

act shape of such a program is not apparent at this moment, but its development would seem to require the application of much time and thought which might be forthcoming from some generous and well-staffed company or a full-time actuary in a rating organization or some combination of the two. Certainly any line of business that is already producing close to half a billion dollars in annual premium, and is still growing, deserves the benefit of all the actuarial talent it can get.

PREMIUMS AND RESERVES ON NON-CANCELLABLE AND GUARANTEED RENEWABLE A & S POLICIES

(SUMMATION BY JOHN H. MILLER, VICE PRESIDENT AND
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I feel some diffidence in bringing you from the esoteric realms of negative binomials and Poisson distributions to the very pedestrian business of health and accident insurance. I had always thought that Poisson distribution referred to some method of merchandising fish, so I see that I'm going to have to get a little further education on the subject.

Mr. Barber's mention of accident proneness in respect to automobile insurance reminded me of the old chestnut I'm sure you've all heard; but it describes, I think, better than anything else the problems of health insurance. That is, the statement that to collect on a life insurance policy you must die; to collect on an accident insurance policy you must have an accident; to collect on a health insurance policy you must have a policy.

In connection with the auto merit rating plans, something was said about off-balance which is a perpetual state of the health insurance company. There are two general categories of companies in this business; there are those which consistently make a profit, perhaps a nominal one, and are severely castigated for gouging the public and then there is the other class that consistently loses money and they are severely castigated by their stockholders and critics in general for not knowing how to run their business. So you see you just can't win!

In our seminar yesterday there was some discussion of the federal income tax. The new life insurance tax law affects many companies—not only as to the tax on their health and accident insurance but also as to the classification of the company. As I think most of you know, the definition of life insurance reserves in the Federal tax law includes not only life insurance but non-cancellable insurance and adjustable premium guaranteed renewable health and accident insurance. There are companies which write no life insurance at all that are classified as life insurance companies for tax purposes because their reserves on these types of health and accident insurance with renewable guarantees are more than half of their total reserves. If they don't meet that test then they're taxed as stock or mutuals as the case may be, so that health and accident business may be taxed in different ways according to the way the company writing the business is classified.

The title of this seminar gave a little trouble. I was asked if it was correct.

The title is "Premiums and Reserves on Non-Cancellable and Guaranteed Renewable A & S Policies," which brings up the matter of definition of non-cancellable—a question that was debated not without some rancor and contention among opposing groups of companies and finally resolved by the NAIC which said that the term "non-cancellable" could be used either alone or in conjunction with "guaranteed renewable" if the policy was not only non-cancellable and guaranteed renewable but also provided a guaranteed rate. The reason for that primarily was that for 30 or 40 years the term non-cancellable had been associated with a guaranteed premium. The NAIC also recognized the use of the term "guaranteed renewable" qualified by the words "adjustable premium" to recognize policies which reserve to the insurer the right to adjust the rate on a class basis only, but otherwise had the attributes of non-cancellable insurance. So to be perfectly accurate the title should have read "Premiums and Reserves on Non-Cancellable or Non-Cancellable and Guaranteed Renewable Policies and on Adjustable Premium Guaranteed Renewable Policies." But that sounded too much like the title of a 17th century novel and without an explanatory comment the average reader not familiar with this controversy would have felt that the person preparing the program didn't know what he was talking about, so I took the simple measure of replying that I thought the title was just fine.

There was some discussion in the seminar on the annual statement requirements. Traditionally the non-cancellable policies have required, in addition to the pro rata unearned premium reserve, the so-called additional reserve, generally computed as a mid-terminal level premium reserve either on a full preliminary term or net level basis; but in the Task Force 4 recommendations, which were adopted by the NAIC, a little more flexibility was permitted and companies now can combine the pro rata unearned premiums with the additional reserve and set it up on a basis comparable to life insurance or on a basis that's roughly midway between.

Then there was considerable interest in the computation of gross premiums. Here with the increasing development of level premiums for life or level premiums to 65 with a step rate or adjustment at that point, we find quite a departure from traditional or customary fire and casualty procedure. We have a continuous policy, a level premium coupled with a risk cost that usually increases with age, and an expense cost that usually decreases, particularly when non-level commissions are used. With this combination you have a situation more akin to life insurance, particularly long-term life insurance, than to any other form of insurance and it's necessary to bring in mortality, interest and the rate of lapse.

Sources of morbidity rates were discussed, or mainly the lack of sources because there is not a great deal that is presently available. A committee of the Society of Actuaries has been assembling data on disability insurance experience, but thus far the data have not been sufficient in volume, homogeneity or maturity to warrant the development of a new table.

The Task Force 4 report on reserves included tables for hospital and surgical costs. Other papers on individual company experience giving some data on major medical expense insurance have been published and are being used for premium and reserve computations.

With the recent development and emphasis of benefits for hospital and medical expense, an additional contingency was added to the problem of evaluating the cost of future benefits, namely the cost index of medical care. This has led to the development of the adjustable premium guaranteed renewable policy under which the insurer guarantees the continuance of the policy subject to the timely payment of premiums which can be adjusted in the future on a class basis to recognize changes in the price level as well as other changes in the underlying assumptions.

In accepting the Task Force 4's report the NAIC did it with the stipulation that any company choosing to write an adjustable premium guaranteed renewable health policy should maintain fund accounts of each form of policy so that if the time came when the company wished to raise the rates on existing policies because of adverse experience, there would be a historical basis of a fund account to justify that request. Thus, the obligation a company assumes in issuing an adjustable premium guarantee renewable policy is not only that of attempting to determine an adequate rate and maintaining proper reserves but also of keeping a fund account, so that if the initial assumptions prove to be inadequate or if cost of services requires an increase in rate, the company will have something to point to in justification of its revised rates.

Finally, I would like to comment on the new development of an automobile policy containing certain renewal guarantees and suggest the parallels between that and the health and accident policies with renewal guarantees, which may now be defined as non-cancellable or as adjustable premium guaranteed renewable policies, depending on whether the premium is or is not guaranteed. I think there are many parallels with respect to definition, nomenclature, advertising, and also in the principles and practices of ratemaking and maintenance of reserves.

REPORTS OF THE SEMINARS HELD IN WASHINGTON, D. C.
AT THE 1960 ANNUAL MEETING OF THE SOCIETY
AUTOMOBILE MERIT RATING

(Summation by Thomas O. Carlson, Manager, Southeastern Branch,
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I stand before you as an innocent victim of a mouse-trapping Society Vice President who asked me to conduct a seminar on developments in Automobile Merit Rating, saying that there would be a number of papers to carry the session and I would only have to referee the bout. The word "only" was the mouse-trap. When I saw the first papers, deep-fried in a batter of hypergeometric foundation overlaid with negative binomials and coefficients of variation, I hastily reviewed my dues-paying status in the Society in the same frame of mind as the chap down in my new "Yo'-all" neck of the woods who came into the City Hall one morning to inquire whether his marriage license had not already expired. I suggested, when the Vice President cruelly refused to unspring the trap, that all members should be forewarned that this was to be a discussion taking off from a springboard of theory rather than practice, but he felt that the papers distributed in advance of the meeting