PANEL DISCUSSION — NOVEMBER 1962 MEETING

RATEMAKING IN THE FUTURE

CHAIRMAN: HUBERT W. YOUNT

RATEMAKING AND PRICING IN THE MARKETPLACE

BY: HAROLD E. CURRY

This topic invites reflection and encourages speculation. It has caused me to look back over the more than three decades I have been involved in ratemaking, compare current ratemaking techniques with those prevailing in the earlier years of this span of time and project this historical background into the probable future developments in ratemaking.

These musings suggest the conclusion that the role of the actuary has been undergoing a change, a change that should be of interest to all of us in the actuarial profession now and to those contemplating actuarial work as a business career. These changes are of significance to those of us charged with the task of selecting and training new men for future actuarial responsibility in the organizations which we are associated with as they may have an appreciable impact on the future development of this Society.

My acquaintance with ratemaking started in 1929 and involved only automobile insurance, the line that has been my major interest during the intervening years. At that time the prevailing rating systems were quite simple in comparison to those in use today. Ratemaking was sort of a semi-accounting which involved the totalling of earned premium and incurred losses, using few if any breakdowns insofar as rating territories, type and classification are concerned and adjusting rates up or down to some permissible loss ratio. Many companies even avoided this task thru affiliation with established rating organizations or by maintaining rate schedules bearing some fixed relationship to those promulgated by the national rating organizations. Rates were not subject to approval by state regulatory authorities, the purchase of such insurance was a somewhat casual transaction involving nominal sums and generally limited to those individuals or corporations with substantial assets subject to pursuit for indemnity in the event of accident involvement.

In such a market atmosphere it was not uncommon to find the actuary occupying a rather secondary place in a company's organization chart. In fact, a great many companies did not even have an employee so titled! A reasonable understanding of basic statistical methods and reasonable college training in mathematics were the essentials an individual needed to do a creditable actuarial job. There was one exception among the casualty insurance lines, workmen's compensation, where more advanced ratemaking techniques were being used in any appreciable degree. The actuary was accorded reasonable respect by company management but dubbed a mathe-

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Editor's Note: The Panel Chaired by Mr. Hubert W. Yount included Mr. William Leslie, Jr., Establishing Net Rates Including Expenses; Mr. Seymour E. Smith, Multiple Peril Ratemaking and Statistical Problems; Mr. Joseph M. Muir, Problems in Rating Organizations; Mr. Harold E. Curry, Ratemaking and Pricing in the Marketplace; and Mr. James B. Donovan, Regulation of Ratemaking. Panelists' remarks were completely off-the-record. Mr. Leslie and Mr. Donovan chose not to reduce their remarks to writing. Mr. Smith, Mr. Muir and Mr. Curry edited their own remarks.

matical nut by production personnel and a person to be tolerated but who, obviously, knew nothing about marketing.

This portrayal may be distorted slightly but in those days the actuary did, too often, content himself with a narrow and conservative interpretation of the statistical data available and made a very meager attempt to evaluate the attitudes of the buying public with respect to price or scope of coverage offered.

This attitude toward the actuary continued into the middle 1930's. In the interim, we had been enduring a depression. Many companies had undergone severe retrenchment programs, were struggling to maintain income levels and had developed a sensitivity to prices and quality of product and service. The actuary was consulted more frequently for ideas to aid sales but at the same time safeguard the financial stability of the company. This tended to force the actuary out of his statistical shell and into consideration of the factors that would improve the saleability of the product. The caution born of depression stimulated public interest in insurance protection and, in the automobile line, the enactment of financial responsibility laws tended to add some compulsion to the purchase of insurance.

To the best of my recollection it was in the years immediately following when the actuary started to be recognized as a human being capable of taking diverse statistical facts and ideas and fitting them together to form a workable operating pattern. The more aggressive companies with established actuarial departments started to enlarge these staffs and many companies with no such facility began to shop for actuarial talent or diverted personnel with mathematical ability from other activities to a ratemaking function.

The advent of World War II arrested this development but, in a way, stimulated interest in the actuarial profession. Modern warfare depends heavily on mathematics for successful execution. Actuaries were found to be valuable in many phases of war. Individuals with an aptitude for mathematics discovered, for the first time, the opportunities in our profession.

Two events that occurred shortly after the end of World War II (1) the S.E.U.A. decision and the subsequent enactment of rate regulatory legislation and (2) a tremendous upward surge in automobile use and ownership created a big demand for actuarial talent that could accurately interpret the ever increasing volume of statistical data and, of equal importance, devise rating systems and policy products that would attract sales and still be acceptable to the state regulatory authorities.

There were market stimuli that have tended to increase the demand for actuarial talent such as:

1. More stringent safety responsibility laws.
2. The conviction on the part of many company managements that the automobile line is the key contact for other personal insurance needed by every family.
3. A public demand for new forms of coverage, extension of existing forms, and rating systems that differentiate between risk groups presenting differences in exposure.

All of these factors lumped together are resulting in a change in the stature of the actuary in relation to other segments of company management and even in the personality traits management desires in the actuarial talent they employ.

In past periods there was a tendency to evaluate talent by the single criteria of the depth of his mathematical and statistical knowledge. Little attention was given to his personal appearance, his ability to express himself clearly to a non-technical audience, his knowledge of market conditions, or training in business management.

The actuary today must be more versatile than formerly. Interest in his mathematical and statistical skills has not diminished and these skills are the basic tools of the actuarial profession. In addition he must be able to present his rating conclusions persuasively to company management and to state regulatory authorities (and not infrequently to representatives of the buying public), he must be sensitive to market needs, he must be capable of explaining rating changes to sales people not only to improve understanding but also to expose salient sales aids, he must develop some method of direct contact with the buying public so he can spot weaknesses in the rating system used or breadth of coverage afforded, he must counsel with the underwriting and claims departments in matters of risk selection and policy interpretation and, above all else, he must sponsor rating systems and rate schedules that will result in a profitable operation and be workable in the complex electronic equipment so widely used today. Simply stated, the actuary today is an important part of the total management team. The actuary can no longer deal a fatal blow to an idea by terming it "actuarially unsound" or "discriminatory." He must take basic ideas that are attractive to the buying public and build a rating program that is sound and equitable. In the final analysis, as a part of the management team, he is just as interested as anyone in a profitable operation for his organization, perhaps even more so because his professional competence is at stake.

Rating systems must be such that the buying public accept them as reasonable. The price charged must be one the buying public is willing and can afford to pay. If either the system or the price is not compatible with the buying public's concepts of reasonableness and equity the entire operation will fail to succeed. Therefore, it seems to me that the ultimate test of sound ratemaking is the marketplace. No amount of regulation of ratemaking by state authorities can be an effective substitute for public acceptance. It can *aid* or *impede* the company's response to a market need depending upon the attitude taken.

I have long been chagrined about the quantity of casualty and fire actuaries who attain top company management positions in comparison to the life insurance industry. In this latter branch of the insurance business we find many company presidents who are actuaries by profession whereas in the casualty and fire lines very few company presidents have come up over the actuarial route. I sincerely hope this picture will become more balanced during the lifetime of the younger members of this Society, at least.

As to the future, I believe we have a long ways to go in developing rating systems that are properly sensitive to market needs. Under our American competitive system these deficiencies can be overcome. A lion's share of the responsibility to make this an accomplished fact rests upon the ingenuity and competence of the members of the actuarial profession.