

....CPS BULLETIN....

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Introduction

This issue of **CPS Bulletin** discusses the expected reduction beginning in 2006 of the valuation interest rate from the current rate of 4½% to 4%. This change will require additional work to re-file forms, adjust administration systems, reexamine cash values and review premium rates in tandem with the prospective move to the 2001 CSO table.

Our second article looks at search engines. The amount of available information on the Internet increases dramatically each day. The tools are becoming more sophisticated and although Google is the undisputed search-engine leader, huge sums are being paid for other lesser-known search engines such as "Ask Jeeves". Our article addresses what can be achieved with these search tools and what is the best approach to searching the net.

Because of a major court case that could affect volunteer organizations such as fraternal, our regular Regulatory Update includes a legislative update. The case raises concerns about the liability that can be incurred by an organization due to the actions of its volunteers.

We hope that you enjoy receiving this newsletter. If you have any comments or suggestions on how we can improve **CPS Bulletin**, please contact us by visiting our company web site at www.cpsincorp.com ✦

A Matter of Interest

The low interest rate environment has not been kind to fraternal benefit societies. It has reduced investment income, brought into play guarantees that were rarely expected to come into effect (such as guaranteed annuity credited rates) and, in some cases, resulted in cash flow analyses requiring additional reserves.

Now fraternal are faced with yet another consequence. It appears fairly certain that the valuation interest rate under the Standard Valuation Law (SVL) will fall beginning January 1, 2006 to 4% from the current 4½%. The lower interest rate will mean that reserves will need to be increased. This will affect only certificates issued after December 31, 2005 but will nevertheless involve quite a few adjustments to the plans that are currently being issued. The last time that the rate changed was in 1995, when it was reduced from 5% to the current 4½% rate.

The change in the valuation interest rate also impacts the rate that can be used to determine cash values. The cash value rate is equal to 125% of the valuation interest rate, rounded to the nearest quarter-percentage point. The current valuation rate of 4½% provides for a maximum cash value interest rate of 5.75%; the new 4% valuation rate will result in a maximum cash value interest rate of 5%. The change for the cash value interest rate will not go into effect until January 1, 2007 (as opposed to January 1, 2006 for the valuation rate).

Why is the rate changing?

The formula in the SVL is tied to the monthly corporate bond yield indices published by Moody's Investor Service ("Moody's Index"). The formula depends on the type of contract, the maximum number of years that the contract can remain in force on the basis guaranteed in the policy and whether the average Moody's rate is above or below 9%.

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For ordinary life insurance, the formula currently reduces to the following:

$$\text{Valuation interest rate} = 3\% + 0.35 \times (R - 3)\%$$

where R is the lesser of the 12 and 36 months arithmetic mean ("average") of the Moody's Index. No change is made in the valuation interest rate unless the formula yields a change of at least ½%.

For the last 10 years, running averages have been as follows:

Period ending June 30:	12 month running average	36 month running average	Lesser of the two averages (R)
1995	8.42%	8.03%	8.03%
1996	7.55	7.83	7.55
1997	7.74	7.90	7.74
1998	7.11	7.47	7.11
1999	6.96	7.27	6.96
2000	7.93	7.33	7.33
2001	7.72	7.54	7.54
2002	7.44	7.70	7.44
2003	6.71	7.29	6.71
2004	6.26	6.80	6.26

According to the formula, if one of the running averages were to fall below 6.22%, then the valuation interest rate would be reduced to 4%. In 2004, the 12-month average fell to 6.26%, just missing the cut. Since July 2004, the Moody's Index rates are as follows:

Month	Index
July 2004	6.24%
August 2004	6.08
September 2004	5.91
October 2004	5.87
November 2004	5.89
December 2004	5.84
January 2005	5.72
February 2005	5.55
March 2005	5.77

The average for April 2005 to June 2005 would have to be in excess of 7.20% in order for the valuation interest rate to remain at 4½%. Similarly, the rate for those 3 months would have to average below 4.37% for the valuation interest rate to fall to 3¾%. Both of these

events currently appear unlikely and the rate looks to be heading for 4%.

