The Actuary

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The Actuary
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THE CASE FOR POLICIES WITHOUT GUARANTEED CASH VALUES

by Lorne Campbell

The pricing actuary's task is formidable. Each year, although the raw materials that determine the price of his product are often becoming more expensive, that price must, at least ostensibly, drop.

Policy issue and maintenance costs move inexorably with inflation levels — selection costs rise alarmingly — lapses eat up record amounts of unamortized acquisition costs — the government seeks ever larger contributions to its coffers — competition from other purveyors of financial services pushes up costs of our traditional distribution systems — and increased regulation, e.g., from the S.E.C., adds dramatically to compliance expense. And all this is happening in an uncertain economic atmosphere, requiring actuaries to understand and cope with the risks associated with uncertainty.

Nevertheless, an insurable person today can generally buy permanent insurance at apparently lower cost than ever before. How has this been achieved?

It has been accomplished by mercilessly squeezing profit margins, by assuming recent lapse experience to be a passing phase, by swallowing mortality declines as quickly as they appear, by weakening valuation and non-forfeiture standards, and by invading traditional field compensation. We have introduced non-guaranteed premiums, we have designed interest-sensitive, universal and variable products, and soon a combination of all these innovations may sweep the market. Yet the downward pressure on premiums continues. If our product objective must be to offer minimum-cost guaranteed-premium, permanent insurance, then

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TROWBRIDGE TO BECOME EDITOR OF *THE ACTUARY*

We announce with great pleasure that C. Lambert Trowbridge has accepted our President's invitation to become Editor of this newsletter.

Elected to Fellowship in 1946, Mr. Trowbridge has been both a major contributor to our literature and a leader in our committee and administrative work. He served as Society President in 1974-1975. In his business career he has performed with distinction as a company actuary, as chief actuary of the Social Security Administration, and as a professor of actuarial science. Now retired, he and his wife live in Seattle.

From Mr. Trowbridge our contributors are assured of incisive yet sympathetic editing, and our readers of stimulating issues.

E.J.M.

IDEAS FOR POTENTIAL AUTHORS

by Robert B. Likins

Since sharing expertise is an important part of professional development, we of the Committee on Professional Development offer readers a reminder of several ways they can foster their own professional development through submitting their ideas for publication. The editors of all the actuarial journals listed here are eager to hear from authors.

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The purpose of the Society newsletter is to let actuaries and students say what they want. There are no written guidelines except that contributions must be signed and are subject to editing. Articles or letters may generally run up to two columns in length (about

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DEMOGRAPHY AND EMPLOYEE BENEFITS IN PEOPLE'S REPUBLIC OF CHINA

by Robert J. Myers

In the course of a visit lasting about 21 days to the People's Republic of China in April, I made certain random investigations of demography and employee benefits that subsequent cross-checking seems to confirm as valid.

Because of its huge population and relatively limited natural resources, China has for several years had a strong policy that there should be no more than one child per couple. Couples who have "over-quota" children are penalized, e.g., by having to pay the medical charges for them, and even by reduction in salary.

China has no nationwide social security program for either the government agencies and individual factories and other work establishments (almost all owned by the government), or the communes or districts that comprise the remainder of the country and economy (these engaged mostly in farming). Once persons begin employment, they rarely leave their original work establishment or commune.

The communes have no old-age, disability, or survivor pensions. Protection in these areas is provided through the extended-family approach; in the few cases of individuals without a family, the commune gives subsistence.

But there is a general governmental requirement that government agencies, factories, and other work establishments have pension plans with certain common characteristics. The pension starts at the mandatory retirement age—60 for men, 55 for women. My enquiry why men and women aren't treated equally yielded no really adequate response; one woman described

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funding even low cash values and hence providing for the resulting C-3 risk may not be the best approach.

What Next?

Companies are already offering whole life products with low cash values and extraordinarily low premiums. The next step must be to face the ultimate question, What is the lowest guaranteed premium that will fund death benefits and precious little else? In such a search for the ultimate net payment product, it has been shown that if guaranteed values can be eliminated, premium reductions of the order of 10%-20% may still be possible.

