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EMPLOYEE BENEFIT PLANS

Group Life Insurance Maximum Limits

A. What are the actuarial considerations in determining the maximum amount of group life insurance that can be safely issued to an individual? What statistical data have been developed in this connection?

B. What practical arrangements are available to meet the demand for low cost death benefits in large amounts for employees?

MR. HAROLD F. HARRIGAN opened the discussion by stating that the basic consideration existing with regard to determining the maximum amount of group life insurance that can be safely issued to an individual is whether the proposed plan can be provided on a sound financial basis, both for the individual group and for the insurance company.

Chance fluctuation and antiselection on the part of those controlling the purchase of insurance may affect the financial experience adversely. In underwriting higher maximum amounts of life insurance, all features of the group involved must be considered: nature of company's business, volume of insurance, number of employees, schedule of insurance, distribution of employees by insurance classes, reduction formula at older ages and disability provision. Also important is the employer's attitude and whether he is likely to leave you at a time when experience is unfavorable.

Metropolitan uses both reserve and pooling methods to handle excess life maximums. The reserve method is generally used for those cases where the reserve can be readily established or where the policyholder requests some unusual features in his plan which cannot be readily adapted to the pooling arrangement. A properly balanced schedule is always a prerequisite.

For medium sized cases or where the policyholder wants to spread the effects of a large claim, the Metropolitan has, for some years, used a medical risk pooling arrangement in which employees insured for amounts larger than would normally be available are included. Claims among the lives in the pool are charged back to the groups in the pool on a pro-rata basis, depending upon their expected claims. Medical examinations of the employees in the pool are primarily for the purpose of evaluating the total risk and determining the expected claims. The right is reserved by the Metropolitan to limit the insurance on an employee who is so substandard as to possibly affect the pool to an undue extent. Groups with an unusual proportion of substandard lives would not be considered for the pooling arrangement. In actual experience this rejection right has not had to be exercised to any substantial degree.

The Metropolitan also utilizes another form of pooling arrangement which does not require a medical examination. In lieu of medical examinations, tighter "actively at work" provisions are used. Under this type of arrangement, a reduction formula providing a reduction to no more than 50% starting at age 65 and an extended death disability provision are required. To date experience under this arrangement has been satisfactory.

MR. ALDEN W. BROSSEAU stated that there were two actuarial considerations affecting the safety of large amounts of group life insurance—antiselection and claim fluctuations.

To combat antiselection, the group underwriter employs various types of underwriting controls—rigorous actively at work provisions, barring definitions of eligible classes that exclude lower paid employees, requiring a minimum number of employees in the class eligible for the maximum amount of insurance, varying the maximum amount according to the employer's contributions, requiring schedules based on earnings rather than position. Other controls operate by permitting antiselection and then attempting to counter it by obtaining individual evidence of insurability. There are serious questions as to the propriety of individual underwriting controls except where the spread of risk is inadequate to permit schedules of insurance that would be quite satisfactory on a no evidence basis if the group were larger. There is no justification for it where the insurance on the bulk of the group is merely incidental to large amounts for the executives.

New York Life is opposed to seriously unbalanced schedules providing amounts for executives out of line proportionately with those for rank and file and is especially opposed to medical examinations in order to make such schedules feasible. Group insurance is properly designed for the group, not for the individual. This concept requires that amounts of insurance bear a reasonably consistent relationship to income for all members of the group.

With regard to the problem of claim fluctuations, various underwriting rules may be used. For example, the maximum limit may depend on the size of the group (number of lives, amount of premium or volume of insurance). Another approach is to limit the maximum to some multiple of the average amount on the employees in the lower classes. Another is to relate it to the volume on the top 25 employees.

Problems of persistency combined with the competitive facts of life may make it difficult to employ extra risk charges, special reserves and other similar devices, since they tend to increase the average retention. A solution is to increase pooling. This approach minimizes the possibility of deficits and improves persistency, but requires more careful initial underwriting to prevent antiselection by executives from draining the pool.

MR. ERWIN A. RODE agreed with the basic principles outlined by the previous speakers and indicated that the Prudential utilizes controls and pooling in much the same manner as Metropolitan and New York Life. Mr. Rode described an approach used by the Prudential by which normal actively at work requirements are applied up to a certain level of amounts, tight actively at work for the next level and finally medical evidence of insurability for the top level. A balanced plan is always insisted upon.

So far, the experience under pooled amounts has been quite favorable. However, the exposure is of short duration and it is expected that the mortality level will ultimately reach a level significantly above that of the over-all experience.

MR. LINCOLN C. COCHEU said that his Company, the Continental Life, had studied this whole problem and had concluded that maximum amount rules now in use by various companies did not follow from actuarial considerations. Mr. Cocheu indicated that there was a definite relationship between maximum amount limits and nonproportional reinsurance and that his company had entered into a nonproportional reinsurance agreement with another company about 5 years ago.