

# .....CPS BULLETIN.....

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## Introduction

As we mourn the terrible losses of September 11th, we gain strength from the unshakable spirit of our country. We stand in awe of the heroism and tireless efforts of the firefighters, police officers and emergency relief workers who epitomize this country's heart and strength.

As we get back to business, we discuss a new mortality table that is being developed. The 2001 CSO Table is being created to replace the 1980 CSO Table. The article covers the reasons why a new table is being developed at this time and also reviews the possible impact the new table will have on certain types of plans. The table has not yet been adopted, so it probably will not be available for use until January 1, 2003 at the earliest.

Another article in this issue addresses the need for companies to have a disaster recovery plan in place. The attacks on the World Trade Center have illustrated the importance of such a plan. We also provide an update on two NAIC topics – the 2002 maximum interest rates for life plans and the drafting of a model regulation regarding suitability of insurance.

If you would like us to e-mail future issues of the newsletter to you, please let us know your e-mail address and we can arrange to make that happen. ❖

## The 2001 CSO Table

For a number of years now, there have been discussions about developing a new CSO mortality table. The time has finally come where it looks like a new table will actually be completed very soon. This new mortality table is called the 2001 CSO Table. It is expected that the NAIC will adopt the table early next year. In anticipation of the adoption of the table, here are some considerations that might interest you.

### **Why is a new mortality table needed at this time?**

The last new mortality table was the 1980 CSO Table, which replaced the 1958 CSO Table. Substantial changes in mortality have taken place over the last couple of decades since the development of the 1980 CSO Table. Over the years, mortality studies have shown that during a 20-year span, mortality experience shows significant improvement. It is now established practice in a number of advanced countries to continuously examine mortality experience and recommend changes to standard tables when justified.

### **What are some of the changes in mortality that have occurred over the past 20 years?**

People are expected to live longer than they did 20 years ago. The expected lifetime for children born today is 78 years for males and 82 years for females. Twenty years ago, when the 1980 CSO Table was developed, the expected lifetimes were 72 years for males and 77 years for females. Improved nutrition as well as the rapid development of new drugs to help prolong life has contributed to longer lifetimes. Not all changes in mortality over the past 20 years, however, have lengthened people's life expectancy. In particular, AIDS was not even an issue when the 1980 CSO Table was developed. All of these items are considered in developing the new table.

## INSIDE THIS ISSUE

- 1 Introduction
- 1 The 2001 CSO Table
- 3 Preparing for a Disaster
- 4 NAIC Update
- 4 Interest Rate Monitor
- 4 About CPS

See [2001 Table](#) on page 2

**Which items will the new table impact?**

The new tables will immediately affect minimum reserves, deficiency reserves and non-forfeiture benefits, as well as tax-reserves and the definition of life insurance for IRS purposes. These will in turn impact product pricing and commissions.

**How will certain items calculated under the 2001 Table compare with results from the 1980 Table?**

The new tables will have the effect of lowering reserves and cash values on plans issued using the new table. Premiums will also likely decrease, which will reduce the amount of commissions paid. The new table will have no impact on previously issued policies.

**What is the magnitude of some of the changes between the 1980 and 2001 Tables?**

The overall improvement in mortality experience has been about 20% compared with 1980 CSO mortality. For males, whole life reserves using the 2001 Table are generally 80-90% of 1980 CSO Table reserves, 55-70% for term reserves and 60-100% for universal life (UL) reserves. The improvements for females are more modest, especially for female smokers.

**What are some of the other differences between the 1980 and 2001 Tables?**

The ultimate age in the 2001 Table is 121 compared with 100 for prior CSO Tables. This means that instead of having to pay the sum insured (or escheat the money to the state if you cannot find a member) at age 100, you may wait until the member reaches age 121. It will also obviate the need for the Extended Maturity Benefit features of life policies that are used for tax planning, by avoiding a taxable event should the insured live to age 100.

The 2001 Table does not have a separate mortality table for extended term. This is unlike the development of the 1980 Table, at which time a separate CET Table was created to recognize that members on extended term have higher mortality. Members in poor health might take advantage of this to select against societies under the 2001 Table by stopping premium payments. Societies may need to review overly generous extended term availability.

