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Session 83PD
Product Development from a Small Company Perspective

Track: Product Development, Smaller Insurance Company

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Summary: This session discusses how small companies can set themselves apart through innovation in their product portfolio.

There are many ways in which small companies might feel disadvantaged. New product development is often one of them. Small companies don't have the resources of larger companies to devote to new product development. They also don't possess the efficiencies to compete on price alone. To be competitive, or even just to survive, small companies need to be creative and distinguish themselves through unique product offerings.

Mr. Kenton L. Scheiwe: Let me introduce the panel. Janice Duff, first vice president and actuary from Baltimore Life Companies (BLC). is going to talk about some of the niche things that Baltimore Life does. Because they are a fairly small company and are successful in their niche marketing, she will have a lot of good things to say.

David Wylde, vice president and actuary from American United Life Insurance (AUL) is going to look at it from a reinsurance perspective. He will give you insight into how reinsurers can help you as a small company.

Let me begin by providing you with some of my observations from my experiences of working with small companies. This is an opportunity for me to show you what I sometimes think of when I go into a small company, and especially what I think of when I leave.

First, I'm going to look at some disadvantages of being a small company. Then I'm going to look at some advantages of being a small company. Third, I will look at some things that can set small companies apart. Finally, I am going to talk about an

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overhead expense study, the "1999 Overhead Expense Study," that Milliman & Robertson (M&R) produced. It has some neat aspects that pertain to a small company. It basically compares your expenses against other companies.

Let's begin with disadvantages for small companies. The first one is obvious. Efficiency is generally a function of size. As a small company, you can't do much about this. It's one of those things you'll just have to live with. This will be discussed more with the M&R expense study.

The second disadvantage for small companies is limited people resources. Once again, what are you going to do about this? This is something you're going to have to live with and somehow overcome.

These are my observations. Please be careful. I see this all the time when I go into companies whether they are large, small, or medium-sized. Some companies have a tendency to overanalyze situations that don't mean a whole lot to the company. Every manager has to make the decision about to which areas people resources should be allocated. The way in which companies' resources are allocated is often questionable.

The third disadvantage for small companies is limited information resources. This can be overcome by attending professional meetings and by using the Internet. In my workplace, I rely on other people within M&R and outside of M&R. It's easy for me to pick up the phone and call someone who is knowledgeable in the area in which guidance is needed.

This kind of meeting is an excellent place to get to know people. Don't just ask them where they're from but also find out what they are doing. What areas of expertise do they have? Make a mental note so that the next time you come across that, you can pick out this name and give them a call. I have never had the experience of calling another actuary for information and found that they have been unhelpful. Actuaries are willing to share the knowledge that they have. Use that to your advantage.

Let's continue with advantages for small companies. The first advantage is that small companies can move quickly. I work with some rather large companies and, generalizing somewhat, these large companies don't always move quickly. Some small companies are like this. But then some small companies move rather quickly. A decision is made, and within a very short period of time, they have what they wanted to accomplish. An example of an area where companies move at different rates is the product development area. Some companies can have a product idea and have this product on the street in a few months. They have the product priced, they have the product filed, they have some state approvals, and they are out selling the product.

This does not happen that often in large companies. That's something you can take advantage of, especially if you're in some kind of niche market, where timeliness is very critical.

The next two advantages for small companies are about personalized service, not only to the policyholders, but also to the agents. You have the advantage that you can know your agents, and many times you can know your policyholders very well. At one time I worked in a fairly small company, and I knew people who worked in the policyowner service department. They knew many policyholders quite well. They often knew them by name, and there was either a smile on their face, or not a smile on their face when they heard from some of those policyholders. But yet, it was a personal sort of relationship. A small company can take advantage of that much more than a large company.

The fourth advantage for small companies is that you are also able to sell products in niche markets where size is not necessary. You can find those niches and take advantage of them.

A proverb that I grew up with that stuck with me for my whole life has to do with selling niche products and taking advantage of something you're good at. The proverb says, "One, two, whatever you do, start it well, and carry it through." Obviously, that is something that applies not only to what you're doing, but also to your niche market. If you find something that you're good at, why don't you take advantage of that?

The fifth advantage for small companies is one of my favorites. People in small companies often say, "I like working at a small company because I knew I could make a difference. In a large company, I had the feeling that no matter what I did, whether I showed up or not, nobody would know. But in a small company, I liked the idea that I could make a difference, which is unique to small companies, and always gave me a better attitude and enhanced work performance." This is something a small company should not lose sight of.

Finally, and I've mentioned this before, please spend time thinking about what it is you do. There is a whole list of things that need to be done, and especially in a small company, you just can't get them all done. How are you going to get them done? Are you going to have somebody outside of the office, whether reinsurers or consultants, do the work? Are you just going to forget about it? Are you going to make sure that it gets done within your office by using your own resources? How are you going to get it done? This is something that is critical for managers in a small company environment, not only in the product development processes, where it is obviously key, but also throughout the company.

What can set you apart? First, the product you offer can do this. If you're in some niche markets, that product will obviously set you apart. Some of the products in niche markets are tax-advantaged products in the group insurance market, annuities with special riders or investment funds, and one of the numerous versions of the life insurance contract. We are only limited by our imagination.

Your distribution system can also set you apart. I encourage you to market your product to unique individuals and organizations. Examples are small businesses, associations, military personnel, college students, and religious organizations. I've

worked with all kinds of companies that single out one of these and develop and sell a product for that sort of distribution system and then cater to those people. This is what you will have to do as a small company: target a niche market for your products.

How do you market this product? Examples of nontraditional marketing are: independent marketing organizations (which might be tough to use if you work for a small company); the Internet; and something I heard about that goes on in Japan. I don't know how familiar you are with the Japanese market, but the way that life insurance has been sold over there for many, many years is through the wives and mothers that stay at home.

In thinking about this presentation, I wondered about U.S. insurance companies taking this approach. My initial idea was, why couldn't we have home parties and have all these women who are now selling Tupperware, Mary Kay, and candles, sell insurance? I can see my wife having a party to sell insurance that would appeal to the mothers in attendance. For example, she could be selling a life insurance policy that will have some type of accumulation account to pay for college.

A third thing that can set you apart is your service and training. You'll have to provide exceptional service and do a better job than what the large companies are doing. One set of companies that have capitalized on this are the Farm Bureaus. Generally, they have agents that are very dedicated to the clients. They have been able to have repeat sales over and over again with these clients.

Finally, let's talk about the M&R overhead life expense study. The objective of the study was to estimate overhead expense for the individual ordinary lifeline of business only. The basis of the study is the statutory annual statement information from 1994 to 1998. The overhead expense definition is the excess of the general insurance expense over the imputed variable expense. Variable expenses will be discussed in a moment.

