SOCIETY OF ACTUARIES

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THE LIFE ACTUARY

NEWSLETTER OF THE LIFE PRACTICE AREA

In This Issue: A Closer Look at Emerging Issues!

Letter from the Life Practice Area Chair

Looming Industry Tax Issues

by Edward L. Robbins

When we launched this newsletter for life practitioners, we believed that our charge was to put in your hands a semiannual package full of pertinent, helpful—and, above all, readable—articles. My topic today is highly pertinent, perhaps helpful and hopefully readable without becoming unduly technical. It can be thought of as a call to action for life actuaries to become more involved in tax issues. Although taxes affect all of us, wherever we work, my focus here is on taxation in the United States.

One of the chief criticisms about professional actuaries coming from employers and clients is that actuaries are too narrow in their focus, that they tend to find comfort in "closed-form solutions" rather than reaching out beyond the "closed form" to attempt to solve real business issues. Indeed, the basic education and examination system in which we have grown up has encouraged this type of thinking. That vestigial, closed-form-solution bias remains with most of us as many as 30 to 40 years later, and we need to get over it if we are to operate as practical professionals.

Life insurance company federal income taxes aren't simply a necessarily evil. They're typically a life insurance company's largest expense by a wide margin. Further, tax reserves constitute an area of great significance in the determination of life insurance company taxable income. Therefore, we as actuaries should be paying significant attention to tax reserve developments. More to the point, it is stating the obvious to say that, when it comes to fair life insurance company taxation, actuaries should take a lead role in shaping the tax reserve game.

Tax reserves are primarily an actuarial issue. There is no professional body other than the actuarial community that can deal with these complex calculations. Yet there appears to be a constituency that feels that tax reserves are an industry advocacy issue, not a professional actuarial issue. This distinction arises from how some have perceived the charges we have given to our two major professional associations, the Society of Actuaries and the American Academy of Actuaries. This perception is manifested in the apparent tendency of some to approach reserve methodology in a theoretically-based, pre-tax manner regardless of the tax consequences, in order not to be sullied by the appearance of being industry advocates. That said, the subject of tax reserves, while certainly an industry advocacy issue, is also very much a matter of equity and fairness. Put differently, if trends and developments occur such that tax reserve calculations result in taxable income that does not appropriately reflect economic income, or places significantly different tax burdens on similar taxpayers, the professional actuarial community needs to be heard.

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Life Practice Area of
the Society of Actuaries
475 N. Martingale Road • Suite 600
Schaumburg, IL 60173

Phone: (847) 706-3500 • Fax: (847) 706-3599 •
Web site: www.soa.org

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Glenn Pinkus, Desktop Publisher
(gpinkus@soa.org)
Phone: (847) 706-3548
Fax: (847) 706-3599

Narayan Shankar, Staff Liaison
(nshankar@soa.org)
Phone: (847) 706-3523
Fax: (847) 273-8523

Editor:
Steve Malerich
(smalerich@aegonusa.com)
Phone: (319) 398-8093
Fax: (319) 398-7949

Society of Actuaries

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Thinking about the Unthinkable

by Steve Malerich

A few months ago, I was approached by two members of the Life Practice Area Communications Oversight Group (COG) about taking on the responsibilities of editor for this newsletter. After a few phone calls, and a careful re-reading of the first issue and other materials from the COG, I (obviously) decided to accept the role.

One other thing came out of that effort, however. Having found interest among the group, I make it my focus in this issue.

An Emerging Issue

Among the long list of emerging issues presented last August, one strategic issue caught my attention: "Industry response to and product management under unthinkable economic scenarios that might materialize, such as very prolonged low interest rates and/or deflation."

After 20-some years of generally declining interest rates, why is it still "unthinkable" that interest rates might be low for a prolonged period? If we won't think seriously about the possibility, how can we hope to be prepared if it does happen?

Looking further out, suppose interest rates do remain low for several more years, will we become accustomed to such low interest rates, slowly adapt to them, and eventually come to expect them?

To actuaries today, that may be hard to imagine. But looking back, today's interest rates were considered high 35 years ago. Just as we read and talk about 35- or 40-year lows, the same rates were near 40- or 45-year highs when last seen. Looking back to that much earlier time, such rates capped a 40-year peak.

Many companies were ill-prepared for the rates that later made those highs seem low. Though most survived the highs around 1980, it was a painful time for many.

It also seems that many of today's companies were not prepared for today's low interest rates. Although most will survive, it is a painful time.

How can we ensure that the next generation of actuaries will be any better prepared for another reversal of a long-term trend?

Although we can't be certain, we can increase the likelihood. To do this, we must look beyond economic cycles and seemingly random short-term movements. We must look for things that cause long-term trends, and things that alter those trends. Instead of speculating about a single long-term natural rate for reversion, let's look for factors that will influence the trends of the next 20 or 30 years.