The 2001 table has a 25-year selection period (where the effects of underwriting are noticeable) whereas for the 1980 CSO Table, 10 and 19-year selection factors for basic and minimum reserves were subsequently developed. Societies with strong underwriting criteria will be at an advantage and the gap between standard and guaranteed issue terms will probably widen.

**What other issues may affect fraternal once the 2001 Table is adopted?**

The 2001 table appears to favor term insurance and last survivor insurance since those plans could experience the greatest reductions in rates. Conversely, Long Term Care (LTC) rates may increase to allow for an expected longer period when benefits are payable. Societies who are considering introducing new term and LTC plans may wish to wait until the 2001 Table is adopted in order to weigh competitive needs.

Universal Life plans will most likely be negatively affected by the adoption of the 2001 Table. Many companies are already under profit pressures because of the constraints caused by the guideline single premium calculations; the reduced mortality charges are unlikely to help relieve this pressure. Overall, this may lead to higher expense loadings and reduced commissions for UL products.

Whole life premiums using the 2001 Table are expected to be less than premiums using the 1980 Table (with a concomitant reduction in commissions). This will increase pressure on societies to increase efficiency or to raise their non-competitive profile by providing more fraternal benefits.

**When will the 2001 Table become effective?**

It appears that the 2001 table might be adopted by the NAIC in March 2002. After that, the states must adopt the table. Assuming at least half the states adopt it in 2002, then you would have the option of using the table beginning in January 2003 (assuming you receive approval of the new plans in the states where you are licensed by that date). Under this timeframe, it would not be mandatory to convert all of your plans to the 2001 Table until January 1, 2008. However, delaying conversion to the 2001 Table could put you at a competitive disadvantage when compared to those companies that did convert. ❖

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## Preparing for a Disaster

Computer security and disaster recovery have been getting a lot of attention in the wake of the recent terrorist attacks on the United States. Published news reports show that small offices located in the World Trade Center (WTC) generally lacked the sophisticated disaster-recovery plans of their bigger neighbors. However, early reports indicate that most plans that the companies in the WTC had were good enough. The larger companies tended to have “hot backups” that enabled them to switch to backup facilities in another location with little or no interruption. Smaller firms generally relied on backing-up data to tape and sending the tapes off site.

Interestingly enough, the Y2K scare galvanized many companies to prepare computer backup plans and carry out dry runs to ensure that they actually worked.

The experience of two smaller firms that were located in the WTC (as reported in *Internet Week*) illustrates the importance of having some kind of backup plan. Julien J. Studley Inc. (JJSI), a commercial real estate company, had a dozen people working in the WTC. They had a fairly standard office configuration, which included a Windows NT server, routers, workstations, printers, and switching equipment. JJSI went to this server-based computing model about five years ago. One of the benefits of the server model is the ability to have a centralized backup procedure. Within a week of the attacks, JJSI was running from a backup made at the end of August that had been shipped off to a data storage facility maintained by a company that specializes in storing backup information for disaster recovery.

Compare this with the experience of James Ratner, an independent, who had two PCs without backups in his WTC office. All that data was lost. Mr. Ratner believes he has a fairly good memory and “kind of” remembers what he did. He also had some data duplicated on his computer at home and expects that clients, courts, and opposing attorneys will have copies of most of the documents he stored on his PCs. He is now forced to track down this information and reproduce it on his new computers.

The way to a less stressful life is to be prepared and implement a backup plan. Without such a plan, the

consequences of an occurrence could be catastrophic, both in terms of operational impact and public image. Even though you may be a small company and you don't think something like this can happen to you, a small investment now can save a large amount of headaches later.