Let's discuss which expenses are included and excluded. Commission and agency-related expenses were excluded from this study. Marketing and developmental expenses in the home office were included. Basically, expenses in the home office were included. Expenses outside of the office were excluded.
There are 321 companies included in the study. The reason there are not more than 321 is because we wanted the same group of companies over the five-year period. We didn't want companies coming in and out of the study. We wanted to analyze the same group of companies over that five-year period to see the trend in expenses for these 321 companies.

Only companies in which their primary business is ordinary life or had at least $25 million in ordinary life direct premium were included. We excluded reinsurance companies. Overall, 82% of total ordinary life insurance was included in the study.

The variable issue and underwriting expenses are $50 per policy, plus $1 per $1,000 of face amount for average sizes of at least $50,000, or plus $0.70 per $1,000 of face

amount for average sizes of at least $150,000, or plus $0.20 per $1,000 of face amount for average size over $500,000. The variable maintenance expense is either $17 per premium-paying policy or plus $11 per paid-up policy. Once we knew the variable expenses, everything else was thrown into overhead expenses. Average size is based on annual statement information.

Variable maintenance expenses were $17 for premium-paying policies and $11 for paid-up policies. That is rather low. The reason they were rather low is because they didn't want to have companies with a negative overhead expense. By applying this formula, there were very few companies that had negative overhead expense. Those were efficient companies! After removing these variable expenses, everything else is thrown into overhead expense.

Let's look at Table 1. The percentages in the top four rows reflect the percentage of direct ordinary premium. Even though it's not labeled, it shows the percentage of direct ordinary premiums. The top left number, 9.5%, is the percentage of direct ordinary life premium.

Here are some observations when you look at these numbers. Look at the top two rows. Notice how the weighted average and the arithmetic mean are pretty far apart back in 1994, and they seem to gradually go together by 1998. To me, that means that the difference in overhead expenses is narrowing between the large companies and the small companies. I think that's verified in the following tables.

TABLE 1
ALL COMPANIES SUMMARY OF OVERHEAD EXPENSES

	1994	**1995**	**1996**	**1997**	**1998**
Weighted Average	9.5%	10.1%	10.4%	10.8%	10.9%
Arithmetic Mean	12.3%	11.9%	10.9%	11.1%	11.2%
Standard Deviation	22.7%	21.6%	19.5%	16.6%	18.7%
Median	9.8%	10.2%	10.7%	10.8%	11.3%
Expense per Policy	$48	$52	$52	$56	$55
Ratio-to–Variable Expense	169%	185%	191%	199%	200%
Number of Companies	321	321	321	321	321

The standard deviation for overhead expenses is large. Companies are all over the place. Keep in mind these are just averages, and the standard deviation is quite large.

Finally, look at the line that says "ratio-to-variable expense." Those are pretty big numbers. The average ratio is about 200% for all the companies in this summary. That is quite large.

The following will split expenses between large, medium, and small companies. This is how a company is defined into its particular area. Large companies have greater than $100 million in individual life premium; medium companies have $25-100 million in premium; and small companies have less than $25 million.

Let's compare the arithmetic mean among large, medium, and small companies (Table 2).

TABLE 2
ARITHMETIC MEAN OF OVERHEAD EXPENSES

	1994	1995	1996	1997	1998
Large Companies (excluding 3 large Mutuals)	9.6%	9.9%	9.8%	9.8%	10.4%
Medium Companies	10.4%	10.0%	8.2%	8.6%	9.0%
Small Companies	18.1%	16.6%	15.3%	15.8%	14.7%

Note that the large companies exclude the three large mutuals. If we had included those three large mutuals, the large company expenses would have been extremely large. By excluding those three large mutuals, we have better comparable numbers, because those three large mutuals just dominated the large company numbers.

Once again, this shows that if you compare the large companies with small companies, you'll find that small companies are doing a better job over this five-year period from 1994 to 1998. Look at the medium companies. It seems like they are winning the day. On this type of measurement, as a percentage of premiums, the medium companies have been the ones that have been most efficient.

Another way to look at the overhead expense is on a per-policy basis (Table 3).

TABLE 3
OVERHEAD EXPENSE PER POLICY

	1994	1995	1996	1997	1998
Large Companies (excluding 3 large Mutuals)	$39	$41	$42	$45	$46
Medium Companies	$34	$33	$28	$27	$28
Small Companies	$37	$39	$38	$36	$30

Large companies seem to be pretty high. Medium and small companies are pretty similar.

This shows me that in comparing the large companies and small companies, and in comparing Table 2 with Table 3, it looks like the small companies, overall, have larger average size policies than the large companies do. That's the only way I can justify these numbers. In Table 3, the large companies have a lot bigger per-policy expense than the small companies. In the prior table, the expense as a percentage of premium was pretty close. Once again, the medium-sized companies seem to be the ones that are most efficient.

Table 4, the ratio of overhead expense to variable expense, shows the same thing.

TABLE 4
RATIO OF OVERHEAD EXPENSES TO VARIABLE EXPENSE

	1994	1995	1996	1997	1998
Large Companies (excluding 3 large Mutuals)	135%	146%	153%	159%	167%
Medium Companies	120	113	98	96	100
Small Companies	147	150	149	139	116

Look at how big those large companies' numbers are. There are a lot of large mutual companies that have had extraordinary large one-time projects during the years 1994–98. Maybe that's what is driving these large companies' numbers up. Demutualizations especially have to be a big expense for them. Class-action suits might also be inflating the large company numbers.

Another observation was made with the small companies. Look at how much improvement there has been over these few years. Maybe 1998 is just an aberration. To go from nearly 150% in 1994 down to 139% in 1997 and 116% in 1998 is quite an achievement. Maybe cost efficiencies are taking place in the small-company environment.

Finally, let's look at the stock/mutual split for small companies in Table 5.

TABLE 5
STOCK/MUTUAL SPLIT FOR SMALL COMPANIES

	1994	**1995**	**1996**	**1997**	**1998**
Arithmetic Mean					
Stock	18.3%	16.7%	15.3%	15.5%	14.3%
Mutual	16.8%	16.1%	15.8%	17.9%	17.8%
Expense per Policy					
Stock	$36	$38	$36	$34	$28
Mutual	$48	$50	$50	$58	$51
Ratio–to-Variable Expense					
Stock	143%	147%	145%	130%	109%
Mutual	166%	171%	174%	195%	169%

Mutual companies generally have slightly higher expenses than the small stock companies.

There are a total of 88 out of 321 companies that qualify as small companies. Seventy-seven were stock companies and only 11 were mutual companies. There's not a big sample of small mutual companies. They are almost all stock companies.

Let me make one final observation about this study. I've often heard that small companies have to get bigger and grow out of their problems. I'm not so sure that being big in itself means that your expenses are going to be low, and I think this study shows that. For efficiency's sake, you have to be big. But just being big won't

necessarily mean that you are going to be efficient. As a small company, there are still some advantages, and in the expense area, according to this study, it seems that small companies aren't out of the ballpark. You can still compete.