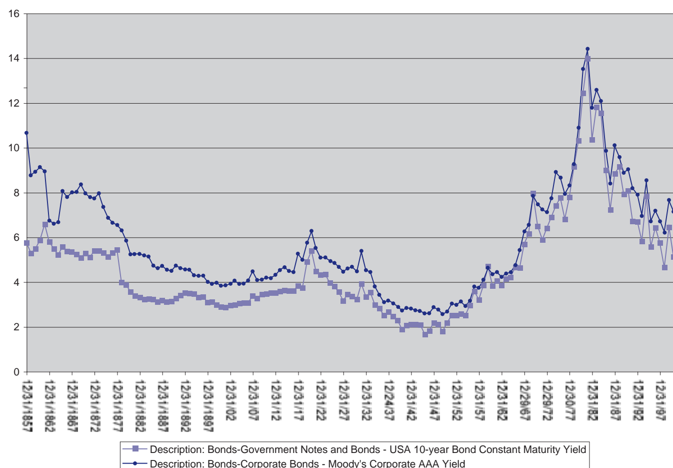
The Current Trend

I started to think seriously about such long-term changes after our 1998 annual meeting. There, in a session called "Cash Flow Testing in a Low Interest Rate Environment," we were shown long-term historical data revealing that, from a historical perspective, interest rates really weren't very low.

That presentation certainly caught my attention, but it was only a starting point. It made clear that there was room for interest rates to go lower, but nothing was said about what might cause them to do so. Having been shocked out of my complacency, I decided to look for possible causes.

In searching for an answer, I found a likely cause to be in demographics which, I concluded, probably had a lot to do with the reason rates increased so much in the 1970s then began a long, slow decline after 1980. In my mind, and on paper, I constructed a scenario of how the demographics of those years could have had a dramatic influence on inflation and interest rates. An extension of the same demographic movement made still lower interest rates seem likely.

Rather than fill this issue with the details of that scenario, I'll refer you to David K. Foot, professor of economics at the University of Toronto. At our 2001 annual meeting, through his keynote presentation, I learned that Dr. Foot has studied and written extensively on precisely this cause of economic change. According to the profile on his Web site, "demographics explains two-thirds of everything."



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There is a watershed issue developing, and only certain tax actuaries are intimately familiar with it. Put differently: Only actuaries can resolve the problem that they could otherwise end up partly responsible for causing by their inaction. However, before we discuss the issue, and to put things in perspective, let's take a short look at the history of certain major changes in life insurance company taxable income over the last 20 years. This history is given to illustrate how our industry has been subject to several significant, inappropriate accelerations in taxable income during this period.

Historical Background

The litany of successive accelerations in taxable income since the 1984 Tax Act includes the following:

- Beginning with the 1984 Tax Act, tax basis reserves were generally set at a level that for a typical company was somewhat less than statutory reserves. This difference was commonly referred to as the "overhang." Further, an addition to this overhang was created via the Act's making the policyholder dividend provision nondeductible to life insurance companies.
- The 1987 Revenue Act initiated the applicable federal interest rate (AFIR), to be used as the tax basis valuation interest rate whenever it exceeded the prevailing statutory assumed interest rate (PSAIR), beginning with contracts issued in 1988. Indeed, over the following 10 years the AFIR was generally considerably above the statutory rate for most life company products. This further depressed tax reserves, causing the overhang to increase substantially.
- The 1990 Act brought about the tax DAC. More about this is in the *Fairness and Equity* section below.

Thus there have been several successive waves of increases in the difference between statutory effective liabilities and deductible liabilities. Perhaps, if this had threatened to take place all at once back in 1984, there would have been significantly greater pushback to this turn of events.

Fairness and Equity

Perfect equity in a tax system is unachievable and unrealistic. As the common phrase goes, "Life isn't fair." The closest principle we have to fairness and equity in the federal income tax environment may be the classical principle, "Pluck the most feathers with the least amount of squawking." Even that doesn't always work, as sometimes we tend to "squawk in advance" by asking for certain treatment, only to find that the response from Congress isn't always exactly what we requested.

As an example, back in the 1980s the battle between stocks and mutuals was at its height. Under the 1984 Tax Act, one result of this battle was the "surplus tax" on mutual companies. The surplus tax formula proved quite unwieldy and woefully inequitable between companies. Therefore, in exchange for sunsetting the surplus tax, some members of the mutual segment unofficially offered up a tax basis deferred acquisition cost (tax DAC). So what did Congress do? In 1990 Congress signed the tax DAC into law but did *not* repeal the surplus tax at that time. There were two messages here:

- We are not clear communicators as to what tax equity means in the life insurance environment.
- What you get may not be what you asked for. [Revenue considerations will often override equity.]

