TRANSACTIONS OF SOCIETY OF ACTUARIES
1960 VOL. 12 NO. 34

Annuities and Settlement Options

A. Do current immediate annuity rates reflect present conditions as to mortality, interest, and expense? To what extent do statutory reserves that exceed gross premiums less expenses represent a serious problem?

B. What is being done in the way of using generation type annuity rates for settlement options? What problems are involved? Should and can these options be made consistent with the maturity cash options in endowment annuity policies?

MR. EDWARD A. LEW reported that the Metropolitan's new immediate annuity rates are based on the Annuity Table for 1959, that is, the a–1949 Table Projected 10 Years, with no projection from 1959 on. As a test of this mortality basis, they recomputed the mortality ratios in the intercompany 1953–1958 experience for refund and nonrefund annuities combined, using the Annuity Table for 1959 as the standard of expected deaths. This produced over-all mortality ratios slightly in excess of 110% for males and slightly below 110% for females. An analysis of the mortality experience by age groups at issue showed the margin to be 20% to 35% in the sixties, 15% to 20% in the seventies, 5% to 10% in the eighties, and a very thin experience in the nineties. He concluded that for immediate annuity rates at ages 60 and over, there is at the present time in the Annuity Table for 1959 a reasonable margin for future improvements in mortality.

Mr. Lew noted, however, that they found it necessary when using the Annuity Table for 1959 to make a special provision for select mortality, because at the advanced ages select mortality lasts a great deal longer than the one or two years originally assumed; this special provision increases with advancing age at issue over 60.

MR. N. DOUGLAS CAMPBELL, commenting on section B, illustrated that relatively few companies are currently using up-to-date mortality standards and very few are using generation type optional settlement tables.

He stated that any averaging approach to settlement options must lead to inequities amongst policyholders and also to fairly tedious and approximate devices to transfer overcharges from one group of policyholders to the other group where there are undercharges. A generation type table takes care of these matters automatically and for this reason is to be commended.

He stated that an important problem is the general acceptance of generation optional settlements by the field force and the clients. However, he expects that if there were a general movement towards a generation approach it would soon find acceptance, because it is fundamentally sound and in accordance with the facts as developed over the past years. He felt that many of the arguments of a public relations nature that have been recently presented in favor of the 1958 CSO Mortality Table might also be advanced to support the need for a new mortality table for optional settlements. Mr. Campbell emphasized the need for such a new table by pointing out that a greater proportion of sales than ever before involves a presentation of conversion of policy proceeds into income and that there is every indication that the amount of insurance proceeds going into this type of agreement will increase as time goes by. He felt that those companies which have introduced generation type optional settlements are on the right track and he expressed the hope that it will not be long before many of the companies follow this practice.

MR. JOHN J. MARCUS reported that Prudential, after lengthy study, decided not to use variation by generation in their recently announced settlement option and endowment annuity rates. He cited the following as reasons for their decision: Under a year-of-entry system rates continually deteriorate for a particular beneficiary. Under a year-of-birth system inequities between different payees may arise because of the age groupings, while, on the other hand, refinements in age groupings increase administrative complexity. Introduction of generation mortality may make advisable other equally important variations such as by payee and nonpayee election. Another important reason was the endowment annuity policy problem.

With regard to the endowment annuity, Mr. Marcus felt very strongly that confusion would prevail if a monthly income other than that provided on the face could be obtained on a guaranteed basis by placing the cash under a settlement option. He said that a possible solution would be to drop the endowment annuity series and provide that premiums could be continued under an n-year endowment so as to build up the cash value at a later duration at which time it would be applied to purchase a life annuity. They rejected this alternative because of the popularity of the endowment annuity policies and the possible agency problems involved in the sale of the alternative policy. Before reaching a decision they explored the ratebook and other administrative problems of using generation mortality. This led them to reject a system requiring premium rate changes for at least some issue ages each year in order to provide for higher maturity values. They also rejected a system under which the guaranteed monthly life income would vary with the issue age.

MR. EDWARD RUSE reported that the Confederation Life Association adopted generation settlement options two years ago and have experienced no trouble, in either the United States or Canada, with technical difficulties in the field and with acceptance by the field. In introducing the new settlement options their careful planning included agency meetings on the subject. Mr. Ruse said that they had to abandon their endowment annuity policies and that these were replaced by double endowments. This replacement has also been accepted by the field force.

MR. DONALD R. ANDERSON stated that his firm has recommended the use of the Progressive Annuity Table for optional settlements to a client just starting to write business in Canada, and it appears to be satisfactory. For lives born in 1900–1919 inclusive, the table is used without a rating, and for each succeeding 20 year generation the table is rated down one year. The 20 year generation was used rather than the 25 year generation suggested by the Fassel-Noback paper, so as to provide an additional margin of safety for future improvements in mortality. The resulting settlement option incomes on the 10 and 20 year guarantee basis matched the incomes on the basis of the Standard Annuity Table rated down 2 years with $2\frac{1}{2}\%$ interest over a considerable range of ages for settlements in 1960 on this basis.