Ms. Janice A. Duff: I am currently the vice president and actuary of Baltimore Life Companies. In my prior role, I served as the company's marketing actuary, and as such was heavily involved in the product development process.

In a company with limited resources—be it people, expertise, or finances—we learned first-hand the importance of clearly identifying and executing the steps in the development process. As we actuaries are known to do, I would like to outline such steps in formula terms. If we set the vision, plus determine the strategy, and develop relationships, plus determine the resource needs, develop the product, get it to market, and monitor the results, then the result should be a successful product development exercise. Let's go through each one.

At the core of the process is setting the vision. What do we want to accomplish? What do we want to be known for? In our case, when we first developed our independent sales division in the early 1980s, then known as the general agency, our emphasis was on the brokerage market. As such, we were developing various products for broad distribution systems. That worked for many years.

But then we found that in order to stay on top, we needed to be more price-competitive. With expense limitations, we found that really wasn't viable. We decided to instead focus on setting ourselves apart, based on product offerings, service, and the like. Finding niches, or as we like to call them, nooks and crannies, became our trademark.

Armed with the vision to pursue, in our case, niche marketing, we then set to work to determine the strategy for its execution. It all boiled down to answering the "who, what, when, where, how, and why" questions.

We'll start with who. It's important to decide who to target, because niche marketing is all about meeting specific needs, not trying to be all things to all people. Most of our niche marketing is done in the middle market. We have some in the upper market, and actually, we have some final expense products in the lower scale.

We tend to focus on individual sales, although, in recent years, we have been building up some of our group and employer sale environments.

Next is what. It's important to decide on what your product strength is. What are you going to focus on? What are you going to look to other companies to help you with? At BLC, we specialize in traditional and fixed universal life (UL). For other products, such as disability income and long-term care, we've decided to partner with other companies. Again, when you're focusing on niche marketing, you need to decide what's going to be your specialty, and what are you going to look to others to help you with.

The question of when can vary, depending on the opportunity. You might decide, in some cases, 'to be a trailblazer. BLC actually was a trailblazer in the UL market.

We also decided five to six years ago to develop a whole life product for the final expense market that is somewhat unique, and I think it still is. You pick your premium pay period, be it single-pay, 20-pay, or life-pay. It kind of adds a flexibility to what is typically a traditional life type product. In these cases, we were trailblazers.

In other cases, we've actually decided to learn from others' experiences. We've been approached, for instance, by organizations that wanted us to replace a former carrier's product. It might have been in the Section 419 market or in other arenas. We welcomed that, because that was a chance for us to learn from others' experiences.

Where can vary depending on the opportunity you are pursuing. You might focus across the country. You might actually decide to look overseas. Or, in the case of certain distribution systems, you might just decide to look at a certain territory. It will depend, actually, on the next item.

How do you plan on distributing? The options are almost limitless. You can work with career agents, brokerage agents, or independent marketing organizations. Again, worksite is an up-and-coming arena for many companies. In the extreme, you might decide to use direct marketing or the Internet to do your distribution. I think the thing to keep in mind with niche marketing, is you're not likely to develop a product that all of those distribution systems will be able to make use of. Try to think about what distribution system is best suited for the product at hand.

The final question is, why. That's probably the easiest because the goal here is to set your company apart as a product development leader.

We come to what I consider one of the most critical steps in the process, and that is developing relationships. I think it's safe to say that niche marketing is all about building relationships. BLC strives to develop and maintain strong relationships with marketing partners.

The marketing partners are the ones that know the markets and the needs. Along with carriers with technical expertise, ideas can become plans and theories can become reality. One thing that we chose to do was actually develop a marketing actuary position, which is housed in our corporate marketing department. That worked very well, because putting an actuary in the very early discussion stage allows parties to make informed decisions quickly instead of getting an actuary involved after an idea has been tossed about for some time.

As we've discussed, it's important to realize that, as niche players, you can't be everything to everybody. Our experience shows, as we've been pursuing niches, that out of the 40–60 opportunities that come our way in a given year, nearly half of them are dismissed pretty early on. The fit is just not there. But, by the end, we' have

three or four solid opportunities that we're interested in pursuing. Again, you can't be everything to everybody, but look for the opportunities that seem to make the most sense.

Given the limited resources of people, knowledge, and finances, in order to be successful, small companies need to evaluate opportunities quickly but thoroughly and know whether or not to pursue or move on. Marketing plans and cost benefit analyses are important. However, companies need to balance the need for detail with the need to be responsive. You can't spend a lot of time evaluating an opportunity before making a decision whether to move on. Successful players are those who act, not react, and lead, not follow.

''Clearly the key to niche marketing is being prepared to meet even the strictest of requirements.

You've got a vision, a set of strategies, and some strong relationships. You're ready to tackle one of those three or four product ideas that made the cut. What do you do?

You're now at the stage where you need to determine the resource needs. Who will develop the product? It's wonderful if you've got inside expertise to do that, but if not, search for consultants or partners with alliances in mind. BLC has actually done this. We've worked with reinsurers who will price the product for "free" in order to develop a reinsurance commitment once that product is actually on the street. That has worked well for us.

Who will file? Again, internal expertise should be used whenever possible, but if not, consider buying services on an as-needed basis. Perhaps you'll have them do the initial submission of a project or filing. But then you will internally take care of the resubmission and any disapprovals that come in. Make use of existing policy forms whenever possible and within NAIC illustration guidelines. That's something we do a lot of. We' have multiple products under an existing policy form.

Who will administer? Here's another area where the options are somewhat limitless. Ideally, to reduce unit costs, you would put as much on your system as possible. But consider outsourcing for those products that have currently unsupportable, complicated features or questionable volume. If the ultimate goal, though, is to bring it in-house some day, then you might consider tweaking the product design with that in mind.

Another thing that we at BLC have taken advantage of is, some marketing organizations actually offer services, be it billing or customer service. By taking advantage of that, you can greatly reduce the overall administration costs.

We're actually to the point where we want to develop the product. I would say, without question, the key is communication. The best product development exercises are interactive: actuaries and sales and marketing folks working together to create products that will sell and be profitable because we all want that.

Making product changes after the fact can be difficult and costly. Get all the ideas on the table up front, and you'll have the most chance of success.

Know your strengths, which is a big, big thing for niche marketing. If agency support is your strength, tout it. If ease of issue is your forte, capitalize on it. Remember, niche marketing is more about what you can bring to the table than what you can't.

Assumptions and goals. This is obviously key to the product development process. What are expected sales? What are must-have features? What type of underwriting will be used? For instance, if you're going to assume six tables in the definition of standard, then obviously the price of the product is going to be higher than if you didn't do that. Get all your assumptions on the table and make sure that everyone is in agreement as you begin that pricing exercise.

Sometimes developing a project plan isn't easy to do. Sometimes you want to just jump right in and start pricing. But it's good to set up a project plan and try to follow it because it sort of sets the stage. It will outline the effort involved. More importantly, it will put the opportunity costs in black and white. If I'm undertaking this project, I cannot undertake another one. It makes everybody aware of what decisions are being made.