[In fairness, now that the mutual segment of the industry has decreased substantially, we have won a minor victory in causing temporary sunsetting of the Surplus Tax on mutuals.]

Part of our communication problem has been the difficulty of explaining to the public the principles behind life insurance reserves. Additionally, the fact that reserve deductions are a special exception to the federal accrual rules is something that many lay people do not appreciate. Indeed, some members of Congress have the notion that deductible reserves are a special favor to the life insurance industry.

It is apparent to tax practitioners that two of the above-cited components of the current tax environment are consummately inequitable.

The tax DAC is a deemed addition to taxable income. It

is calculated as a specified percentage of premiums, that percentage of premiums varying by product line. The inequities include the following:

- The tax DAC is calculated without regard to the required initial allowances that already exist in the tax reserve formulas. Individual life insurance reserves contain a required CRVM allowance, noncancelable health insurance contains a similar allowance and deferred annuity reserves contain a CARVM allowance.
- The formula is simplistic in that the DAC formula amortizes straight-line over 10 years in most situations. This is obviously unfair to group life insurance, which is one-year term coverage.
- The fact that the tax DAC is on *all* premiums makes the playing field non-level versus competing forms of savings, such as mutual funds. This item has caused life insurance products to lose some competitive edge as asset accumulation vehicles.
- The 1984 Act recognized that the net surrender value should be a floor on tax reserves. The tax DAC allows the "net reserve" to drop below that floor.

The emergence of the AFIR has caused additional inequities. Asset accumulation products with non-guaranteed elements, such as universal life and deferred annuities, are the products where the AFIR distorts economic income the most. To understand why this is true, let us take a moment to compare the tax environment with the statutory and GAAP environments.

- Statutory: The principle of combination of conservative valuation interest rates, coupled with conservative assumed guaranteed interest-crediting rates, is designed to result in reasonably consistent liability values.
- GAAP: The combination of reasonably current interest rates used in discounting, coupled with anticipated current interest-crediting rates on the products, is also designed to result in consistent liability values.

In contrast, the AFIR has given us a combination of [conservative] future interest rate guarantees but close-to-current valuation interest rates. This has caused an unduly depressed tax basis reserve, generating relative taxable income in the early durations and relative tax losses in later durations.

In particular for deferred annuities, the requirement to use the greater of the AFIR or PSAIR exacerbates the inequity, inasmuch as the AFIR is a recent 60-month average while the PSAIR is a recent 12-month average, thus causing an upward bias in a volatile interest environment.

The Looming Issues

Given this set of adverse historical developments, we now have a potential developing trend on the part of industry actuaries and regulators toward stochastically developed statutory reserves. Current activity is with variable annuities with significant death benefit and living benefit guarantees, but there is a constituency that wishes to extend this approach to all products. This situation has come about due to the difficulty of devising a formula reserve for variable annuities with such guarantees. From a "pure actuarial" perspective, stochastic reserve approaches could arguably make perfect sense, inasmuch as we are living in a world where we should be thinking of probability distributions rather than point values. However, the Internal Revenue Code as it deals with tax reserve calculations does not fit well with a stochastic reserve calculation structure. The current tax reserve rules in Code Section 807(d) speak to contract-by-contract calculations, contract-by-contract comparison with net surrender values, and contract-by-contract comparison with statutory reserves actually held, to name only some of the problems associated with stochastically developed statutory reserves. To fit stochastic reserve calculations, which are performed in aggregate for blocks of business, into the current tax structure is problematic to say the least. From a practical perspective, it might be best to slow down the stochastic statutory reserve track and stay with a formula reserve standard. Or, at the very least, couple the stochastic approach with a formula reserve minimum.

An alternative approach to this problem is to change the Internal Revenue Code to accommodate stochastic tax reserve calculations. But, as indicated above, we should be careful what we ask for, since we may not recognize the Congressional response to our request as being at all similar to what we request. The result could be an additional adverse effect on an already overtaxed industry. Even if we were to get exactly the calculation approach(es) we request, there would be substantial transitional issues to resolve.

The Variable Annuity Reserve Working Group (VARWG) of the American Academy of Actuaries is currently dealing with this issue in its attempt to develop comprehensive guidance for statutory reserves for variable annuities with guarantees. Theoretically the most correct reserve would arguably be a stochastically generated reserve, and it would be tempting to ignore tax considerations in pursuit of this theoretical result. However, the VARWG's charge includes being "practical." Additionally, the group is well aware that the issue of fairness of tax reserves appropriately fits within the professional actuarial scope and is currently considering ways to help ensure that the statutory reserve methodologies it is recommending fit appropriately within the current tax environment.

