the Section 7 requirement. Some of the earlier comments indicate that this is a done deal and that Section 7 is almost gone at this point. I know the NALC is doing some stuff, but I'm not too close to the details. Can anybody comment on whether it is still pushing for keeping Section 7? How is that fight going, and what will that step be?

MR. MARCO: I can't speak to what the NALC is doing, but my understanding is that it seems likely that the Section 7 exemption will no longer exist after 2000 unless a lot folks start making a lot of noise. I think it's fair to say that the regulators believe it shouldn't be there. Perhaps we can get the thoughts of some of the regulators in the audience; however, my understanding is it probably won't be there at this time in 2001.

FROM THE FLOOR: This is my view, not the universal regulator's view. Section 7 doesn't tell us anything we don't already know anyway. To send a lot of these small companies into an onerous, rigorous calculation routine is not really fair to them.

FROM THE FLOOR: I sit on the Life and Health Actuarial Task Force for the NAIC. I'd like to comment on your response to the gentleman's question. I was with the company that helped form the NALC, (so I don't have a good relationship with those people). An exposure draft, detailing what the NAIC intends to do with the AOMR is being exposed for comment now. Section 7 is out as an opinion only. Section 7 is definitely being exposed for comment. It's expected to be adopted in December. The NALC has said that it will go to the A Committee and try to stop it. Then they will try to stop it on a state-by-state basis.

I guess I have two opinions about that. First, if I was a small company, I'd do the same thing. I'm in Arkansas, and we have a lot of small companies and funeral companies, so the small amount issue is very important to us. This issue is important. The way I will handle that issue is you can do a Section 8 opinion for me on basically two pieces of paper. You don't have to do cash-flow testing. If you have Treasuries, and you're selling pre-need, and if you can show me that your mortality is somewhere in the vicinity of the reserves you're releasing, that is okay. In other words, it's no worse than your 1958 Commissioners' Standard Ordinary (CSO) or your 1980 (CSO). In my opinion, you've come darn close to completing a Section 8 opinion.

The problem is, if you go from state to state, that isn't going to happen. I like the idea that you guys have to look at the asset side and at least assure me, the regulator, that the assets aren't totally out of line with the liabilities. You can do that in the page. If I were with a small company, I think I'd take the NALC side, because, from state-to-state, you're going to have some regulator who's going to want cash-flow analysis and you're a little company. I don't know what to suggest to you except that John might have problems in Arkansas, so consider redomestication.

MR. MILLER: It was effective, huh.

MS. TRUELOVE: I have a question that was given to me. Do consulting firms ever use other consulting firms?

MR. MILLER: We do in the sense that we use another consulting firm's cash-flow testing software. There have been times where we've used a different firm to enhance that software for us. Back in the days when we were struggling to model collateralized mortgage obligations (CMOs), there was another firm besides the software vendor who could do a better job modeling the CMO cash-flows, so we have used other consultants. But that's not that common for us.

MR. MARCO: You probably used it as overload as well.

MR. MILLER: Yes.

FROM THE FLOOR: My comment is in regards to the same issue. Most actuaries from consulting firms go to meetings like this, and we network with some of the other insurance people and consultants. It's kind of comforting to know that even if I don't know the answer, I have a group of people I can consult to find the answer that I need to solve the problem that my client is presenting to me. In that regard, consultants end up using other consultants.

FROM THE FLOOR: Not for a fee.

MR. MARCO: Time for a plug. One of the earlier questions was what can we do about protecting the Section 7 opinion. I'm no longer on the board of the Small Insurance Company Section, but I do know they are very much concerned about it. They considered, for the first time ever, issuing a public statement of opinion relative to this.

In the end, it was decided that it was too much of a lobbying issue for them to do it as their first statement of public opinion. They have blast e-mailed all their members recommending that they write to the NAIC. They listed the different people that should be written to in support of retaining the Section 7 opinion. Do you want to know what you can do? E-mail a letter. Write to these people if you want to protect your right to have a Section 7 opinion.

FROM THE FLOOR: I think John from Arkansas got it right. It's really not whether you have or do not have the Section 7 opinion. It's that there is some kind of recognition of the company's position and a modified simple version would be sufficient. So Section 7, in itself, is not the issue. How much work will the small company have to do to satisfy the regulators that it is in a solid position?

MR. MARCO: I think it's fair to say that, as an appointed actuary, you have to satisfy more than just the regulator with your opinion.

MR. MILLER: Sure.

MR. MARCO: What happens if you take a shortcut and then two or three years later that company goes insolvent?

MR. MILLER: Then you didn't do it right.

MR. MARCO: The reason why I think you don't want to take a shortcut is because someone will say you made a mistake. You've just illustrated my point.