What are the immediate consequences, other than increases in the reserves, required for new policies?

- Changes in cash values for new policies. If the cash value interest rate is greater than 5%, then new cash values will have to be developed and submitted to the states. As indicated previously, the new cash values do not need to be implemented until January 1, 2007.
- An endorsement will have to be filed with each state where a society is licensed before January 1, 2006 to stipulate the new valuation interest rate that will be used in the policy form.
- Premium rates will have to be reviewed. Current premium rates may not be adequate to support a 4% valuation interest rate and may give rise to deficiency reserves. This could put an additional strain on operational results.

In this context, the review should encompass whether now is the time to adopt the 2001 CSO Table. That table will be mandatory beginning January 1, 2009. Preliminary calculations show that for many plans the combination of a move to the 4% valuation interest rate together with the adoption of the 2001 CSO Table will leave premium rates more or less where they are currently.

- Administration systems will have to be updated to recognize the new reserves that will be used for policies that have the 4% valuation interest rate and possibly new cash value tables.
- If a society issues annuities and the guaranteed credited rate is greater than 4%, then additional reserves will need to be established for new issues beginning January 1, 2006 since the guaranteed credited rate would be greater than the new life valuation rate.

Much thinking and work needs to be done for this transition and fraternal are fortunate to have a lead-time before these adjustments must be implemented. Societies should use the next few months to explore the alternatives and put in place a coherent strategy to deal with the change. ❖

Seek and Ye Shall Find

There is so much information today on the Internet that it is indeed true that seek and ye shall find. This article will explain some of the more popular ways to search the web.

In a recent competition, hacking experts were allowed to use only google.com to find as much personal information as they could, such as social security numbers, driver license numbers, medical records and more. The winning team accomplished the objective in about three-quarters of an hour. While most of us do not have the insights of these hackers, we can find, with sufficient persistence and practice, many of the items that we need on the Internet.

Most of us are familiar with the most popular search engines. The granddaddy of them all right now is Google. Other popular sites include Yahoo, AltaVista, MSN and Ask Jeeves. Once you type in a word or phrase, the search engine will attempt to match your term with the sites that it has in its database, and then provide you with a list of the sites. The search engines will "relevance rank" the matches for you, which mean that you only have to check the first page or so of hits in order to locate the sites that are most appropriate.

Search engines do not really search the World Wide Web directly. Instead, they search their database of web pages selected from the billions of web pages that exist. When you use a search engine, you are always searching a somewhat stale copy of the real web page. However, when you click on the links provided in the search results, you retrieve from the server the current version of the page. Search engine databases are selected and built by computer robot programs called spiders, which are said to "crawl" the web in their hunt for pages to include. They find the pages for potential inclusion by following the links in the pages they already have in their database. If a web page is never linked to in any other page, search engine spiders cannot find it. The only way a brand new page (that is, a page that no other page has ever linked to) can get into a search engine is for its URL to be sent by a human to the search engine companies as a request that the new page be included. All search engine companies offer ways to do this.

The size of each search engine's database varies. Google is the largest, with over 8 million pages in their database. MSN has the 2nd largest database, with about 5 million pages. Just because a search engine has more pages in its database does not mean that it's better; relevancy does matter. For example, Google has twice as many pages in its database than Yahoo but that does not mean that it is twice as good.

Most of the search engines have become portals, which mean that they provide an opening to many information-related services on the Internet. For example, when you click on the "more" link on google.com, you will find many links to various services, such as *Froogle* (for shopping), *University search* (for searching a specific school's website), and *Scholar* (to search for scholarly papers). Google has recently contracted with major universities to "electronify" their libraries in exchange for public access to that information. If your need is particularly important and you can't find the answer yourself, Google has a link called "answers", where "more than 500 carefully screened Researchers are ready to answer your question for as little as \$2.50 -- usually within 24 hours". Google handles over 50 languages and translates 5 European and 3 Asian languages.

