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A LOOK AHEAD

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Introduction

"Nothing endures but change"

— Heraclitus (540-480 B.C.)

Scientific information today has a half-life of less than ten years. This means that in less than ten years, half of today's scientific knowledge will be obsolete. The same is true of business knowledge to a lesser degree. In the insurance industry, ideas, information and attitudes are changing even though insurance is a tradition-bound business, usually slow to innovate and often hampered by uninspired and politically oriented regulation.

Diversification

In a bygone industrial era, an individual human need was met by one, or sometimes several competing specialized American business enterprises. The continuation of each enterprise depended on the degree of efficiency with which it operated but there was no intent that each enterprise should serve all of man's needs. However, today's American business environment emphasizes diversified growth through affiliates, subsidiaries and holding companies to form conglomerates and other large, broadly based business enterprises. We see greater emphasis being placed on serving a broader spectrum of human need.

The trend toward diversification is also affecting the American insurance function which is increasingly being organized around larger and more flexible corporate structures in a position to offer more complete financial services. Forty-seven of the fifty largest property-liability companies have life affiliates, all of the ten largest stock life insurance companies have property-liability affiliates, over three fourths of the largest 100 life insurance companies are developing or currently offering variable annuities, and insurers are sponsoring a substantial number of mutual funds.

It is good business policy to maximize the utilization of financial capacity and of sales and administrative personnel, so it is likely that diversification will continue in the insurance industry.

Environment

American business enterprises are being expected to help solve social problems of ecology, poverty, discrimination and urban sprawl. Employers are being expected to go beyond fulfilling the economic needs of their employees. Today's employees are increasingly looking for job fulfillment; employment which satisfies psychological needs by providing meaning to their lives. Expansion of the role of American business is requiring changes in insurance company management philosophy and behavior.

In addition, American business enterprises are being faced with a force generally called "consumerism"; an increased pressure from consumers who combine forces to obtain influential support in legislatures and in government agencies.

Cooperation with Government

While in the past the insurance industry has used voluntary assigned risk plans and pools to distribute and subsidize marginal and sub-standard risks, growth in the insurance industry has resulted mainly from providing coverage for risks which are generally viewed as insurable.

In recent years, pressure has increased to provide coverage for risks which do not meet the traditional definition of insurable risks. The property-liability insurance industry is cooperating with government in providing coverage for property exposed to flood, as well as crime and fire coverage for property located in extra hazardous urban areas. The insurance industry's Healthcare proposal is an attempt to cooperate with government in meeting the problems of inadequate medical care and the life insurance industry is cooperating with government by investing millions of dollars in high-risk urban areas.

Cooperation with government has taken different forms. In flood insurance, through federal subsidies, the general public will share in the extra cost of insuring highly exposed properties. Under state FAIR plans, private insurance companies are absorbing the extra cost of providing fire coverage for high risk urban properties at inadequate premiums while profits from federal riot reinsurance have been used to fund a federal crime insurance program serviced by and competing with private insurance companies. There is no government subsidy for investment losses which may be sustained by life insurance company's investing in high-risk urban areas. Such investment losses will have to be absorbed by private insurance company stockholders and/or policyholders. It seems likely that in the future, actuaries will need to take into account the extra cost of high-risk cooperation with government.

Future Environment

Just as the present business environment differs from that of a past era, the future business environment will also differ from the present. It seems likely that there will be continued expansion of interaction between government and the insurance industry as our society increasingly looks to the insurance mechanism as a means of tackling social problems of poverty and urban decay, as well as economic problems resulting from automobile accidents and the non-portability of pension funds and other employee fringe benefits.

In the property-liability business, since 1965 we have seen an increasing interest in the mass marketing technique for personal lines coverages i.e. group sales of insurance to employees of a single employer or to members of associations and educational or charitable organizations, usually on the basis of the employee or member paying the total cost. It is likely that in the future, the mass marketing technique will be used to distribute coverage to an increasing share of the personal lines market. At the same time, the American business scene is developing into a service economy with a consequent decline in the relative importance of basic industries such as manufacturing, mining and farming. Service businesses have historically been relatively small firms which do not appear to be ideal markets for the mass marketing technique.

In the life business, companies are expanding into equities and into property-liability insurance in order to increase agent earnings and productivity and to increase underwriting capacity which has been strained by jumbo jets and super tankers. The emergence of a marketable equity-based variable life insurance contract should stimulate interest in permanent life insurance contracts, but could very well result in a significant step toward federal regulation.

The expansion of equity based products introduces a variable investment element and subjects this part of the insurance business to SEC (Securities and Exchange Commission) legislation and regulation. The SEC views variable products as securities and tries to make them fit that mold. This threatens the large front-end load concept which has been so essential to the successful marketing of life insurance personal lines.

One solution would be for Congress to enact legislation taking variable insurance products away from SEC control and transferring jurisdiction to a separate department which would regulate and control these equity based insurance products. Such an exchange of one brand of federal regulation for another would seem to be a step closer to federal regulation of the Canadian type. Whether or not this step is taken, or another means found for increased marketing of variable products, it seems clear to me that actuaries of the future must have a greater knowledge and understanding of the functioning of the entire investment process.