Consult with others. Obviously, small companies can't have all the expertise or all the answers. If it's a new market for you, then seek advice. Ideally, you'll reflect that in the pricing of the product as a development cost.

Finally, consider test marketing, especially if it's a new area for you. You could use an expert group of sales representatives to test the water before diving in with the full team.

We've developed the product and we're ready to get to market. How many people here find that the implementation process tends to be difficult? We're all excited about the development. Getting through the implementation is sometimes a challenge. It's pretty common.

I would argue that the best-developed product would fail with poor implementation follow-through. The desire to move ahead to the next pricing challenge often leaves product implementation efforts behind. One idea that we had was putting development in marketing and putting implementation in actuarial and/or model office. The key there is to have early dialogue for a smooth transition. You don't want to have all the actuaries developing the product and then announce, here's the new product bulletin, go implement, when the other folks have not had any prior exposure to that product. Be sure to have early dialogue.

Make sure all systems (administrative, evaluation, illustration, and compensation) are ready, ideally, when they are introduced (if not when they are introduced, then shortly thereafter).

Service would mean service to clients, service to agents, and service to partners. Remember that product offerings are what can set small companies apart from the low-cost competitor down the street. Make sure that you keep all parties informed and, hopefully, content. The more parties involved, the more important that dialogue becomes. You won't save any time or money making use of others' efficiencies, if you don't communicate.

What's next? You've got a product on the street that's doing really well. It seems to be a hit. Don't rest on your laurels too soon. There's no doubt that other companies might venture in. You'll need to make subtle, or not-so-subtle, changes to stay on top.

Monitoring the results. Unfortunately, this is also an area where sometimes not enough emphasis is placed. Post-introduction monitoring is difficult for small companies. What we suggest is, make use of existing management reports (for instance, sales reports) to get a sense of whether you're making progress or whether there is a problem.

Use vendor-based or homegrown systems to evaluate actual-to-pricing results, keeping in mind that statistical significance can be difficult to achieve, given your size. That's where using research from companies such as M&R or AUL comes in handy.

Finally, when something does become a trend, you want to act on it. Adapt to make sure your product continues to be successful. If you can see that the mortality experience is not what you had priced for, be sure to reflect that in your next version of the product.

In summary, small company product development success is basically contingent on three things. One is capitalizing on your internal strengths (knowing what you do well, and letting everybody else know what you do well). Two is developing relationships to overcome those weaknesses that you do have. Finally, three is adapting to changing product needs and markets.

In a world of mergers and acquisitions, those companies that are destined to survive will be the ones that set themselves apart, particularly in product innovation and service. With the right talent, larger ones needn't swallow up small companies. Small companies can use their size to their advantage.

Mr. David N. Wylde: This talk is about the small company dilemma. If you don't think you have dilemma, then you don't need to be here. The general session speaker, Jim Benson, made an interesting comment. He said that within the next 10 or 15 years, there wouldn't be more than 50 insurance companies in the whole U.S. Either that means we're all going to be out of business, or he's wrong. I'm here to tell you that the small company can compete.

How can the small company compete with the big boys without losing its independence and agility? Of course, what that really means is without being purchased or going out of business. How can you stay in the market without being

sold? I mean that's the deal. 'What's happening is small companies are being bought up.

What advantages do big companies have? What are you actually up against? Well, large companies have access to resources, information systems departments, actuarial, and claims expertise. They have a lot of people that they can bring to bear.

Access to capital. Some small companies are surplus rich, but many don't have that much. Trying to compete with a large company who has a very good source of capital and a very low cost of capital is hard. They have a large array of products, just from the fact that they are big. They can get into term, universal life, variable life, and specialty products like long-term care. I'm just giving you a laundry list here. I'll get into more detail a little later on.

Multiple lines of business. Big life companies are often also property and casualty companies. They have one-stop shopping—anything from mutual funds to life insurance to car insurance to homeowners. Big companies can bring this, and there's a lot of synergy that evolves from that.

Diversity of risk. Just from the fact that they are big, their financial results tend to be smooth. A large life insurance company's mortality experience, with a lot of exposure, tends to be pretty smooth. The reinsurance perspective for small company clients ' shows that one year they'll have one claim, and the next year they'll have nothing. It can be that variable.

What can the small company do about this? I decided to take a quote from the book of least-loved insurance phrases. It says, "I'm from your reinsurance company, and I'm here to help." Now, that's not always a bad thing. The reinsurer can actually help you compete with the big boys.

How can we do this? How can the reinsurer help overcome some of the big company advantages? The following is a list of suggestions.'

1. Resources

2. Actuarial expertise. Reinsurance actuaries see a lot of different products from a lot of different companies, and while we respect the proprietary nature of products, we can share the ideas generated by them.

3. Underwriting. I will discuss the underwriting services that reinsurers can provide later.

4. Systems. We have a lot of information systems expertise and can help you with reinsurance administration using electronic transfer of reinsurance information. We can actually do your full reinsurance administration for you if you'd like.

5. Claims. We see a lot of claims. We can help you there, too. I'll talk about this in more detail later.

6. Access to capital. Reinsurance can help you with surplus relief and statutory strain relief. Especially with first-dollar-quote share, you basically end up ceding all the mortality risk to the reinsurer, and you become almost a super-agent. We pay you expense allowances that are similar to commissions. That helps you to make your profit stream much more stable.

7. Expenses. Kent was talking about the high expenses that small companies have. That's one thing that a reinsurer can help with. We can help the company reimburse some of your fixed expenses.

8. Large array of products. Many reinsurance companies have product development departments as part of the service they can provide. They provide turnkey products, term insurance, variable, and specialty products like long-term care, corporate-owned life insurance, bank-owned life insurance, simplified issue, and things like that. It is very, very cost effective for you to be able to take a product that has already been developed by a reinsurer and that has the appropriate mortality and lapse assumptions built in, and just run with it.

9. Diversity of risk. Reinsurers can help you stabilize the earnings by ceding the mortality risk. You can use either traditional excess reinsurance, which everyone is probably familiar with, where everything over your retention of $100,000, $250,000, or whatever is ceded to your reinsurer. Or the new idea is first-dollar quota share, where the reinsurer participates in a portion of every single policy. That can really help the bottom line.

10. Access to large markets. The reinsurer can almost act as a broker. It's not really fee-for-service. We have a lot of different clients. We can get you in contact with different marketing organizations to help sell your product. If you have a special niche product but you need to have a bigger salesforce to sell it, we might be able to find a client who doesn't have that product, but has the salesforce, and vice versa. If you have a good salesforce, but it is looking for a product that you don't have or aren't able to develop; perhaps, through an alliance with another company, or the direct sales side of a reinsurance company, we can help develop a product and have something available for your salesforce.