Most search engines use Boolean logic, which mean that when you enter key words in the search box, an implied AND is assumed between words. Thus, if you enter 4 key words in the search box, the search engine will look for documents containing all four of those words in any order and in any location within the document. Most search engines will increase the relevance rank if all of the words appear.

Advance searches offer numerous options for making your searches more precise and getting more useful results. One use of advance search will allow you to limit the age of the documents that you search for so that the information is current. Google's advanced search capabilities are excellent for searching a particular web site instead of using that site's own capabilities. Google has also recently introduced a capability to search your own computer (which can be very useful given the much-depleted Microsoft search capabilities in Windows XP) as part of its advanced search capabilities.

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While many of the search engines use Boolean searches, there are some that use "natural language searching", such as Ask Jeeves for kids (www.ajkids.com). With natural language searching, you can enter a search like "highest mountain in the world" to get your answer.

In addition to the popular search engines that maintain their own databases, another way to search the Internet is to use a Meta search site. These sites allow you to gather results from many web search engines by using one single service. Two of the top choices are Webcrawler.com and Dogpile.com. Currently, Dogpile.com is the most popular of these Meta sites; it uses the information from other search engines when generating the search results, including Google, Yahoo, AltaVista, Teoma (the database behind Ask Jeeves) and About.com.

We hope this little summary provides you with a starting point for browsing. Now you can go out and have fun. By all means, become an expert, but keep away from our personal information. ❖

About CPS

CPS Actuaries and Computer Programming & Systems, Inc.

CPS is an independent company with over 35 years of client service. We offer a wide range of computer and actuarial services, including the following:

- Actuarial valuations
- Annual and quarterly statement preparation
- Policy administration software
- NAIC compliant illustration software
- Web site hosting, instant messaging, and e-mail
- Design, install and maintain local and wide area networks
- Hardware & software installation and upgrades

For more information regarding our services, please call us at **203-324-9203**, or visit our web site at www.cpsincorp.com ❖

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Regulatory Update

New York Liquidity Survey

NY has a Liquidity Survey that must be completed by all NY licensed fraternal. The due date is May 1, 2005. According to an individual in the Department, this may become an annual requirement. The link to the survey is as follows: www.ins.state.ny.us/acrobat/interrog.doc.

Signatures on Jurat for Fraternal Domiciled in Pennsylvania

PA issued Notice 2004-03, which indicates that now that the annual statement Jurat page permits different officer titles to be entered, they want the quarterly and annual statements to be signed by the society's CEO, CFO and Corporate Secretary. If your society does not have individuals that have those titles, then you will need to write to Mr. Kaushik Patel in the PA Insurance Department and indicate how the individuals that do sign your financial statements meet the requirements. If you do not comply, then the statement will be deemed to be filed incorrectly and subject to return.

Heikkinen v Archdiocese of Milwaukee

In this case, a jury awarded \$17 million to a plaintiff who was rendered a paraplegic by a van driven by a volunteer for the Legion of Mary. The volunteer was delivering a statue to a parishioner with the knowledge of the priest. The case hinged on the facts that (1) the purpose of the Legion of Mary was to assist the church in their work and thus the volunteer was considered an employee/agent of the church, and (2) the parish's insurance specifically said that any volunteer doing service on behalf of the church is covered by its policy.

While this decision is far from final, it behooves all volunteer organizations to examine the volunteer issue carefully and ensure that, in this litigious society, risk is minimized. ❖

Interest Rate Monitor

The following are some key interest rate benchmarks:

Benchmark	Current	3 Months Ago	1 Year Ago
Fed Funds	2.81%	2.31%	1.00%
Prime Rate	5.75%	5.25%	4.00%
30 yr mortg	5.46%	5.26%	5.56%

Source: www.bloomberg.com as of April 14, 2004.