The actuarial community is the primary professional constituency that can come up with a solution that melds statutory and tax considerations in a constructive manner. Thus the VARWG has committed to avoid the "path of least resistance" in carrying out its responsibility, and will be seeking that proper melding. I applaud their work in this effort.

Securing the Professional Future of Life Actuaries

by Narayan Shankar

The Issue

Life Practice Area leaders have identified the "future of the life insurance company actuary" as the key issue requiring attention. There is slow growth in actuarial job creation in life companies and life actuaries face a "one-industry concentration" risk. Actions needed to address this issue fall into two categories: (a) fully actualize the potential of actuaries in insurance companies by expanding to nontraditional positions for which actuaries are qualified and (b) broaden industry base beyond insurance.

Status

The SOA Board of Governors has approved a major strategic initiative to achieve both of the above objectives. Implementation of strategies to achieve these objectives will begin soon. The thinking and brainstorming the Life Practice Area has already done will enable the implementation to get off to a flying start.

Strategy

The main strategic themes are:

1. *Enhance business and communication skills of actuaries*. These skills are considered important for nontraditional positions within insurance companies as well as in broader financial service organizations (such as banks). The SOA exam system may need to be modified to include more emphasis on these skills. FSAs may need additional education. The SOA will facilitate the efforts of members by developing appropriate programs, probably in partnership with other organizations with expertise in these areas.
2. *Improve the image of actuaries*. The profession has underachieved in terms of the recognition it has received for its contributions and talents. A concerted effort to better communicate the accomplishments and capabilities of the profession and its practitioners is needed to raise awareness among potential employers and the public.

In addition, there are long-term process changes that need to be undertaken. These are less concrete than the two main strategic themes identified above. Such initiatives include:

1. *Environmental scanning and capitalizing on emerging opportunities*. The SOA should become a more nimble and proactive advocate for actuaries, helping to identify, develop and quickly capitalize on new areas where actuarial skills can be applied. It is important to be opportunistic and work with a sense of urgency, establishing an effective process to make that possible.
2. *Attract more business-oriented members to the profession*. While no stereotype is an accurate description of any individual, it is probably true that the typical actuary can get caught up in analytical detail not justified by the validity or accuracy of the input data. To an extent, this is the case because the modeling exercise itself is "fun." Actuaries derive consumption utility from their jobs, so they are sometimes not mindful of the business results of their work to the same extent as those for whom the business results are the primary focus.

The Bottom Line

Ultimately, the success of our profession will depend on members dedicating themselves to advancing their careers by strengthening their business acumen and communication skills, and becoming results-focused on their jobs.

Next Steps

Much hard work lies ahead. Most of our objectives can be accomplished only by mobilizing and motivating SOA members to volunteer their time and energy on SOA task forces that drive the initiatives identified above. We will be calling upon members to support our efforts.

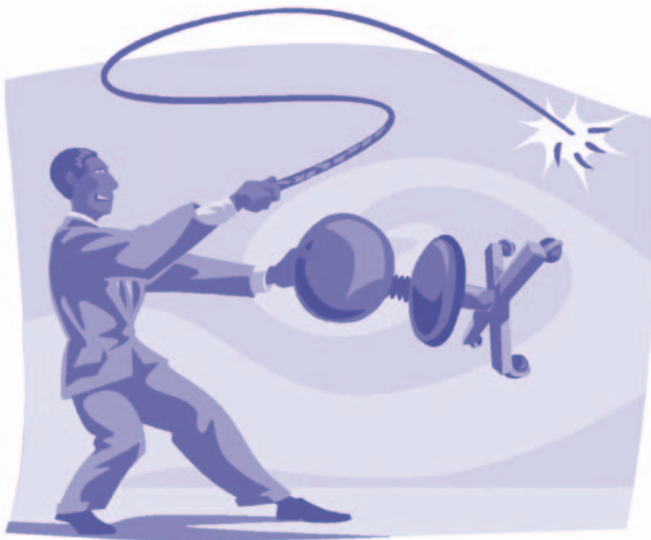
The Future of SOA Mortality Studies

by Larry M. Gorski

Current, relevant and statistically reliable mortality experience studies are a necessity for life actuaries whether they function as pricing actuaries, valuation actuaries, illustration actuaries or risk managers. Over the years, the SOA has filled the need by conducting life insurance mortality studies and then publishing the results in SOA publications. The information published by the SOA has been the starting point for statutory valuation tables, product pricing assumptions and cash-flow testing assumptions. The availability and usefulness of the SOA mortality studies is dependent on insurers providing usable mortality experience on a timely and consistent basis. Recently, contributions to the SOA mortality experience studies have been declining. In an attempt to increase the significance and value of SOA mortality studies to their many and varied users, the SOA formed the Mortality Studies Working Group (MSWG). The composition of the MSWG reflected the range of users of SOA mortality studies.

