TRANSACTIONS OF SOCIETY OF ACTUARIES
1950 VOL. 2 NO. 2

POLICY CHANGES

A. Have companies made any recent investigations of the costs of making changes in contracts, and how have these been affected by general increases in costs?

B. Has there been an increase in volume of policy changes in the post-war period and what steps are being taken to keep the volume to a minimum?

C. What methods are being employed when a request is received to change a premium-paying policy into a paid-up contract for the full face amount? How are the terms affected if part of the payment is to be derived from accumulated dividends?

MR. J. G. BEATTY said that his company has been trying to reduce the cost of policy changes through education among managers and agents. Their functional cost analysis shows that it costs about $20.00 to make a change where evidence of insurability and rewriting the policy is involved and this does not include the medical fee which is charged to the insured. A simple change, involving only a request form, costs about $3.00, and other types of changes run from $3.00 to $20.00, according to the degree of complexity. His company is taking far more short cuts than they formerly did because their experience indicates that they get into more trouble with what is included in their policies than from what is left out.

Many more changes than formerly are made by endorsement instead of rewriting the policy, and the endorsements are as brief as possible. They do not bother about slight inconsistencies in various provisions as a result of the change and are using more printed riders for such benefits as additions of disability, double indemnity and family income benefits and are relying on the request form in more cases, including the reduction to paid-up insurance.

Whether as a result of education or economic conditions, the number of policy changes has not increased since the war, although the cost has gone up about 50%. Since they have adopted many short cuts, this means that the increase in cost per work unit is even greater. The difficulty with changes is that they do not lend themselves much to mechanization and streamlining. The increasing complexity of plans of insurance is another factor which makes it difficult to streamline the operation.

Mr. Beatty felt that the cost of making changes is out of line with their value to the company and that, although they cannot be eliminated, we should make every effort to keep them to a minimum.

In converting policies to paid-up insurance for the full face amount, they charge the AM$^{(5)}$ $2\frac{1}{2}\%$ single premium on the difference between the sum assured and the reduced paid-up value, loaded $6\frac{1}{2}\%$. They do not have the problem of accumulated dividends applied to make the policy paid up, except on certain old issues.

MR. J. L. STEARNS said that for 37 years the New England Mutual has included a change privilege, guaranteeing the right to convert the policy by payment of the difference in reserves. Their problem, therefore, is not the basis of making the change but the simplification of methods to cut down the cost. He said there are always possible improvements in office routine. For instance, they reduce ratings on substandard policies and make changes of premium date without a signature and without calling in the policy for endorsement. Forms for indicating other changes desired are supplied to the agencies.

The number of changes computed in 1941 was 38 per thousand policies in force; the number in 1944 was 25 and in 1949 30 per thousand policies in force.

For the last 19 years, their change clause has guaranteed the privilege of conversion only to premium-paying forms, and they have restricted changes to paid-up insurance to the amount being currently sold on the single premium basis. On changes 5 or more years after issue, the basis is difference in reserves, and during the first 5 years a loading is charged consistent with the loading in a single premium policy. There is no restriction on size of policy made paid up by dividend accumulations, if the dividends are sufficient to cover the difference in reserves.

MR. J. W. CLARKE said that in The Travelers they have reduced the cost of making changes by simplification and transfer of the work. Changes are handled by a subsidiary of the Life Underwriting rather than the Life Actuarial department. Change rules and practices are established by cooperation between these two departments. This cooperation has been effective to reduce changes referred to the Life Actuarial department from about 55% of the total in 1941 to about 20% of the total in 1949. Most of those referred in 1949 are for special figures rather than a complete calculation.

Although the total number of changes handled by The Travelers has in fact dropped from 3,561 in 1941 to 2,173 in 1949, the company has made no effort to reduce the number of changes handled. They feel the making of changes and change quotations is a part of the service owed to policyholders.

In making changes to paid-up whole life they purchase the difference between the reduced paid-up value in the contract and the face amount at

97% of current manual single premium rates. Values in the changed contract are based on the reserve basis under the original contract. The agent receives the difference between commissions paid on the original contract and present scale commissions on the single premium manual rate last in effect on policies issued under the reserve basis of the original contract. If the change is made in the first year, the charge is the difference in premiums with interest. On endowment policies they use the same method but at 98% of current single premium rates.

MR. J. E. LOWTHER indicated that the Metropolitan prepares functional costs each year, and the 1949 report shows that Home Office costs for changes in plans or amounts or class of insurance were about $20.00 per policy and additional expenses incurred in the agencies, exclusive of commissions and taxes, bring the figure to $21.50. These figures exclude the cost of preparing change quotations not accepted. Costs in 1949 are about 20% higher than in 1946, but the volume of changes has decreased. No special efforts have been made to keep the volume down.

In changing premium-paying policies to paid-up insurance for the full face amount, his company will not make changes on Endowments where the date of maturity is less than five years from the date of change. In other cases, the cost is the difference in cash values loaded 5%.

They will not change to a single premium policy any contract issued prior to 1935, these policies being on a $3\frac{1}{2}\%$ basis. They will not make changes to single premium Endowments where the policy matures less than 20 years from original date. The cost of changes to single premium policies is the greater of (a) difference of reserves, including surrender dividends, loaded 5%, and (b) difference in premiums less dividends accumulated at 5% simple interest, plus any excess commission on the original policy.

The terms of their policies do not feature the dividend accumulation option which permits dividends to be applied to shorten the premium-paying period.

MR. C. B. SPURGEON stated that some years ago the Mutual Life of Canada estimated the average cost of policy changes, including all calculations and changes, at $10.

To keep costs down they have adopted the practice of issuing riders for additional benefits without asking for the policy, and of endorsing the policy for most changes involving reduction of benefits, such as change to reduced paid-up, reduction in face amount or cancellation of provisions—a new policy being issued only in certain cases such as change in plan.

Their usual charge for changing an Ordinary Life policy to paid-up for the full face amount is the difference in reserves, less dividend accumulations, divided by .9. For Limited Life or Endowment policies they quote only the discounted premiums.

MR. S. L. CHAMBERS confined his remarks to section C.

Although these requests usually involve participating policies, they recently made some test calculations on the basis of nonparticipating policies in order to avoid the complication of dividends. They used three methods of approach: (1) difference in reserves between the existing policy and the paid-up policy for the face amount loaded 10%; (2) the net single premium for the difference between the face amount and the reduced paid-up value loaded 5%; (3) the commutation of the gross premiums less a small deduction for saving of renewal expenses.

On grounds of equity as compared with a policyholder who makes a partial surrender by taking a reduced paid-up policy, the charge should not be greater than (2), which may be regarded as a maximum. It may be argued that the change should not be granted on a more favorable basis than to the policyholder who maintains his original contract and hence (3) may be considered as a minimum provided it is less than the maximum charge under (2). Tests show that (1) and (2) are closely in line except on some old Endowment policies where the paid-up values were on the proportionate basis. The commutation basis (3) corresponded fairly closely on Endowments and on life plans at old ages. For young entry ages on the life plan, however, the first two methods showed a cost as low as 78% of the commuted premium.