The Actuary

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Reinsurance Section

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problems associated with self-administered reinsurance. In March 1985 an exposure draft of Guidelines for the Reporting of Self-Administered Reinsurance was released to Section members and software vendors. The draft was presented in panel discussions at the St. Louis and Quebec 1985 spring meetings. A revised version was presented for a final discussion at the Boston 1986 spring meeting. The final guidelines have been published and were read into the Society proceedings at the 1986 Annual Meeting in Chicago.

Plans underway by this committee include an exposure draft on audits conducted by reinsurers, which is planned for late 1987 or early 1988. A preliminary survey gathering data regarding audits has already been sent to reinsurers. There are also plans for a workshop on electronic data transfer.

Education

There was a one-day seminar on AIDS presented in conjunction with the spring 1986 meeting in Boston. 140 members registered for the seminar and 129 actually attended. This was considered a good turnout and resulted in a modest financial gain for the Section.

Election

In carrying out the election process each year, this committee has noted a decline in the number of ballots as well as in the percent voting. An attempt will be made to counteract this trend by expanding the biographical data included in the ballot material mailed to members. An article will also be included in the newletter prior to the election urging members to vote.

Financial/Tax

The charge of this committee was recently expanded to include the monitoring and reporting on all reinsurance regulatory activity. Initially its interest was limited to the financial and tax areas. The NAIC Technical Advisory Committee has requested advice on reinsurance ceded and this committee will be one of the sources.

Plans for the balance of 1986 and 1987 are to compile and maintain a list of industry tax, accounting and regulatory committees and appoint liaisons from this committee to each of the other groups for purposes of providing both input and resources from the Section. There are also plans for a regular column in the newsletter dealing with regulatory and other financial/tax issues of current interest.

A panel discussion and follow-up workshop on Financial Reinsurance was included in the program for the Annual Meeting in Chicago.

Program

This committee has been actively planning programs for Society Meetings for the years ahead. In addition to regular programming a half-day teaching session on negotiation is planned for 1987 and there are tentative plans to offer a teaching session on practical uses of risk theory in 1988.

Statistical

This committee will produce an annual reinsurance experience summary which will incorporate the survey previously conducted and distributed by NARE. Munich American Re will play a key role in this project.

Discussions are currently underway regarding who will be responsible for continuing the large amount mortality study initially produced by the Equitable Society. Several alternatives are being considered including a non-insurance company.

Treaty

Plans include a project to review standard treaty provisions gathering input in this review from both ceding and assuming companies.

Underwriting

A panel presentation and follow-up workshop on Reinsurance Underwriting Issues was presented at the spring meeting in Boston. This committee also produced an article on Alcohol Abuse in the June 1986 issue of the newsletter.

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Thanks are in order for the Section members who have participated actively on the Council as committee chairpersons and as program participants. The Section owes most of its success over the last few years to these individuals. Any of the readers wishing to participate in Section affairs who are not presently involved should contact Denis Loring at his *Yearbook* address. □

Taxation of Life Products

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ination rules applicable to group-term life insurance plans and group accident or health plans whether insured or self-insured.

The members of Congress primarily responsible for drafting the new provisions point out that any particular changes that result in tax increases for individuals should be considered in the context of a bill that overall will reduce taxes paid by individuals during the period 1987 through 1991 by $122 billion and increase corporate taxes for the period by about the same amount. □

STATUTORY ACCOUNTING FOR COMPUTER SOFTWARE

by Robert J. Johansen

Instructions for the 1985 NAIC Life and Health Annual Statement Blank state:

> Under no circumstances should computer software other than operating system software be considered as an asset, either admitted or non-admitted.

Historically, this rule evolved when hardware costs were substantial compared with the cost of software, much of which was either bundled with the hardware or produced by the user's staff, with or without outside assistance. Now hardware costs on a capacity basis have dropped while bundled software is rare and the costs of developing or purchasing application software have soared.

With the compexity of today's Life and Health insurance plans and processing, the costs of developing appropriate software in house are now so high as to tip the scales in favor of purchased software where, in effect, several companies share the development cost. Even so, the cost of a complete system can run to several million dollars. Under current rules this cost must be expensed in one year, dealing a severe jolt to statutory earnings. The reasoning behind the rule was that software, then often customized, did not have a resale market value.