The MSWG's mission was to make recommendations with respect to:

1. The types of industry-level mortality tables that will be attractive to insurance companies.
2. Other types of insured mortality-related data that the SOA might make available, which would be valuable to insurers.
3. Strategies to encourage companies to contribute data.
4. The right frequency for mortality studies.



Some of the issues discussed and addressed by the MSWG during its nine months of deliberations were:

1. Identifying approaches to analyzing preferred underwriting mortality.
2. Timing and frequency of studies and periodic updates/reports.
3. How best to study the factors that impact insured mortality.
4. How best to present the results.
5. Identifying ways to increase the number of contributing companies.
6. How to best make the results available to users.

The MSWG has recently issued its report. The recommendations of the MSWG, if implemented, will quite likely have a significant impact on future SOA life insurance mortality experience studies.

To learn more about the recommendations and how they may affect the way in which you carry out your actuarial responsibilities, download the report of the MSWG from the SOA Web site.

Of course, implementing the recommendations will not occur overnight and we will need volunteers to make it happen. If you are interested in volunteering for this important and future-looking endeavor, contact the SOA Life Practice Advancement Committee.

Life Practice Spotlight: A Look at Jim Dallas

by R. Dale Hall

This edition's interview is with Jim Dallas, a senior consultant with the St. Louis office of Tillinghast - Towers Perrin. Jim has held a variety of positions in the life insurance industry, including work in both insurance companies and consulting firms. In addition, Jim is co-author, with David Atkinson of Reinsurance Group of America, of *Life Insurance Products and Finance: Charting a Clear Course,* one of the textbooks on the SOA exam syllabus.

Dale Hall (DH): Jim, thanks for taking time out of a busy schedule to talk about your work and the actuarial education process that develops over time. You started out as a student at General American Life and then went to work in reinsurance at ITT Lyndon. What were some of the actuarial techniques you learned in those positions that helped build a strong base for your work today?

Jim Dallas (JD): The time I spent early on in my career focused on acquiring knowledge of insurance products and developing models to project the impact of life and annuity products inside financial reinsurance programs. Working with actuarial modeling software provided a terrific way to learn and expand my knowledge about life and annuity products. Using modeling software and adapting that software to your particular application forces you to quickly gain an understanding of different financial reporting structures, such as GAAP accounting and the taxation of life insurance companies. With certain applications, you also gain a quick appreciation for the asset side of the balance sheet as well.

DH: What were some of the "best practices" that you learned from those experiences and from the actuarial exams you were taking at that point that you were able to incorporate into your work?

JD: It became clear that there was a need for actuaries to be very disciplined in setting assumptions and to perform sensitivity analysis. For example, when developing a reinsurance transaction, we would first ask for details in developing baseline assumptions, but we would then assess various plausible sensitivities in order to understand the potential outcomes. Once you better understand the other potential outcomes, you are in a better position to structure the reinsurance in such a way as to reduce risk, or to manage the risk better.

I also learned to think about ideas not only in actuarial terms, but also in financial terms. The first time I worked closely with people with more of a finance background than an insurance background was in the reinsurance business, and that provided a new insight into the work.

DH: More recently in your career you've taken on a senior level role at RGA Reinsurance, and now you're in a senior consultant position at Tillinghast. Both of these positions brought you into contact with a variety of executives in a wide range of insurance organizations. What types of skills do you find to be critical to achieving success in those roles?

JD: One of the important skills that helped me in those roles was learning how to think things through creatively in order to find a solution that is mutually agreeable to both parties. Negotiation skills are also helpful in finding solutions that consistently meet the goals of both sides.

There is also the art of learning that if something doesn't appear to be a sound deal, it's alright to not have it happen. It is often better to not execute a transaction that you are not 100 percent comfortable with than to write it only to have it go sour down the road.

I also worked more closely in those roles with marketing people who did not have actuarial backgrounds, but needed to understand complex financial instruments and reinsurance products. I quickly picked up on the fact that actuaries aren't the only ones capable of high-level thinking. There is an ongoing stream of people we meet and always something new to learn.

DH: Now that you've had the perspective of both a senior-level actuary at a major reinsurer and a senior actuarial consultant at a major consulting form, what types of similarities do you see in your activities?

JD: I think an important similarity is to obtain several perspectives on the solutions you can provide. Review by others is, and should always be, an essential part of any actuary's job, whether it's in a company or as a consultant. Some people have a fear of having their work scrutinized by others, but in the end it can prove to be a beneficial course of action.

DH: Jim, many thanks for the insight into your actuarial career and for the information we can all put to our own personal use. Best wishes for continuing success.

