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DIGEST OF DISCUSSION OF SUBJECTS OF SPECIAL INTEREST

ORDINARY INSURANCE

Underwriting

A. To what extent has "guaranteed issue" underwriting been extended to mass selling plans (such as salary savings) other than pension and profit-sharing plans? What safeguards are necessary and what adjustments are made in commissions and dividends? Are higher costs for standard risks acceptable to the buyers?

B. To what extent, if any, is selection against the insurance company at the time the insured retires greater under the various types of business insurance than under personal insurance? How can such antiselection on business insurance be guarded against or provided for?

MR. KARL M. DAVIES outlined the Equitable's recent extension of its guaranteed issue underwriting practices. He stated that the extent to which guaranteed issue underwriting practices were broadened is potentially rather large and that such underwriting practices have not been limited to any particular type of mass selling. The new program makes available any of the regular permanent plans of insurance, but the extended term nonforfeiture option is not available with guaranteed issue.

In considering a group, adherence to the following fundamental principles derived from group insurance is required: (1) there must be an employer-employee relationship or some other natural grouping of a similar nature, (2) the employer must make a substantial contribution to the cost of the insurance, (3) there must be a clear definition of the classes of eligible employees based on conditions of employment which precludes individual choice, and (4) there must be a formula exactly determining the amount of insurance applicable to each employee. In addition, the actively-at-work requirement and the usual guaranteed issue underwriting rules apply.

Preliminary inquiries on the new basis involved deferred compensation plans, a kind of stock redemption plan, a mortgage redemption plan, a salary savings plan providing supplementary insurance on the Life Paid-up at 65 plan to employees covered by a group term plan, and other types of salary savings plans such as those involving the employees of a trucking concern for a flat amount with the employer paying a large part of the cost.

Mr. Davies stated that the biggest difficulty encountered is that of clearly determining the eligibility and amount rules in terms of classes of employees. There is also concern over how these rules will be followed and revised in future years as new employees become eligible. Regular underwriting may be required in future years as additional lives join the original group.

In studying this extension of guaranteed issue underwriting, special mortality assumptions based on, but slightly higher than, the Equitable's 1950–1955 ultimate experience were used. The policies are placed in a separate dividend class under which it is expected that lower dividends, constant by duration but varying with issue age, will be paid. The first year commissions on whole life plans are reduced by 10% of the premium. For the high cash value policy, no reduction is made in the first year commission but renewal commissions are reduced from 10% to 8%. On other permanent plans, the first year commission is reduced by 20% of the regular first year commission.

It is hoped that the requirement of a substantial contribution by the employer will always make the plan attractive to the individual concerned. Employers seem to feel that the absence of individual underwriting is worth some extra cost. The Equitable is insisting that the agent or agency manager submit to the home office a letter to the effect that the dividend and cost aspects of the plan have been fully explained and that cost illustrations have taken into account the guaranteed issue dividend reductions.

In connection with section B, Mr. Davies described the conversion option contained in their special minimum amount plan designed primarily for business insurance programs. If the policy is surrendered for its cash value on any premium due date between age 60 and age 70, the conversion option permits the continuance, without evidence of insurability, of whole life coverage for a reduced face amount equal to the difference between the original face amount and the cash value paid. Since it can be shown that continuing the original policy subject to a loan is substantially more expensive than exercising the conversion option, it is expected that there will be less antiselection under the conversion option than if the option did not exist and the original policy were continued with a loan.

The premium rate for the continuation policy is specified in the original policy and is actually the attained age rate for the Equitable's Adjustable Whole Life policy. Commissions at the renewal rate only are paid under the continuation policy. Cash values are equal to the full reserve and dividends are expected to recognize that exercise of the option does not entail the usual acquisition costs of a new issue.

MR. DATON GILBERT reported that, to date, guaranteed issue underwriting in the Connecticut Mutual has been restricted to qualified pension trusts and to qualified profit-sharing trusts involving automatic application for insurance. Although his company is continuing to study the possibility of broader use of the guaranteed issue technique, it has not yet found an attractive area for such extension.