Let me give you a little more detail on what reinsurance can bring to the table. Most reinsurers will have a good life-underwriting guide (LUG). This is how you actually do the underwriting. Practically all reinsurers have their LUG in electronic form. It is something you can just load from a CD-ROM. You don't have to worry about three or four volumes of a hardbound underwriting guide. Electronic LUGs are very easy to update, either through CD-ROMs, diskettes, or even downloading from secure Web sites. If your reinsurer doesn't have an up-to-date guide, I think you should look for another reinsurer.

Reinsurers are also doing impaired risk research. They have a large underwriting staff and knowledgeable medical staff. They are constantly reviewing the medical journals to get the most up-to-date information to incorporate into their life underwriting guide, so that you can make the best possible offer to your applicants using our LUG.

Along with that, there's preferred risk research. Of course, that's a hot topic nowadays. How do you underwrite the preferred risk? How do you design preferred risk classes with the appropriate mortality assigned to them?

AUL has a specific service that helps you design a preferred-risk class, and along with that, decide what the mortality implications are of the risks in that class. We are actually starting to get some preferred mortality experience, which I will share with you a little bit later. But you should expect a reinsurer to be able to give you some advice on designing new underwriting classes.

A reinsurer should have a good staff of insurance physicians. AUL has three full-time medical insurance physicians to help underwriters with a particular impairment, or just to help with some problem that you have with a particular case. You can actually get advice and help from our medical directors. I don't think too many small companies actually have a medical director on staff.

Large case capacity. This might not be an issue for small companies, but if you have one case where you need $30-50 million of insurance, it helps to be able to call the reinsurer, and have him or her help to get that case placed. A world-class reinsurer will have a very large capacity available for its clients.

Reinsurers can also help to give you fast, competitive, facultative offers. It is not necessarily facultative because it's a large case. It's facultative because it's an impaired risk or there's something unusual about the case. Call up your reinsurer. Ask their advice. 'He or she has probably seen dozens of similar cases and he or she can give you good advice on how to underwrite the case.

When I talk about competitive offers, I mean a competitive but appropriate rating. It doesn't mean that we want to find a way to push the table rating to standard. We want to give you a good, appropriate offer.

Outsourcing of underwriting services. Some small companies let the reinsurer just do all the underwriting. Reinsurers can sometimes, on per-case fee arrangement, be your underwriting staff for you. This varies from reinsurer to reinsurer, and there are actually companies out there that do only underwriting. They're not even reinsurance companies. It's just a fee-for-service. But I suggest it's a good way to cut costs, once you get a good comfort level with how the service underwrites your business.

I like using the reinsurer to help underwrite because they are participating in the risk. They have a really good incentive to make appropriate calls.

What are some other resources? Let's look at this a bit. Reinsurers are (or need to be) experts in connectivity. Business to business is the new buzzword that you will be hearing among information systems professionals. AUL is one of the leaders in reinsurance administration. We like to call it paperless reinsurance. While we're probably not quite there yet, we do get reinsurance administration information electronically via tapes and diskettes. But it seems like there is always a paper copy sent as well. We're not quite paperless, but electronic transfer allows us to very quickly and accurately reinsure business from you. There are electronic funds transfers used to pay premiums and claims. You don't have to worry about cutting checks. You can just pay the reinsurer directly by electronic funds transfer.

We can also do your reinsurance administration for you. Send us a cut from your life system, and we'll put it through our reinsurance administrative system. We do the billing, give you periodic valuation reports, policy exhibits, and things like that. All reinsurers have this ability in some form. 'Ask them. That's one of the criteria I think you should be looking for as you choose among several reinsurers.

We do see a lot of claims and we have a lot of expertise. We should be able to give you some advice on contestable claims. We can tell you whether we think this is one that you can contest or one that you need to go ahead and pay.

Fraudulent claims expertise. Like I said before, reinsurers see a lot of claims. We see a lot of different fraudulent situations, and we can give you advice on how you might handle these cases.

Education. This can take the form of a seminar on a specific underwriting or actuarial topic. Or it could be a simple claims and administration audit. We can verify that your claims or administrative staff is doing an accurate and professional job.

Access to capital/surplus relief. We can, through financial or traditional assumptive reinsurance, unlock the profits from a block of business. How does reinsuring a block help get some immediate capital? If you're in a capital-poor situation, sometimes getting all those future profits up-front can help alleviate the situation, and reinsurance is there for you.

Statutory strain. Usually you get a 100% first-year coinsurance allowance, and that's used to reimburse you for the underwriting and set-up costs that the reinsurer doesn't have that you have. I've actually participated and quoted using greater than 100% of the first-year allowance. Oftentimes, your first-year expenses exceed the gross first-year premium, and a coinsurance allowance of 125% or 130%, which might be unusual, is not out of the question. Ask your reinsurer about it. The overall price is going to remain the same and the renewals will be a little lower, but it allows you to help overcome the surplus strain from selling new business.

Stabilizing earnings using reinsurance. Obviously, you are ceding the excess mortality, and as a big claim comes in, you' have some reinsurance there to reimburse it. Some people cringe at the term locking in profitability. Sometimes you'll hear that, and here's what that really means. With first-dollar quota share, it

means the reinsurer is participating in every single policy. You can retain 5-10% of each risk; a reinsurer or pool of reinsurers takes 90% of the risk. Locking in profits means you're replacing a larger unstable stream of profits with a slightly smaller, very, stable stream of profits. Basically, the coinsurance allowances become like a commission for you. For a small company, a little variance can mean a great deal to its bottom line. Stabilizing earnings becomes very important. Reinsurance is good for that.

Actuarial resources. We can help in product development of products like: term, variable, specialty products like long-term care, simplified issue, corporate-owned life insurance, and things like that. Reinsurers can give you advice on things like mortality/lapse assumptions, help in filing, and things of that nature. Many reinsurers have turnkey products. It's like, Here you go, all filed, ready to go. That has a lot of appeal to it from the small company perspective.

Valuation. I think I only need to say one or two words. X factors. XXX is a big deal. A small company just does not have the mortality experience to know what the appropriate X factors are. Reinsurers see billions of dollars of life insurance and have a good handle on mortality assumptions. This goes a long way into calculating the appropriate X-factors for valuation and pricing.

Underwriting classes have changed dramatically in just the past few years. Right now we are working on mortality assumptions. The X-factors are simply reproducing, with a margin, what is in the product pricing. The experience is going to come out in the future. The other place the reinsurer can help you is with mortality experience studies. Obviously, with a small company, credibility becomes an issue. A reinsurer can pool together many of their similar clients with similar underwriting and similar products and provide you with a credible experience study to show the regulators so you can validate your X factors.

The mortality research that reinsurers do becomes a very important part of this. The studies that AUL does are on a company-by-company basis for all of our clients. We actually have a history of mortality experience that we can share. We respect the proprietary nature of mortality experience at the individual client company level, but we feel that we can share aggregate studies with all our clients. We also share each client's own reinsurance experience with that particular client.