Hot Topics

Developments at the NAIC Life and Health Actuarial Task Force

Larry M. Gorski

The December 2003 NAIC Life and Health Actuarial Task Force (LHATF) meeting was typical in the sense that some recommendations concerning laws, regulations or actuarial guidelines were adopted, others were exposed for comment and others were discussed during the meeting with no action taken. One of the more interesting and unexpected developments took place near the end of the two-day LHATF.

It is traditional that the agenda (Charges) for the upcoming year for NAIC committees, task forces and working groups is discussed at the fall NAIC meeting. The charges for each such unit of the NAIC structure is sent to the highest level (Executive/Plenary Committee) of the NAIC structure and approved at the December NAIC meeting. This year, the process encountered a few bumps along the way.

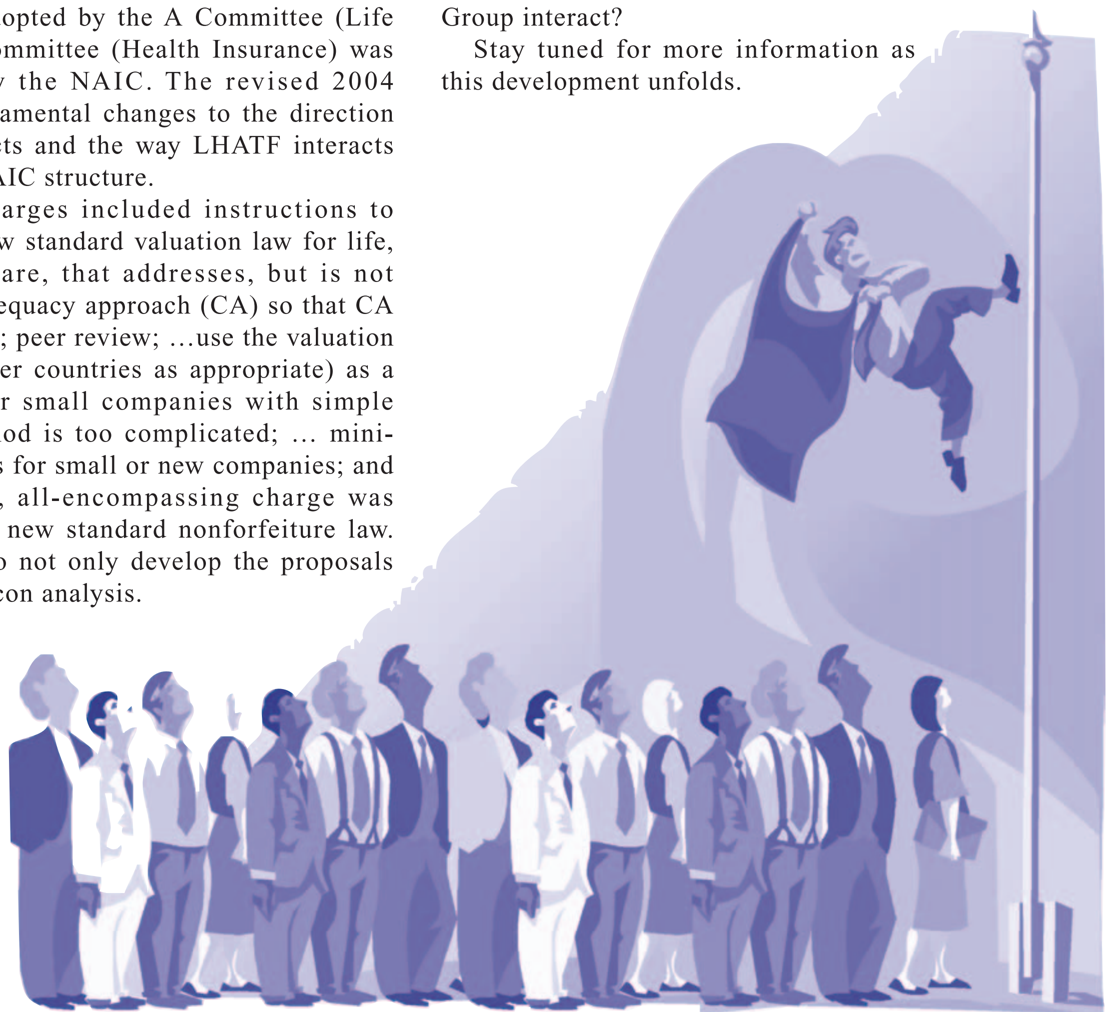
Shortly before the December NAIC meeting, it was revealed that a proposal to amend the 2004 charges agreed to by the LHATF and adopted by the A Committee (Life Insurance) and the B Committee (Health Insurance) was under consideration by the NAIC. The revised 2004 charges made some fundamental changes to the direction of certain LHATF projects and the way LHATF interacts with other units of the NAIC structure.

