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REPLACEMENT

A long-continuing problem to which life insurance actuaries have given too little attention is that of the replacement of one life insurance policy by another. A recent LIMRA release, quoting some of the remarks at a LIMRA Agency Management Conference, suggests that the industry has been rife with replacements for more than half a decade, and that new products have become vehicles for replacement rather than generators of legitimate new sales.

From the individual product actuary's viewpoint, the replacement matter is indeed difficult. He or she cannot avoid the widely held (and probably valid) presumption that a life-policy replacement is *usually* against the best interests of the policyholder; but demonstration of this phenomenon is indeed difficult. That the presumption is a by-product of the long-established system by which life insurance agents are compensated makes the matter no easier. Most replacements result in another first-year commission; insurance companies pass on expenses, including commissions, to policyholders; ergo, all other things being equal, the gain to the replacing agent is at the expense of the insurance buyer.

Replacements are of at least two types, one under better control than the other. Where an agent is suggesting "within the company" replacement, conversion and commission practices to prevent policyholder harm can be devised. Most companies have developed procedures that adequately handle these not-so-very-common situations.

Much more troublesome is the replacement of an existing policy in one company by an agent or broker representing another, based on some argument that hides the commission matter. The replacing company may or may not encourage the replacement effort, but the fact remains that replacement efforts are often successful, and that raiding of business is very common. Replacement of cash value insurance by term or its equivalent has long been an approach of some segment of the industry, though replacement by universal life or its variants may account for more of what is going on today.

Much of the difficulty surrounding this problem arises from the exceptions to the general rule. Not *all* replacements are evil; there are policies that in the owner's interests *should* be replaced. A new policy may be *less* expensive, even though a new commission must be absorbed, if the old policy is otherwise high cost. The old policy may no longer fit the policyholder's circumstances, and may not be sufficiently flexible to be changed. The original company (or agent) may be providing such poor service that the policyowner may be *willing* to pay more. One of the technical problems, then, is to devise some approach to the separation of the "good" replacements from the "bad". This one will not be easy.

Actuaries are thought by many to be the problem solvers of the insurance industry. Although the replacement problem is not one to which typical actuarial techniques can be readily applied, it is an *important* problem, and certainly within the general scope of the actuary's expertise. We suggest that actuaries, and not only supervisory actuaries, take an active role. If home office product development actuaries don't apply themselves to this matter, who will? *C.L.T.*

WORKDAY PROBLEM

By Bob Likins

Your Agency Department has recently learned about a new hot selling product that the ABC Life Insurance Company has introduced to its field force. You have been asked, as product development actuary, to develop a similar, competitive product.

Later you report with a package of preliminary pricing results and product descriptive information. Your product is competitive. Your sales people want to move ahead with the product's development.

You ask how much of the new product *will* be sold. The marketing staff would like to know how much they *need* to sell in order to justify the development time and cost. They indicate that sales people are better able to respond to a sales target.

The problem: Who should answer the question first, marketing's sales estimate or your sales requirement to justify the effort?

Here's one response; what do you think?

These two efforts by actuarial and marketing should be done independently.

Implicitly or explicitly the actuary must build development costs into pricing. Therefore, given a period of time for amortizing development costs, the actuary can calculate the needed volume of sales that justifies the product's development. This assumes there aren't even more important uses for the development staff's time. Providing this information before the marketing staff has had a chance to independently review the saleability of the product could bias their sales estimate.

With a description of the product's pricing and features, the marketing staff can develop an estimate of additional sales (not cut-in sales). The estimate must be realistic, but even with the best efforts, it's a guess. □

DEATHS

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