And why not? We have already moved far in that direction by offering participating products whose illustrated cash values are more than half dependent on non-guaranteed dividends, and a policy without guaranteed cash values may be less liable to abuse by a poorly advised company management than is a non-guaranteed premium policy.

Policy designers may give thought to policies with no cash or other nonforfeiture values at any duration, or policies offering paid-up and extended term but with cash values after, say, the 15th year only, or, as in the U.K., policies whose cash values are determined from time to time at management's discretion. I believe that only the second and third of these three possibilities have merit.

The historical argument in favor of guaranteed values is of course impressive. We may reflect upon Britain's notorious insurance auctions of the 19th century that led to demand for guaranteed values in America. But we must recognize that the U.K. experience has shown that a country blessed with a responsible actuarial profession can successfully undertake to offer equitable non-guaranteed withdrawal benefits.

The Outlook

This article has concentrated on the merits of non-guaranteed cash value products as a means for giving the public death benefit coverage at the lowest possible premiums. But the beneficial effect on the insurer's financial stability demands at least equal consideration. Traditional level premium products have the potential of causing massive financial drain on an insurer in times of depressed security values, as has already been demonstrated on deferred annuity products. The public is more and more showing its ability to engage in severe financial anti-selection. Can all of us be sure that we would survive a massive run on cash values in an already high and possibly increasing interest rate environment?

At the Society's meeting on interest-sensitive products in New York last spring, speaker after speaker offered a way to cut the C-3 Gordian knot — simply eliminate that risk by wise product design. Ditching existing product lines cannot be accomplished overnight, but surely actuarial support for a movement towards rational products such as variable life, non-guaranteed cash value life, and level commission term, would be a gigantic step in the correct direction.

PEOPLE'S REPUBLIC OF CHINA

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the arrangement as unfair to women saying that its purpose was to have women available to take care of grandchildren while men could stay at work and avoid this chore.

The retirement pension amount is 75% of basic pay (but note that all workers get so-called bonuses amounting to at least 15% and perhaps more than 30% of basic pay, so this pension rate is well below 75% of total renumeration). A somewhat higher rate is paid to officials and to those who had been active in helping the Communists achieve control of the country in the late 1940's.

Disability pensions are at the same rate as retirement pensions. All pensions are paid out of current funds without recognizing the liability involved; hence different work establishments may have widely different pension costs. There are no survivor benefits except lump-sum payments meeting burial expenses and continuation of the deceased's base pay or pension for six months. Widows' pensions aren't generally necessary, anyhow, because both spouses must work if able. Women get pensions on their own earnings records.

All medical care is furnished by government hospitals and their outpatient clinics. Charges, which may well represent less than real costs, are paid by the work establishment or commune—100% for the worker, 50% for the first child or for subsequent children born before the one-child family principle was established. Cash maternity benefits at full base pay are provided for limited periods before and after a first birth.

DEATHS

George M. Bryce, F.S.A. 1943
Carl A. Haase, F.S.A. 1954
Oswald Jacoby, F.S.A. 1927
William F. Poorman, F.S.A. 1925

OSWALD JACOBY (1902-1984)

Although absent from actuarial practice for most of his illustrious career, Oswald Jacoby never lost interest in or touch with our profession. Walter Klem tells us that a few years ago the two of them resolved to attend the 100th anniversary of the Actuarial Society's founding together; Mr. Klem comments, "Alas!"

Mr. Jacoby was rightly proud of having completed the exams for Associateship at age 19½, and for Fellowship at 21½, a record that stood for many years. In our October 1979 issue we quote him thus:

> "I might well have appeared as having completed the fellowship before reaching 21. J. D. Craig (Actuary of Metropolitan Life then) refused to let me do that. The conversation was:
> 'I can pass them.'
> 'Yes. But I want you also to learn the subject matter'."

His one and only, we think, appearance at a Society of Actuaries meeting lingers fondly in one's memories of a famous man with a winning personality. It is recorded in T.S.A. IV (1952), 148, giving his account, as Commander Oswald Jacoby, U.S.N., of the Korean armistice negotiations at which he was present.

Surely the Society would do well to pause in honor to our profession's most famous bridge player, at the bridge tournament as well as the general session, in Toronto this fall.

E.J.M.