The revised 2004 charges included instructions to LHATF to "propose a new standard valuation law for life, health and long-term care, that addresses, but is not limited to, …a capital adequacy approach (CA) so that CA equals RBC plus reserves; peer review; …use the valuation laws of Canada (and other countries as appropriate) as a guide; …safe harbor for small companies with simple products if the CA method is too complicated; … minimum capital requirements for small or new companies; and FIT impact." A similar, all-encompassing charge was directed at developing a new standard nonforfeiture law. LHATF was instructed to not only develop the proposals but to provide a pro-and-con analysis.

Needless to say, the revised charges generated a significant amount of discussion during the LHATF meeting and behind the scenes. It appears that not everyone agreed with the proposal to revise the LHATF 2004 charges. At the Executive/Plenary Committee meeting, the original LHATF 2004 charges were adopted but the proposal to revise the charges was deferred for further study.

The strategic question is: What does this action signal for future projects and decisions by LHATF? Will LHATF look more favorably at valuation methodologies that rely on actuarial judgment as compared to formulas? Will LHATF pursue nonforfeiture proposals that are less formulaic and more dependent on actuarial judgment? How will the LHATF and the Life Risk-Based Capital Working Group interact?

Stay tuned for more information as this development unfolds.



Report on LPA Committees and Task Forces

by Karen Gentilcore

The Life Practice Area (LPA) oversees more than 20 research projects and experience studies. This past year, four oversight subgroups were established to foster ownership of responsibilities and tie our strategic initiatives and member needs with the committees' work.

The Research Oversight Subgroup (Mary Bahna-Nolan, chair) developed a set of criteria by which research projects should be selected. The goal is to make wise use of our funds and volunteer time.

The Experience Studies Oversight Subgroup (Faye Albert, chair) has been discussing the issue of annuity experience studies and met in Orlando with employers to get their ideas.

The Communication Oversight Subgroup (Larry Gorski, chair) provided input on the external relations database being developed by the External Relations Committee. They are now looking at the three or four most important organizations with which they want the LPA to build a stronger relationship. This subgroup is also responsible for the LPA newsletter and will be working with the SOA Web redesign team.

The Emerging Issues Advisory Subgroup (Larry Stern, chair) identified the top five issues for life practitioners and had white papers written on each. Two of these, the future of the life actuary and the fair value of liabilities, were discussed in Orlando. Next steps are to move forward with action items that came out of the discussion.

The Committee on Life Insurance Mortality and Underwriting Surveys (Al Klein, chair) has completed reports on mortality improvement and on preferred underwriting of reinsurers. These reports, along with reports of previously completed surveys, can be found on the SOA Web site under Research. Expect to see work on a simplified issue survey and a risk management survey in 2004.

The Committee on Life Insurance Company Expenses (Sam Gutterman and Timothy Harris, co-chairs) completed the compilation of life insurance and annuity product expenses experience information from 29 life insurance companies using 2001 data. The report is posted on the SOA research site. They are now collecting data for the 2002 study.

The call for papers has been issued by the **Committee on Life Insurance Research** (Bob Johansen, chair) for the 2005 “Living to 100” symposium. Thirty organizations have agreed to assist with the symposium, distributing information to their members and encouraging participation. Included in that symposium will be a research paper by Drs. Gavrilova and Gavrilov on “Living to 100 and Beyond: Search for Predictors of Exceptional Human Longevity.” This committee is also working jointly with the Committee on Knowledge Extension Research on a project to identify such predictors. Results of this research will also be included in the "Living to 100 and Beyond" symposium. Save the dates, January 12-14, 2005, and join us in Orlando at this exciting conference. The first draft report, "The Effects of Secondhand Smoking on Mortality and Morbidity" is currently under review. Expect final information in 2004.

The Mortality and Morbidity Liaison Committee (Clifton Titcomb, chair) expects a final draft of the build study in April 2004. This study examines the mortality experience of recently issued life insurance policies that had an identified build impairment. The diabetes study should be available in the next month or so.

The LPA provides significant input into the education of actuaries who have chosen to specialize in the life area. **The Committee on Individual Life and Annuities Professional Development** (Jim Dallas, chair) updated the professional development model plans, including adding a new model plan for U.S. financial reporting. They then compared the model plan topic listings with the continuing education sessions from the 2003 SOA spring and annual meetings. Information on gaps in topic offerings was sent to the sections to use as possible topic ideas in the 2004 meeting planning.

