



SOCIETY OF ACTUARIES

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Ed. Note: Several Society members testified in a recent lawsuit in which 14 stock life companies and two field men's groups sought to prevent Wisconsin's Insurance Commissioner from requiring that buyers be given (1) a preliminary policy summary that displays the policy's Surrender Cost Index (SCI) but not its Net Payment Cost Index (NPCI) nor its Equivalent Level Annual Dividend (ELAD), and (2) a buyer's guide that describes these figures in a manner objectionable to these plaintiffs. We invited those actuaries to send along concise statements. The letter (P) or (D) denotes a speaker for the Plaintiffs or for the Defendant. The Plaintiffs won the case; the Defendant plans to appeal.

By Bradford S. Gile, (D). (These views do not necessarily reflect the opinions or positions of Mr. Gile's employer, the Wisconsin Commissioner.) I will not argue here about the usefulness of NPCI and ELAD but will discuss cost comparisons between participating and non-participating policies. I suspect that if such comparisons were outlawed, the motivating need of plaintiffs to complain would largely evaporate.

In my opinion these are dissimilar forms, non-par itself now being of two dissimilar types—guaranteed cost and adjustable premium. It is true that par policies have non-guaranteed dividends; however, a major guarantee of those contracts, which is backed by statutory provisions in most states, is that dividends will be paid annually according to an equitable plan of surplus distribution. Such a guarantee is not, and cannot be, contained in a non-par policy, so the two forms differ greatly in major guarantees.

Nevertheless, many advocate comparing the two by showing (a) indexes that use 100% of illustrated dividends, and (b) indexes that use no dividends or, equivalently that show the part of the index generated by the illustrated dividends (ELAD). This system has the following fatal defects:

(1) In case (b), non-guaranteed elements are assigned zero credibility, including any contractual or statutory rights afforded by such values.

(2) Using illustrated dividends—case (a)—assigns 100% credibility to them, but although it may be correctly inferred

that a guaranteed cost index number is a faithful showing of maximum cost, it is incorrect to infer that the index using illustrated dividends is a faithful display of minimum cost.

(3) Neither assignment of 0% nor of 100% credibility to illustrated dividends is reasonable except when (i) the company involved faces the prospect of liquidation, or (ii) dividends paid never deviate from those illustrated (a practice common to a few stock companies). History has shown that 100% credibility is far more realistic than 0%.

In the absence of an index that fairly and realistically measures the credibility of non-guaranteed values (and policyholder rights thereto), any such comparison between otherwise similar par and non-par policies is highly susceptible to unfair and misleading statements. In my judgment, the danger of misrepresentation is so great that such comparison should be directly outlawed as an unfair trade practice.

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By Paul J. Overberg, (P). That entire trial should never have happened. It was the result of a failure of communication—a failure not just of the plaintiffs to communicate with Commissioner Susan Mitchell, but, more importantly, a failure of the insurance industry to communicate with the public.

This failure predates the May 1970 report of the Joint Special Committee on Life Insurance Costs—a report that concluded that the industry's then current system was fine, as long as an interest element was added to it.

But, let's return to yesteryear and ask ourselves, "Why did our critics between the 1930's and 1970 accuse the life companies of confiscating the cash value when the insured died?" Why? Because of the way we sold our policies.

Did the public understand that "net cost" measured the cost only if the policy was surrendered for its cash value? and "net payment" was the "cost" if the insured died? Adding interest to these calculations does not fill the communication void.

I am convinced that Commissioner Mitchell sincerely desires to help the buyer make a more informed decision when buying life insurance from among the over 1,000 different policies to choose from in her state. Somehow, the consu-

mer must be given helpful information—the only question is what that information should be.

I share the Commissioner's concern. As long as we give the buyers four indexes that have strange names and no real meaning, they will agree "the fewer the better." But if we explain what they mean, and perhaps give them more understandable names, buyers will understand cost disclosure and how to compare costs.

The court decision indicated that the public's ability to understand is greater than some of us believe. Let's make cost disclosure meaningful to the public. Then, and perhaps only then, can we make it understandable to our critics.

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By William M. Snell, (D). What is the purpose of a cost disclosure system? Is it to protect high cost companies, or to provide the consumer with useful information? I believe it is the latter.

The current NAIC Policy Summary obfuscates disclosure with six index numbers, in effect providing something for everyone. And most confusing of all is ELAD.

As one of those responsible for reaching a compromise between stock and mutual company interests to bring ELAD into the Model Regulation, I can speak of its value (or lack thereof) better than most actuaries. ELAD confuses agents, companies, regulators, and—worst of all—consumers. The time has come to end that four-year experiment, and drop ELAD. That would still leave four index numbers to be delivered with the policy.

Also, the time has come—it is past due—to adopt up-front disclosure. We must provide something before the prospect signs the application. Yet, the sales process must not be unduly hampered.

