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Before the snake bites

Study and conference will explore annuity risks

by Irwin Vanderhoof

Although the greatest risk might not be found in the largest block of business, that may be the best place to start to look. This is one way to characterize the approach of a new study, "Risk of Accumulation Products," to be sponsored by The Actuarial Foundation (formerly the SOA Foundation).

Traditionally, life insurance companies have depended on individual whole life insurance policies for their growth in assets. This has changed in recent years. Now, annuities — particularly individual annuities — have become the largest part of new individual premiums. Companies have responded by issuing a plethora of imaginative products. These are often founded on a variety of recently developed financial instruments, such as derivatives.

However, while these new, complex products are already on the market, the study of such products' risks has not kept pace. One way to discover the problems is to wait for companies to get into trouble. However, we, as actuaries, have a responsibility to count our snakes before they hatch and recognize the problems before they bite our employers.



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In light of the dramatic need to correct this situation and with substantial financial support from the Nationwide Insurance Companies, the Foundation will sponsor a study of the risks of these new products and the new financial instruments underlying them. The study will culminate in a scientific conference in New York in December 1998.

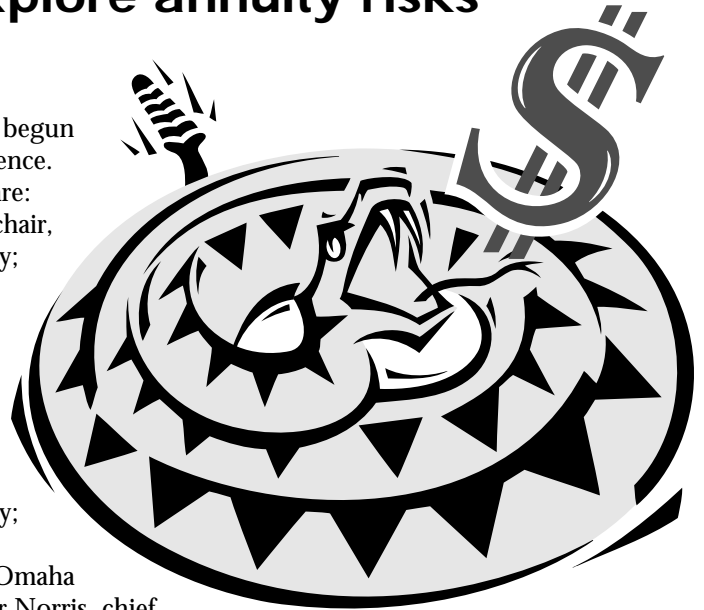
A committee has begun planning the conference. On the committee are: Irwin Vanderhoof, chair, New York University; Dennis Carr, ARM Financial Group Inc.; Steven Craighead, Nationwide Life Insurance Co.; Martin Gruber, New York University; Steven Miller, Mutual/United of Omaha Insurance Co.; Peter Norris, chief investment officer, Equitable Life Assurance Society; and Tim Pfeifer, Milliman & Robertson.

The conference will be built around five topics:

- Catastrophic market risks and market failures, such as the failure of portfolio insurance in 1987.
- The effect of distribution channels on policyholder behavior and persistence.
- Long-time liabilities, options, and guarantees. The last includes interest rate guarantees that extend into the distant future.
- Transfer risk models
- Practical aspects of managing annuity blocks of business

Each topic is expected to have at least one invited paper to lead the discussion.

One step toward the conference already has been taken. Nino Boezio, active in finance-related committees of the SOA and the Canadian Institute of Actuaries, has been commissioned to provide an annotated bibliography, along with copies of the pertinent papers, of existing material on the



behavior of individuals in response to changes in the economic environment.

There should be some relationship between mortgagors' decisions to refinance and annuitants' decisions to surrender their contracts. Boezio's compilation of data on this aspect of behavioral economics should have value for actuaries and other professionals interested in finance. This information is expected to start to become available in March 1998. Boezio will continue to compile and release data during the year to individuals preparing papers for the conference.

Call for papers

A detailed call for papers will be issued early in 1998. Anyone interested in developing a paper or presentation should contact Joseph Abel, Ph.D., the Foundation's director of marketing and development, to register for the mailing list for additional information. He can be reached at the Society office (phone: 847/706-3557; fax: 847/706-3599; e-mail: jabel@soa.org).