I want to talk about a preferred mortality system that AUL has developed to help us decide appropriate mortality assumptions for preferred risk classes. This actually links to the appropriate X factors you're going to use when you try to do XXX valuation and pricing for these classes.

What is this system? This is not going to be a presentation on how to calculate preferred risk mortality, but simply to show you what the system is, give you a little feel for what we can do, or what you should expect other reinsurers to be able to do. It's a system for analyzing and predicting mortality for preferred risk underwriting classes.

Now, how do we do that? It's actually a two-part system. The first part uses a very large unbiased database. I'll get into what that word means in the context of insurable risks. It is used to determine how many people would theoretically qualify for a given preferred-risk class. We look at people with certain cholesterol, a certain HDL ratio, a certain blood pressure, and the risk factors we are all familiar with.

You need to find out what percentage of the insurable population would theoretically qualify for a preferred class, not what percentage is actually placed in the class. A phenomena that goes on, particularly in the brokerage market, is placing a lot more of your preferred and super-preferred risks than residual standard risks. People like to be preferred, and if they're not, they either end up not buying insurance with you, not buying insurance at all, or going to the direct-mail market.

I've actually had clients with very strict preferred criteria, where 65–70% of their business is placed in that class. That's because the brokers know that if it's a super-preferred client, they should go to Company XYZ because it has the best rate for that class. You need to look at an unbiased database to determine theoretical qualifying percentages.

We get that from the labs. In fact, we have over 7,000 records, a random sample, that Lab One has sent us. We believe it comes from many different companies. That helps remove a large part of the agent field selection from the process. It gives us an idea of how many people would theoretically qualify for various preferred risk classes.

Once we' have the qualifying percentage, we have a theory that relates the qualifying percentage to the mortality improvement that you get from the class. You would expect that the fewer that theoretically qualify, the better the mortality improvement. That's exactly what happens. I actually have some experience that I will show you on how the theory has been proved to model what is really going on.

Once we have an unbiased qualifying percentage, we need to consider the impact of agent field selection. I use that term to describe how it can be done. First, the broker decides which applications to send to which companies. He's actually out there saying, "I know your cholesterol, and I know your rate ratio. Company ABC has the best rate for you." Or "Oh, you're just going to miss that one company's standards. I have another company, XYZ, that might work better for you." This really goes on. There's a very efficient market for preferred-risk cases in the industry today, and that really happens.

The second part of agent field selection is the fact that you start to go through the underwriting process, and the agent says, "Don't worry, you're in superpreferred." The agent comes back and says, "You just missed superpreferred, so you're going to have to pay the higher premium for the residual preferred." That's when the broker says the same thing. "I've got another company, and their premium is pretty comparable to the superpreferred, but I think you can get into that class. You just missed it at Company ABC, but I can get you into Company XYZ." The broker can compare the preferred criteria of many different companies.

As part of that, there's another effect that I call the migration effect. That's where people who just miss qualifying for your superpreferred class will not take your residual preferred. The mortality from those people is extracted from your experience. You never place a policy with those better risks. Actually the mortality from the people you do place in your residual preferred is a little worse. You actually sliced out and lost a little bit of the better mortality. AUL's preferred-risk system can actually take that into account. It can slightly increase the expected mortality in the residual preferred, and even in the residual standard class, through this effect.

Let's do a quick example. I'd like to discuss the database portion of the system. I can put in as many queries as I want to define my preferred-risk class. The first column (labelled "One") of the PriMA™ Preferred Risk DataBase Analyzer, Table 6 shows nontobacco using males between 18 and 40. What's my class? You have a build table for height and weight, and the person is' 111% of what might be considered average from the SOA Build Study from 1979. He has cholesterol of 240 or less, and an HDL ratio of 5 or under. It's basically a knockout system. You have to have the build, the cholesterol, HDL ratio, and good blood pressure (135 over 85) to get into the class.

What is the system doing? It's saying that I have out of my database of almost 7,000 people, 1,272 male nonsmokers between 18 and 40, of which 512 have these characteristics. What it's saying is, for this group of individuals, 40% will theoretically qualify for this class.

You can go on" and look at males between the ages of 40 and 60 and males between the ages of 60 and 80, and do the same thing. The reason it is set up this way is many companies have different criteria for different ages. Blood pressure can change, sometimes cholesterol can change, and obviously build can change.

What I'm saying is that for this superpreferred sample life (and this doesn't represent anybody in particular, I just picked some numbers as a good example), this class has, on average, about 26.5% of the insurable population of standard risks (not impaired) qualifying for this class.

Another thing that makes sense is, as I get older, fewer and fewer people qualify. It makes sense that the younger groups get more people to theoretically qualify for the preferred risk class. The relative weight adjustment allows you to re-weight these columns to more appropriately match the age distribution from your company. About 26.5% will qualify for this particular superpreferred class.

Table 6 of The PriMA™ Preferred Risk Mortality Analyzer is the preferred class of that same product. What this is actually doing is taking two independent queries. It takes a query of preferred (and better) and extracts a query of the superpreferred and what you have left is the residual preferred.

TABLE 6

PRIMA ™ PREFERRED RISK MORTALITY ANALYZER						
SAMPLE LIFE	Parameters By Class					
Nontobacco		**Super**	**Pref NT**		**Std NT**	**Total**
Unbiased Proportion	0.0%	26.5%	31.0%	0.0%	42.5%	100.0%
Agent Field Selection Ratio	1.000	1.000	0.750	1.000	0.250	
Migration Factor		0.000	0.150	0.000	0.300	
Improvement Percentage	N/A	29.3%	3.8%	N/A	-27.7%	9.5%
Base Mortality	N/A	100.0%	100.0%	N/A	100.0%	100.0%
Placed Mortality	N/A	70.7%	96.2%	N/A	127.7%	90.5%
Placed Proportion	N/A	43.9%	38.5%	N/A	17.6%	100.0%

Source: American United Life Insurance Company

Column "One" has the same 1,272 male nonsmokers between 18 and 40 in the PriMA™ Preferred Risk Mortality Analyzer. Some 909 will qualify for preferred or better, but remember that 512 have already qualified for superpreferred. What do I have? I have 909 minus 512 divided by 1,272, which gives me 31% that would qualify for the preferred class. You do that for all the various age groupings, and you come up with about 30% qualifying for this class.

How do we put all this together? This is phase two. This is a fully scalable model. What we're trying to get to is, what is the anticipated mortality improvement from the superpreferred, the residual preferred, and the residual standard classes? I just use a base of 100%. It can be whatever mortality you think the old traditional standard class (not the residual standard class) had.

The database shows that the unbiased qualifying percentage for superpreferred would be about 26.5%, about 31% for preferred, and everybody else falls into residual standard. What you can see here is an example of agent field selection. What is happening is you are placing 100% of the people who theoretically qualify for your best class. You're only placing about 75% of preferred, and 25% of the residual standards. This really happens. I have actual data from brokerage term companies where this happens.