The best answer is to use just one index number—the 20-Year Interest-Adjusted Index. The name "Surrender Cost Index" is a misnomer. The policy doesn't have to be surrendered for the index to be valid, a fact pointed out in 1974 by our Society's own committee.

Disclosure should be simple, show the prospect whether the proposed policy falls into the category of low cost, average cost, or high cost, not whether the company is No. One or No. Two. Agents can battle that one out, as

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they have been doing for over 100 years.

This means that range tables are needed in the Buyer's Guide to give meaning to the index figures.

Originally the EPA rating for cars gave two figures. But consumers were confused by them. Now there is only one official EPA rating. Driving habits will result in better or worse performances, but as a comparative index it does an excellent job. We should learn from EPA that one figure is better than two, four, or six.

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By Ernest J. Moorhead, (D). When a buyer is confronted with either a favorable NPCI but an unfavorable SCI, or a favorable SCI but an unfavorable NPCI, what line of reasoning would he be wise to employ to reach a decision?

The plaintiffs support the idea that he should prefer the first of these if he intends to keep the policy until death—but should prefer the second if he plans eventually to surrender the policy.

But the vast majority of buyers begin with the expectation of keeping the policy until they die; what happens in practice is that, for one reason or another, they fail in about three cases out of four to do so. If somebody has evidence that the rate of voluntary termination is low among people who say they intend to keep paying premiums until death, let him produce it.

Agents in the main will pick the index that gives them the best chance of selling their policy. Buyers lack the experience that would enable them to decide which index ought most to sway them. And companies know very well that the road to profits is in designing policies whose surrender values are low and training agents to focus buyers' attention on the NPCI and to play down the importance of the SCI. □

Actucrostics

Two more of these accompany this issue. Solutions will appear next month.

C.G.G.

Examination Restructuring

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voted to these subjects alone.

Goal 6: To improve the treatment of nationally oriented material. In developing Canadian and U.S. readings, two concepts will be kept in mind: (1) to reap the educational advantages of pointing out the differences between the approaches in our two countries; (2) to separate the specific national details, particularly those of law and regulation.

Goal 7: To make the system more adaptable to the requirements of our various joint sponsors and administrators.

Impact

Major revision in organization and content of the Society's education and examination structure has an unavoidable disturbing effect. But it can be quite exciting, even inspiring, as one sees in the enthusiasm and dedication of the many volunteers who work on these changes. We hope most will agree with us that the benefits much more than justify the trouble they entail. We believe we can promise that the new flexibility will cause future changes to become more evolutionary than revolutionary.

Ed. Note: More particulars of these examination changes will be found in the Record, Vol. 5, No. 4 (Bal Harbour 1979), under the heading, "Current Professional Topics." □

ACTUARIES AND STATISTICIANS LISTEN TO EACH OTHER

by Robert J. Johansen

Ed. Note: Mr. Johansen is Liaison Representative to the American Statistical Association and the Committee of Presidents of Statistical Societies. He developed the plan described in this article.

Three well attended sessions on economic statistics at our annual meeting last October presented by the American Statistical Association begin an interchange between our professions that we hope will long continue. At the joint annual meeting of statistical societies next August, the Society of Actuaries will present two sessions, one on the build and blood pressure study, and the other on actuarial methodology. □

To Friendly Algebraists

With this issue is an enquiry from Messrs. Walter B. Lowrie and Arnold A. Dicke of the Part 3 Committee which we commend to your attention and prompt reply. We hope to be permitted to tell readers how many responses came in.

UNSHACKLING THE ACTUARIES

When Representative Bill Archer (R-Texas) and Prof. Wilbur J. Cohen, a long-time social insurance authority and member of the National Commission on Social Security, were interviewed for a *New York Times* article, "Social Security: Can Americans Afford It?", they made these comments about actuaries:

Mr. Archer: Well, a lot of our projections have been inaccurate. Many of the actuaries have been caused by political pressures to adopt projections that were not at all realistic. Even today they're still talking about the long-term at 4 percent inflation. We've got to do something to assure that the actuaries are given a free hand. . . .

Mr. Cohen: . . . Social Security ought to be made an independent corporation, with its own actuaries.

The article appeared on April 6. Our thanks to Ray M. Peterson for telling us about it. □

A number of papers I have heard at A.S.A. meetings are clearly of value to actuaries, and the same is true in reverse. But the sheer sizes of our bodies make full joint meetings out of the question; interchange of speakers on carefully chosen topics appears to be the right answer. The third step in this new cooperative arrangement will be a pair of concurrent sessions at our 1980 annual meeting—one on social indicators, the other on statistical methods and applications in follow-up studies.

Ideas Invited

Society members with ideas for topics they would like statisticians to present at our future meetings, or who would like to appear on a 1981 or later program of the statistical associations, are invited to write to Robert J. Johansen at his Year Book address. □