

Book Review

A Comprehensive Guide to Measuring and Managing Life Insurance Company Expenses

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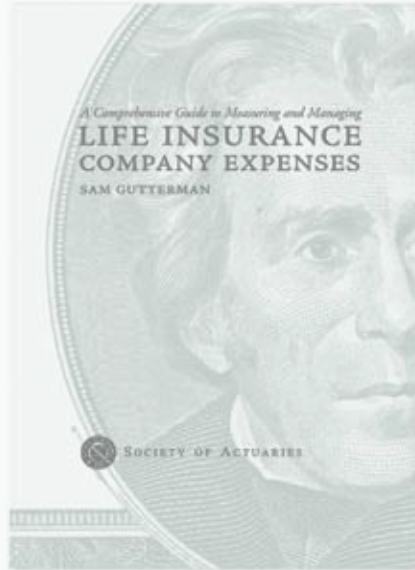
Although expense management is a key controllable component of life insurance-company profitability, until now the subject has been largely ignored in actuarial literature. Therefore, this landmark publication fills an important void for actuaries and other professionals involved in designing and administering insurance products.

The 450-plus page textbook was published by the Society of Actuaries in 2007. It had its beginnings with “Expense and Pricing,” which was written in 1997 by Sam Gutterman in response to a call for papers. Over the next decade the original paper was expanded sixfold in size with the assistance of dedicated volunteer editors including Mike Eckman, FSA; Tim Harris, FSA; Tom Herget, FSA; Paul Strong, FSA; and Steve Sorrentino, FSA.

Although designed primarily as a reference book, the first five chapters provide a valuable overview for readers who are not familiar with the subject or who want to brush up on their knowledge.

Expense management and analysis play a role in a variety of life insurance company functions including measuring performance, establishing benchmarks, communicating financial results, estimating future costs and making business decisions.

There is no best way to derive expense assumptions, allocations or projections that apply in every circumstance. However, there may be an optimal approach to implement a particular business strategy. Thus, the



author describes the pros and cons of various techniques.

The business of insurance consists of developing products and services to meet customer and policyholder needs, creating an infrastructure to attract clients, and establishing processes to service these products. The long-range and intangible nature of these offerings makes the insurance business unique.

Every entity has a strategic plan, even if it doesn't realize it. The plan must be executed through tactical and operational planning and quantified by a budget. A recent study indicates that the ultimate goal of recouping all expenses is achieved by only 42 percent to 67 percent of insurance companies. The others recover less than 60 percent of their total expenses.

Pricing methodologies vary by company.

- Cost-based pricing is intended to recover expected costs plus a profit. Conditions may result in cost overruns, requiring active expense management.
- Market-based pricing sets the price on the basis of market conditions. Active expense management then determines the level of cost control that must be utilized.
- External constraints such as prices dictated by regulators may force an insurer to decide whether or not to participate in the market. In other cases rules may limit the use of certain expense categories in setting rates. These situations require accurate and timely expense information.

The insurance industry is at the forefront of technological development. New technology is always introduced with the promise that costs will be reduced. As a practical matter, anticipated savings are often not realized, because the new equipment is used to perform additional tasks that are not necessary.

The book covers a broad spectrum of the concepts involved in analyzing and controlling insurance company expenses. It is enhanced by a four-page list of acronyms, a glossary of pertinent terms and an exhaustive bibliography. The readable text is supplemented by informative graphs and tables.

A Comprehensive Guide to Measuring and Managing Insurance Company Expenses is a valuable resource for everyone involved in this important area. **A**