Government Intervention

One issue yet to be determined is the future role of the Social Security system in bringing economic security to Americans. The Social Security role traditionally has been to provide a basic level of protection with occasional liberalizations reflecting increases in the cost of living and our standard of living. However, there are some who envision expanding the Social Security system to provide full economic security to nearly everyone, including the poverty-stricken.

Barring a sustained business recession, it seems clear that the next decade will bring some resolution of the poverty problem, either in the form of a negative income tax or guaranteed income, or in the form of a significance expansion of the Social Security system. Such an expansion would appear to increase wage-related benefits for people in middle and upper income brackets regardless of economic need, as well as those at poverty levels, since an increase in the minimum benefit without a proportionate increase in the maximum would compress the benefit distribution, thus destroying the concept of wage-related benefits. Expansion of the public Social Security system would obviously reduce the private insurance market for income protection.

Another issue yet to be determined concerns the private health insurance field which is being threatened by mounting pressure for the establishment of a compulsory national health insurance system as a partial answer to continuing increases in price levels of medical care. This pressure continues to build even though the vast majority of the American public finances its health care through private health insurance. The Health Insurance Council's 25th Annual Survey found that at the end of 1970, over nine out of every ten Americans below age 65 (about 92 percent) were covered by private hospital expense insurance. Of those covered for some or all of their hospital expenses, 94 percent also had surgical expense protection and 80 percent had non-surgical medical expense coverage. Disability income benefits for non-occupational short-term wage loss provided by insurance companies, and other formal arrangements, protected more than two out of every three in the labor force.

A number of comprehensive proposals designed to solve the nation's health care problems have emerged in recent months. The health insurance business is sponsoring and supporting a cooperative proposal called Healthcare. Healthcare would be a voluntary program with Federal standards for health insurance, tax incentives for employers and individuals to upgrade their private health insurance coverage to meet the Federal standards, federal and state subsidies through state pools of private health insurers to provide comprehensive benefits for the medically indigent (the poor, near poor and those previously uninsurable), modest co-payments by insured persons and progressive expansion of benefits throughout the 1970's to avoid overloading the health care delivery system. Healthcare benefits are designed to dovetail with and supplement Medicare, but to ultimately replace Medicaid as a means of financing medical care for low income families.

At the opposite extreme, in terms of cost and approach to health care problems, is the Health Security Plan sponsored by AFL-CIO and the Committee for National Health Insurance. This proposal would scrap private health insurance plans, finance costs publicly through new and existing federal taxes, scrap co-payments by insured persons and absorb Medicare and Medicaid into the new system. It is likely that the resolution of the Social Security issue and the national health care issue may well have major effects on the role which the federal government will play in the actuary's environment.

The Actuary

"man's yesterday may ne'er be like his morrow"

— Shelley (1792-1822)

Twenty-five years ago, two different companies were required to insure a single private passenger automobile, and most casualty actuaries knew very little about fire insurance. Thanks to multiple line legislation, the horizons of the casualty insurance industry, and of the casualty actuary, have broadened to include all property-liability coverages.

A single document issued by a single company to insure the property-liability exposures found in a single house, or the property-liability exposures of owning or operating a single automobile, are ideas which have become reality. These ideas and dreams of a past generation have been replaced by increasing interest in a family account plan and even a life cycle policy.

A family account plan would enable an insured to make a single monthly payment under a single account billing covering the entire range of financial services (including insurance) required by his family. A life cycle policy, as it is discussed in the life insurance industry, would blend varying amounts and types of life insurance to provide varying mixtures of protection and savings from cradle to grave. Life insurance protection and savings would increase as family responsibilities increased through marriage and child birth, and would decrease as the insured approached retirement age. The life cycle policy concept can easily be broadened to include full family protection through the addition of health insurance and property-liability coverages. Some may argue that the resulting life cycle policy would be a bundle rather than a package, but I submit that today's consumer is not really sympathetic to our internal accounting problems and there is a property-liability precedent in at least one company's Master Insurance Program applicable to commercial risks.

The variable outlay approach to the life cycle policy blends in with the family account plan, either of which would maximize consumer and agent convenience and would increase the probability that a family would look to one company for all insurance and financial service needs. Both variable outlay approaches are consistent with today's trends in American social and business environments. It seems clear to me that actuaries of the future must be much more conversant with all uses of the insurance mechanism.

Traditional thinking can be a Procrustean bed, a perpetuation of the parochial vertical linearity which today argues that a casualty actuary is different, and should continue to be different from a life actuary. It is true that a property-liability company cannot legally write life insurance, and vice-versa, but, the fundamentals of life and casualty actuarial science are the same. We are today divided more by differences in vocabulary and experience, than by any real difference in the common core of actuarial science.

I urge that, jointly with the Society of Actuaries, top priority be given to defining the common core of actuarial science and to completely restructuring our present education and examination requirements for tomorrow's actuary. This redefinition and restructuring must recognize the actuary's function of assisting management in the exercise and building of intelligent and informed fiscal control and long range fiscal plans. Tomorrow's actuary will need a greater knowledge and understanding of all facets of the insurance mechanism including much of the financial and investment knowledge covered by candidates for an MBA (Master's in Business Administration) degree, with emphasis on the mathematics of quantitative methods. Obsolescence must also be avoided by giving top priority to the problems of the continuing education of today's actuary. The continued vitality and relevancy of the actuarial profession depends on our ability to anticipate and adapt to our changing economic and social environment.