He suggested that satisfactory underwriting of such business requires that the employer pay all, or a substantial part, of the cost. This automatically rules out typical salary savings business where the problems of maintaining a sufficiently high degree of participation for satisfactory amounts would appear to be serious. When it comes to key man plans, the possibilities appear somewhat more encouraging. However, there is a tendency for the employer to hand pick participants, the amounts of insurance are typically substantial in relation to the number of lives involved, and the type of participant is apt to be alert to the possibility of antiselection upon termination of the plan. Mr. Gilbert concluded that use of guaranteed issue in these other fields is less attractive than with qualified employee trust business because of the probable higher mortality. In any event, any such extension might require different policy forms, rates and dividends from those used with qualified trusts.

MR. ALTON P. MORTON defined guaranteed issue as the issue of individual policies where a satisfactory mortality result depends on the application of one or more group underwriting techniques. These techniques include an actively-at-work requirement, a formula limiting everybody to a flat or scale amount, inspection reports and other preissue information on the employer and on individual employees, and a minimum percentage participation requirement. The period of initial eligibility for guaranteed issue closes with the writing of the original group; thereafter, new applicants are accepted only if eligible by normal underwriting standards.

He remarked that the practical limitations on guaranteed issue underwriting seem to be self-evident. Where extra mortality cannot be offset by expense savings, some employer money is necessary. Otherwise those applicants who are standard by ordinary underwriting standards would have to pay a greater cost under guaranteed issue than for regularly issued insurance.

Test calculations, using model office techniques, led to the broad conclusions that on realistic assumptions no employee group would show extra mortality which could be offset by a combination of savings in underwriting expense and any practical commission reductions and that a special dividend class would be needed in which a higher net cost would necessarily be passed on to all members of the guaranteed issue class.

In connection with section B, Mr. Morton said that selection against the insurance company at the time the insured retires is only a special, perhaps somewhat aggravated, example of the antiselection which applies to all terminations. Whether business or personal insurance, it is only proper to assume that the lapse rate is lower among lives who have become substandard than among lives who continue in good health. The tendency for lapse rates to be lower for people in poor health must be even more marked with the larger amounts of insurance and with third party owners, particularly where a business firm is the owner. Such antiselection in business insurance ought to be regarded as a normal hazard of the life insurance business. He concluded by pointing out that the large amount studies published by the Society suggest some slight antiselection on lapse.

MR. ANDREW C. WEBSTER referred to Mr. Morton's comment that the extra costs had to be met somehow and he wondered why anybody would buy a second rate product when he could buy a first rate product through normal underwriting procedures. He suggested that, if we are going to save money on underwriting techniques, it might be a good idea to review nonmedical limits, since nonmedical business was being sold, whereas, from what he has heard, not much guaranteed issue business was being sold.

MR. ERNEST J. MOORHEAD expressed the wish that those companies which have written guaranteed issue cases on professional and trade association members would contribute to a discussion of this nature. He stated that his company's only case, issued as an exception, involved some twenty policies issued to the members of a county lawyers group. It was found that within one year ten of the twenty policies had terminated.

He suggested that there are two different situations which should not be confused. One is the situation in which an automatic issue series is available and it is suggested that it be used as a vehicle for plans other than qualified plans. The other situation is one in which a special series of policies is developed, perhaps in the Group rather than the Ordinary department, for these other professional types or types outside the pension, profit-sharing, and employer contribution series.

MR. EDWARD A. LEW referred to the Metropolitan's study several years ago of their experience with respect to business insurance cases being converted or renewed at ages past 60 under their renewable convertible term policy. He stated that it was difficult to say whether there was more selection on personal insurance than on business insurance. It appeared to him, however, that corporations were frequently paying the large premiums required past age 60 and that they were in better financial position to do so than were individuals. The fact that there is antiselection on business insurance at the retirement ages needs no further documentation.

Mr. Lew said that he did not know how this antiselection can be completely guarded against. He suggested that some of it can be guarded against in the initial selection and that some of it can be handled by making very ample provision for the extra mortality.

MR. EARL M. MACRAE agreed that in the case of key man insurance, it would be reasonable to expect somewhat greater selection against the company than in the case of personal insurance at the time when the key man retires. Where stock purchase insurance is involved, he felt that antiselection is not increased because of retirement, since the reason for purchasing insurance continues to exist. He concluded by saying that the only practical defense we have against any antiselection in such cases is the employment of sound underwriting, especially in keeping the amount of insurance commensurate with clearly demonstrable insurance needs.