Key points that should be considered as part of any disaster recovery plan are outlined below:

- An automated data backup system is the key to reliable data protection. Never rely on users to back up their own data! People forget or ignore backup warnings or they make errors. Automated backup is the best way to ensure consistent data protection. The key is to find the automated backup software that will meet your specific needs.
- Not only should backup data be stored in the office, but separate copies should also be stored offsite in either a bank vault or at a company that handles disaster recovery.
- Too often, businesses overestimate the value of their system hardware, and underestimate the value of their data. Hardware is almost always covered by insurance policies and is easily replaced, whereas lost data is gone forever. There is insurance available to cover lost software, but very few companies actually purchase such insurance.
- When evaluating backup and recovery software, a company should look for programs that are compatible with both its network operating system as well as its application programs. If the application calls for the use of tape backup systems at separate locations, one should make sure that each site can read tapes written by another site.
- Occasional testing of the backup plan is essential if the organization wants to ensure that recovery capability is maintained.

With the large volume of data on today's networks, complete nightly backups may not be practical due to time constraints. The answer may be to do a complete backup once a week, and program the backup software to do differential (i.e., partial) backups throughout the workweek. Organizing and managing

See **Preparing** on page 4

complete and differential backup tapes can be time-consuming. As a result, a backup program with comprehensive librarian and tape rotation functions can pay for itself in a single occurrence. The librarian function can be used to keep track of the files that were backed up, when they were last backed up, and the backup tape where they can be found. It also can identify files that could not be copied during nightly backups (often because users have left them open). This information assists in quickly tracking and locating individual files, volumes or entire drives of information to speed restoration

One of CPS's specialty areas is setting up secure networks and disaster recovery plans for our clients. Please give us a call if you would like to discuss these items with us. ❖

## Interest Rate Monitor

The following are some key interest rate benchmarks:

Benchmark	Current	3 Months Ago	1 Year Ago
Fed Funds	3.12%	4.00%	6.50%
Prime Rate	6.00%	6.75%	9.50%
30 yr mortg	6.29%	6.76%	7.62%

Source: [www.bloomberg.com](http://www.bloomberg.com) as of Sept. 25, 2001.

## About CPS

*CPS Actuaries and Computer Programming & Systems, Inc.*

CPS is an independent company with over 33 years of service to our clients. We offer a wide range of computer and actuarial services.

There are two major divisions that make up CPS. One is an actuarial consulting firm that specializes in the needs of fraternal benefit societies. The other is a computer-consulting firm that primarily manages computer networks as an outside consultant for a variety of companies, and develops, hosts and maintains e-mail and web sites. For further information regarding our services, please call us at **203-324-9203**, or visit our web site at [www.cpsincorp.com](http://www.cpsincorp.com). ❖

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## NAIC Update

The following is an update on a couple of issues of note with regard to the NAIC.

**Interest Rates:** The maximum valuation reserve interest rate for life insurance policies will be 4.5% in 2002, which is unchanged since 1995. The maximum non-forfeiture interest rate also was unchanged at 5.75%.

**Suitability of Insurance:** An NAIC working group, chaired by Roseanne Mead (who is the Iowa Assistant Commissioner for Consumer and Legal Affairs), has recently been studying the issue of the "suitability" of insurance products sold to individuals. The working group is drafting a model regulation to address this issue. The question that is at the heart of the matter is the following: "Are insurers and insurance agents responsible for determining the suitability of an insurance product that is sold to an individual?"

The issue is a large and charged one, with fears being expressed, according to Ms. Mead, that a really cautious company would have to check every sale, either for market conduct exam purposes or for the purposes of protecting itself from a private right of action.

This is not far-fetched. In the United Kingdom, all insurers have had to set up special units to review policy-by-policy a decade's worth of alleged mis-selling of pension products. This has taken a huge toll in time and cost and has had a large financial impact on a number of companies (for example, the local subsidiary of Lincoln National no longer writes new business in the UK and has been unable to sell its existing block of business).

Individual states have also begun to take their own look at the issue. New Hampshire proposed an insurance regulation to address this issue; it was subsequently withdrawn but the issue is still on the table.

The working group has prepared a draft regulation with regard to suitability, although adoption of the regulation is not imminent because of the many interested parties who wish to provide input to the regulation. CPS will continue to update the progress of this regulation in future issues of **CPS Bulletin**.