What you can see is, 26.5% will theoretically qualify for your superpreferred class, but you end up placing 44% of your business in that class. It doesn't mean your pricing is wrong. It just means you place more into the superpreferred class, but the mortality is right.

What happens is you have 26.5% qualifying for superpreferred and the theory is telling you that the mortality reduction is almost 30%. The mortality that you get to use in your pricing is 30% less than the old standard. Likewise, for residual preferred,

mortality is just a little bit better or about 4% less. This is because you've already taken out the superpreferred.

A good way of looking at that is (Chart 2 The Standard Class). This represents the normal distribution of the standard class. The dark gray on the left is your super-preferred class. The patterned gray area represents that migration effect that I was telling you about that you couldn't ever place people in here. These people are gone. They are gone to some other company; you aren't placing those. The medium gray (middle) represents the mortality of the businesses placed in that class. The same thing goes for the light gray (right) for the standard non-tobacco risks.

What this is showing is that we are using a mortality assumption of about 70% of standard for your super-preferred, about 96% for the residual preferred, and about 127% for the residual standard.

An interesting thing, you'll notice, is that the placed mortality ratios don't add up to 100. Why is that? Well, because we're not placing all the risks. This is a case where, If you were doing a mortality study, and saw that your actual-to-expected ratio was 90%, you might want tell management that you're doing a wonderful job with the pricing. That's not necessarily true. You need to do your mortality studies by class. Because what is happening is, you've thrown out some of these poor risks. This is 90.5% because you're placing more of the better risks. Actually, you may be right on target for mortality and not 10% under.

I actually have some real experience here that helps validate AUL's preferred risk mortality theory. My first experience study was done before superpreferred really came into the market. There were a couple of companies in the study that had a superpreferred class, and I added those risks to the preferred class. We're really looking at preferred and residual standard, which are two separate classes, and nontobacco only. You would be surprised by how few smokers get insurance. I don't know where they are going to get their insurance. Less than 10–15% of our risks are smokers. I know there are more smokers in the U.S. than that.

I'm looking at 1992–98 issues of term insurance because the data I'm getting are from first-dollar quota share reinsurance of term. AUL is specializing in term reinsurance right now because that's just where the volumes are. I'm also looking at 1992–98 claims. I'm looking at very modern data.

I picked ten companies, whose preferred classes were similar enough that I felt I could aggregate the business. Their theoretical, unbiased, qualified percentages were about the same. For this example, that class had about 65% theoretically qualifying. With 65% theoretically qualifying, I think I ended up with a placed percentage of about 75% because of the agent field selection. These are very credible numbers. I have $108 billion of net amount at risk exposed over 1992–98 and about $77.6 million worth of claims.

As a reasonability check, we can do some long division and get a crude mortality rate of about $0.72 a thousand. You're probably looking at the third or fourth duration.

The average issue age might be around 40, and for that age, that's a reasonable number. That's just a reasonability check and nothing more at this point.

Now let's discuss some real numbers. Once again, for the superpreferred for the couple of companies that had this class, I added the preferred and better classes together. All these ratios are based on the SOA 1975-80 Basic Tables. I can give you real numbers to look at.

Total experience for nontobacco users in the 1990's was about 42.6% of the 1975–80 Basic Tables. How was that divvied up between the classes? For preferred, the ratio was about 39.1%, and for standard nontobacco the ratio was about 55.2%. Of course, the real test is, how do these actual results relate to theory? This is what the AUL theory predicts.

Do you remember I told you that the AUL system was totally scaleable? Scaleable means you have to find where you are going to put the standard normal curve along the mortality horizon. 'I have some experience, so let's peg it. Let's scale the standard curve at 42.6% placed mortality and 'see what the AUL theory predicts for preferred.

What this is showing is that we have a really good handle on preferred mortality. The database is doing a good job at deciding how many will theoretically qualify for a class. The mortality theory has the shape and position of the normal mortality curve doing a good job of dividing up the mortality among the preferred classes.

I feel pretty good, as a pricing actuary, about using these kinds of mortalities in my pricing. For years, we heard from our clients that they just didn't believe the spectacular mortality improvements that you get from preferred. It really happens.

I recently (and this is very fresh) have started to get some superpreferred mortality experience. I did a quick-and-dirty policy year/policy count study that was completed just last month. There were superpreferred, preferred, and residual classes for nontobacco for only three years. Calendar year 1997 was really the first year in which a good modern superpreferred class was available for me to look at as a reinsurer.

What I was getting was a superpreferred class where approximately 35% would theoretically qualify. For the residual preferred, approximately 35% would qualify. The remainder was in the residual nontobacco. For policies issued during 1997-99 and for claims of 1997-99, I had 695,000 policy years of exposure, and there were 338 claims. In aggregate, you get some fairly credible numbers, recognizing we're still within the first three years, but it gives us an indication.

Once again, doing a reasonability check, we get a crude mortality rate of about $0.49 per thousand, which makes sense. The $0.72 per thousand we had before was probably something three or four years old. We're probably in the first couple of durations here. Obviously, there can't be anything older than three years.

We have a policy count study, three years worth of data, and the SOA 1975-80 Basic Tables as the base. The total ratio is 35.9%. Remember, the old number was 42.6%. Don't quickly jump on that fact and say, "My gosh, look at the incredible mortality improvement over five years." Remember you placed more super-preferreds. Some of this is secular improvement, but most of it is the fact that you are placing a lot more super-preferreds.

Superpreferred mortality is about 27% in the 1975-80 Basic Tables. That's just an incredible result. Let's see what was predicted by the theory.

Once again, the system is scalable, so I peg the super-preferred and see how the other classes come out using the theory. They came out pretty well. Once again, I think the database is doing a terrific job of dividing up three classes of nontobacco users. In a couple more years, I'll be able to add a super-duper preferred on top of that, and we'll be able to do four nontobacco classes. It does a really good job of coming up with mortality expectations, so I use this in the pricing.

What have we learned? I hope we have learned that a small company can compete, regardless of what Mr. Benson said at the general session. I think you can. How can you compete? Use your reinsurers. What do they have? They have (1) access to resources and expertise; (2) access to capital, either by quota share or surplus relief; (3) access to products, e.g., turnkey, term, variable, or marketing alliances); (4) access to markets; and (5) risk transfer to stabilize your earnings.

Mr. Eddie A. Mire: I have a question concerning the overhead expense study. It seems as though the smaller companies have more efficient overhead expenses than the larger companies. That would seem to fly in the face of all of our anecdotal evidence over the years. Is that true? Have you all wrestled with that question and do you feel that's comfortable and correct?

Mr. Scheiwe: I think we've wrestled with it. I think we have to be careful how we express these statements. It's expressed on a per-policy basis. I think the small companies look better than expected, because of the number of small policies the smaller companies have. That's the way that I interpret this study.