The LPA also provides support to committees that fall under the Education and Examination structure. More nation-specific material will be introduced in the November 2004 Course 8ILA exam, and separate U.S. and Canadian exams will be conducted. An advisory group made up of practitioners from various types of life industries continues to provide feedback on the education and qualification redesign system. The latest information on the redesign can be viewed on the SOA Web site at *http://www.soa.org/eande/index.asp*.

A Trend at an End?

After arriving at a plausible cause of past and possible future trends, I began to wonder, what might stop such a dramatic force from causing still lower interest rates?

I found an answer to this question in, once again, the baby boom generation. Rather than sheer numbers, however, let's look at characteristics of this generation.

Two things stand out as particularly significant. One, this generation grew up during a time when Keynesian theory was a dominant force in economics, and especially in government policy. Two, this generation grew up with television advertising.

Taken together, we have a huge generation schooled on the economics of consumption (a healthy economy is the result of strong consumption) and nursed on the strong temptations of television advertising.

Until our current economic distress and other world events took over the spotlight, it was not uncommon to hear or read of the inadequacy of baby boom savings. Realizing the experiences of youth for this generation, it seems almost foolish to think it could have been otherwise. Even today, with the economy still struggling, the efforts of government are directed at increasing consumption. Adequate retirement savings no longer holds a significant place in the public eye.

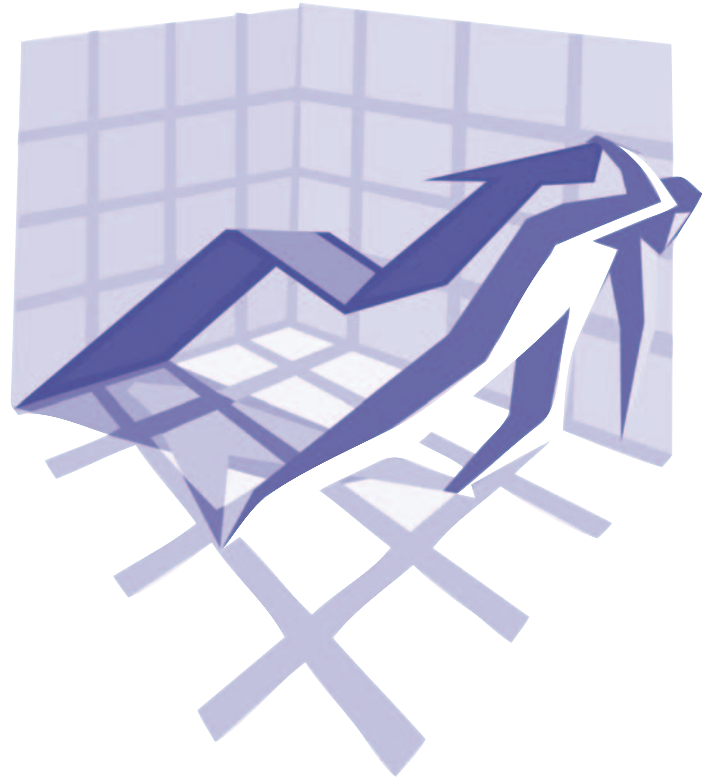
Might this prevent our unthinkable scenario from emerging? Assuming it does, do you think that would really be a good thing for the long-term strength of our financial security systems?

The Next Trend

Now suppose that the unthinkable really does happen, that interest rates do remain low for several years, what might eventually cause them to start another long-term upward trend?

Having been through a period of much higher rates, it should not be terribly difficult for us to imagine such a scenario. Anticipating a cause might be a bit more challenging, but even that should not be hard. You can probably name some possibilities already. Even if you can't, it's not hard to find someone who can. A simple Internet search can quickly lead to a number of sources dealing specifically with this concern.

In considering the issue, it seems to me that the big question about long-term rising interest rates is more about when and how fast than about if. Still, if we and our successors are to be any better prepared for that transition, we will have to keep the possibility in front of us, even if low interest rates start to seem natural.



Conclusion

Economic cycles and scenario generators are important to our work. Understanding the former and using the latter are valuable. Similarly, best estimates based upon professional judgment are valuable. However, we need to look beyond all of these. Rather than looking for a single reversion point for all time, we need to consider how natural rates move over time, to mix major trends with short-term variability. Besides looking for a most likely scenario, we need to look for significant, plausible scenarios.

To be better prepared for the next major change in direction, we must look for the underlying factors that lead to such change.

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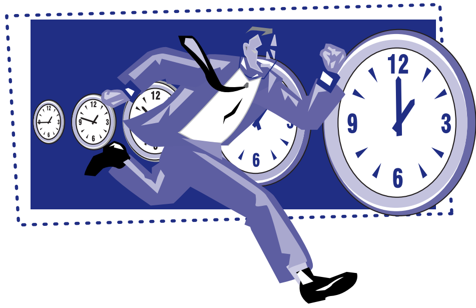

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