It is time now to reevaluate the Blank's treatment of software.

Suppose we postulate that software does not have a resale market value.

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Statutory Accounting

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Nevertheless, it is a producing asset for a company in that it replaces prohibitively costly clerical operations and permits the company to compete by providing faster, better service and the ability to offer the complex plans of the marketplace. In fact, substantial software acquisitions are cost-justified by return on investment or by payback out of savings in a comparatively short period of years.

If a company's statutory earnings would be severely impacted by expensing the cost of expensive software in one year, it will be forced to forego the purchase and either lease a system or contract for administrative services. In either case, the decision is not made on the merits. It is time for a change.

The development by the American Institute of Certified Public Accountants (AICPA) of its recommendations for accounting for software, whether purchased or developed in house, is pertinent to this discussion. In general, the AICPA holds that software for research and development (R&D) should be expensed; software intended for sale or for use in carrying on a company's business should be held as an asset and amortized over its useful life.

Purchased software has, today, become very much a commodity which can be used by a fair number of different insurance companies and service bureaus. In fact, if companies wish to have the vendor maintain the software and update it for new laws, regulations and products, they customize it as little as possible. Again, newer software systems are designed so that the customizing is via files or tables and is not part of the programs themselves.

Because of questions which may arise as to the fair market value of software, particularly that developed in house, this proposal does not suggest carrying software as an admitted asset even though a purchased administrative or accounting system obviously has an inherent value. Rather, software would be carried as a non-admitted asset much like furniture and fixtures. Under the proposed new rule:

- Software which has been produced as part of an R&D effort or is used for R&D must be expensed;
- The cost of software is charged against surplus, not earnings, in the year of acquisition;
- The cost can be amortized against earnings over the useful life of the software in accordance with good accounting practice (cf. FASB 86);
- Management's decision as to rent or buy can be made on the basis of the long run welfare of the company, not because of an accounting rule;
- A company's surplus is not changed from that under the current rule;
- A threshold limit will eliminate minor programs which tend to be short lived and should properly be expensed;
- The cost of inhouse software should not include overhead.

Proposal: Delete the present prohibition and adopt the following rules:

A computer software system (other than (i) operating system software, (ii) software produced by an R&D effort and (iii) software purchased or produced for R&D) costing more than $100,000 shall be carried as a non-admitted asset and amortized over the estimated useful life of the software or five years, if less. The annual reductions should be charged to expense as appropriate. In computing the cost of in-house software, only direct costs are to be included. The cost of modifications made to purchased software prior to its initial installation may be included as part of the non-admitted asset. □

ACTEX STUDY MANUALS

ACTEX Study Manuals will be available for all May, 1987 exams except Part 10. New editions for Associate Courses 110, 130 and 160 and for Part 6. Particulars in your study note package, or from the Actuarial Bookstore, PO Box 318, Abington CT 06230. Tel. (203) 974-3540.

ACTUARIAL PROFILE SURVEY

The responses to the Committee on Planning's summer survey have been tabulated. Results were available at the Annual Meeting. Call or write the Society office to obtain a copy.

1986 ACTUARIAL SCHOLARSHIPS

The Subcommittee on Minority Recruiting is pleased to announce th recipients of the scholarships awarded in 1986:

Carroll, Deanna
Drake

Cheng, Emily
University of New York

Engel, Wendy Jan
Georgia State

Grant, Dennis
Temple

Greene, Karen
University of Connecticut

Headlam, Michele
University of Wisconsin

Jones, Marlene
Georgia State

Joseph, Samuel
University of Connecticut

Lew, Vee Ming
University of California

Mungin, Melvin
University of Pennsylvania

Oglo, Katherine
Georgia State

Powell, Victor
Howard

Shepard-El, Kelli
Temple

Sheppard, Lynn
Howard

Traylor, Yolanda
Princeton

Wiese, Don
Carleton

Since 1977, the Society of Actuaries and the Casualty Actuarial Society have sponsored a Minority Recruiting Program to encourage qualified minority students to seek careers within the actuarial profession. The Minority Recruiting Program receives its financial support from contributions by actuaries and employers of actuaries throughout the United States. In addition to awards from the general scholarship fund, the program offers scholarships from three separate funds that have been established by individual companies. The Equitable Life Assurance Society has established

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