Overall, on a percentage basis, I think the small companies are competing with the large companies. That's just a fact from their annual statement.

Mr. Mire: That's very good news, but just seems to be contradictory to what we've always taught.

Mr. Scheiwe: I've tried to explain it. One explanation to it is all the recent large expenses that the larger companies have been having. That's the only thing I can come up with. Maybe the large companies are having just abnormal expenses through this period. I think that's a weak excuse, but I don't have any other explanation.

Mr. Gregory L. Fitzmaurice: Janice, you mentioned that if the mortality experience were not on the level for which we would price, you would go back and adjust the assumptions. I'm wondering whether that's wise, and whether or not you shouldn't go to the sages of the field underwriting, and say, "Listen, we need to tie up with field underwriting instead." How do you decide which way to go with this stuff?

Ms. Duff: First, we want to really determine if there is a trend or if there is some abnormality. For instance, in our final expense market, we noticed that we were having high claims and we were able to point it directly to, quite frankly, some poor agents that were giving us bad business. If we had overreacted at that point, and changed the product, we would have then been going down the wrong track. We do have to evaluate it.

Mr. R. Dale Hall: My question is for Dave. The reinsurer, I guess, typically enters into a product development engagement with the hopes of gaining a percentage of the pool down the road. How do you deal with the situation when allowances derived in the product development process are out of the market when you take it to other reinsurers to fill out the pool?

Mr. Wylde: I guess you can decide to spread the amount to the reinsurers who can step up to the plate. Each reinsurer has its own profit margins. I think that's where the negotiating skills come in. It depends on how much they want your business. It might not be viable for them. Saying, "Look, I've got these allowances from reinsurer XYZ. Do you want a piece or not?,"' is a good negotiating technique. """I run into that all the time, and there are many occasions where I have to say, "Those are great allowances. You should go with that." Because I don't know how they're getting there. I've got my mortality assumptions and profit margins.

Mr. Hall: Does the reinsurer doing the product development typically require a certain percentage?

Mr. Wylde: Yes, I have seen that. That can vary a lot. Some require 50%. Some are lower, but they're making their money off the reinsurance. You definitely should expect that.

Mr. Mire: Of all the quotes that you give out, how many are finally accepted?

Mr. Wylde: That's going to vary a lot for each reinsurer. I think right now, it's a very competitive insurance market. I'll bet 25% of AUL's quotes are accepted. That's new opportunities. We have a fairly stable base of current clients with whom we maintain relationships. Breaking into a new company is extremely difficult.

A reinsurer has to be outstanding in some fashion, and usually that's low cost. That's how you break in. Value added is a tough thing. The profit margins for companies are so tight nowadays. That's why I've told you what reinsurers can do, but oftentimes, it comes down to the bottom line. Best price gets the business.

From the Floor: You talked a lot about finding your niche. I wonder if companies are marketing some of their other services, like administrative services or investment services, as another source of profit to cut expenses. What have you seen out there away from the product?

Mr. Wylde: Do you mean like a fee for service? A strict fee basis?

From the Floor: Yes. It could be on an administrative system. Investments would be the other place.

Ms. Duff: We are acting as a third-party administrator for another company. Actually, it's the final expense product again. We had developed it, they liked our product, they wanted to put it on their paper, but they knew that we had the cost efficiencies in place to administer it. It does happen.

Mr. Scheiwe: We have clients wanting to administer the business, but not necessarily take the risk. I think it's a small company dilemma; they want to administer it as much as possible, and in that way, it is more efficient on a per-policy basis with administration. I see quite a few of my clients doing that.

Mr. Timothy W. Verschelden: I have a question on your expense study. You listed your variable expenses with different components, per unit, per policy, or by percentage of premium. But then, when you reported your overhead expenses, you report them as a percentage of premium and per policy. Is the total overhead the sum of those two, or are those two expressions of the same total?

Mr. Scheiwe: The percentage that was stated, 25%, was a percentage of the total premium, and that represented just the overhead expense.

Mr. Verschelden: But that's total overhead expense?

Mr. Scheiwe: Right.

Mr. Verschelden: You weren't breaking overhead expenses into separate components?

Mr. Scheiwe: There was no breaking.

Mr. Verschelden: I guess that makes me question the other comparisons later on when we' compared that to the variable expenses.

Mr. Scheiwe: You're asking why I'm comparing overhead expense to the variable expense, and how I get 200% ratios?

Mr. Verschelden: When we take the total overhead expenses, is it just overhead expenses as compared to the variable percentage of premium expenses? Is that what you're doing?

Mr. Scheiwe: I think it's dollar amount. Then you're talking about the overhead expense, which is $500,000; take that ratio. ''

Lotus 1-2-3 Release 5 - [PRIDA12B.WK4]

File Edit View Style Tools Range Window Help Special

CHART 1

PRiMA™ PREFERRED RISK DATABASE ANALYZER

SAMPLE LIFE Preferred Nontobacco				Enter Up To Eight Queries To Uniquely Define A Preferred Risk Class							
				ONE	TWO	THREE	FOUR	FIVE	SIX	SEVEN	EIGHT
DEFINITION OF BASE	Relative Weight for Query			1.210	1.509	0.574					
	Nicotine	T, N, or A		N	N	N					
	Sex	M, F, or U		M	M	M					
	Age	Low (>=age)		18	40	60					
		High (<age)		40	60	80					
INPUT RANGE OF VALUES FOR CRITERIA	Build	Low (<=pct)		111.0%	109.0%	109.0%					
		High (<=pct)		122.0%	119.0%	119.0%					
	Cholesterol	Low (<=chol)		240	240	240					
		High (<=chol)		280	280	280					
	HDL Ratio	Low (<=ratio)		5.00	5.00	5.00					
		High (<=ratio)		6.50	6.50	6.50					
	Systolic BP	Low (<=sys)		135	135	135					
		High (<=sys)		140	140	140					
	Diastolic BP	Low (<=dia)		85	85	85					
		High (<=dia)		90	90	90					
DATABASE QUERY RESULTS	Base Hits		4032	1272	1525	334					
	Low Hits		1175	512	350	47					
	High Hits		2419	909	815	156					
	Pct of Base		30.9%	31.2%	30.5%	32.6%					
	Distribution		100.0%	38.6%	56.4%	5.0%					
WTD AVG VALUES BY CRITERA	Age		43.1	32.8	48.2	65.9					
	Build		106.4%	108.7%	105.5%	99.3%					
	Cholesterol		205.6	202.1	208.4	201.7					
	HDL Ratio		4.80	4.84	4.77	4.77					
	Systolic BP		124.1	121.5	125.5	128.8					
	Diastolic BP		78.3	76.7	79.4	77.0					
DATABASE INFORMATION	File [c:\123files\prima\prida12b.wk4] last updated on 10/29/99 *** LabOne Data ***										
	Total Records (6823) Nontobacco (5860) Tobacco (963) Male (4326) Female (2497)										

CHART 2