Return of Premium Term

Actuaries' Club of the Southwest, Spring Meeting

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Agenda

ROP Term
in the Individual Marketplace

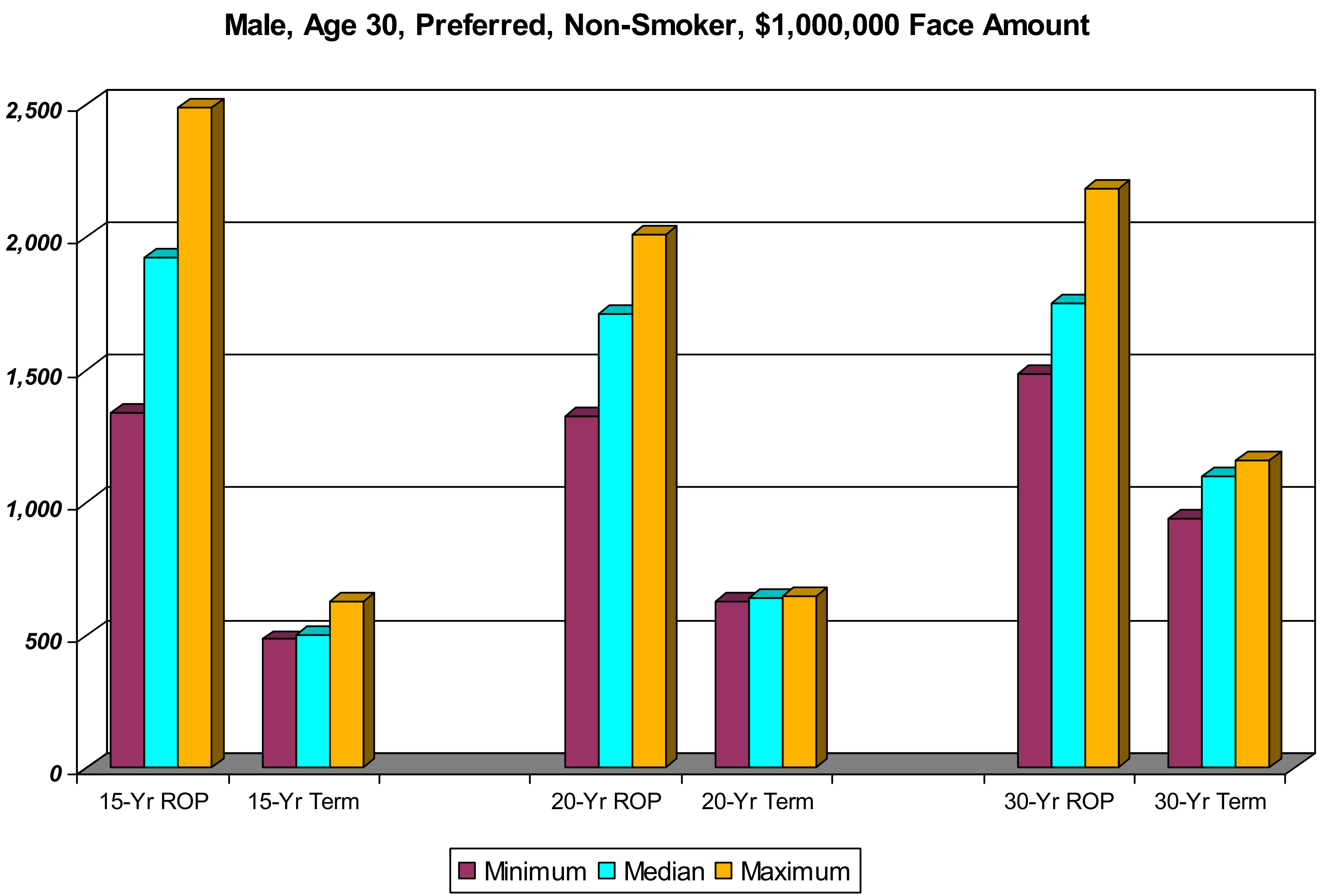
ROP Term
and the Worksite Marketplace

ROP Term typically provides for the return of an increasing percentage of premiums paid if the policy is cancelled

Sample Return of Premium Percentages

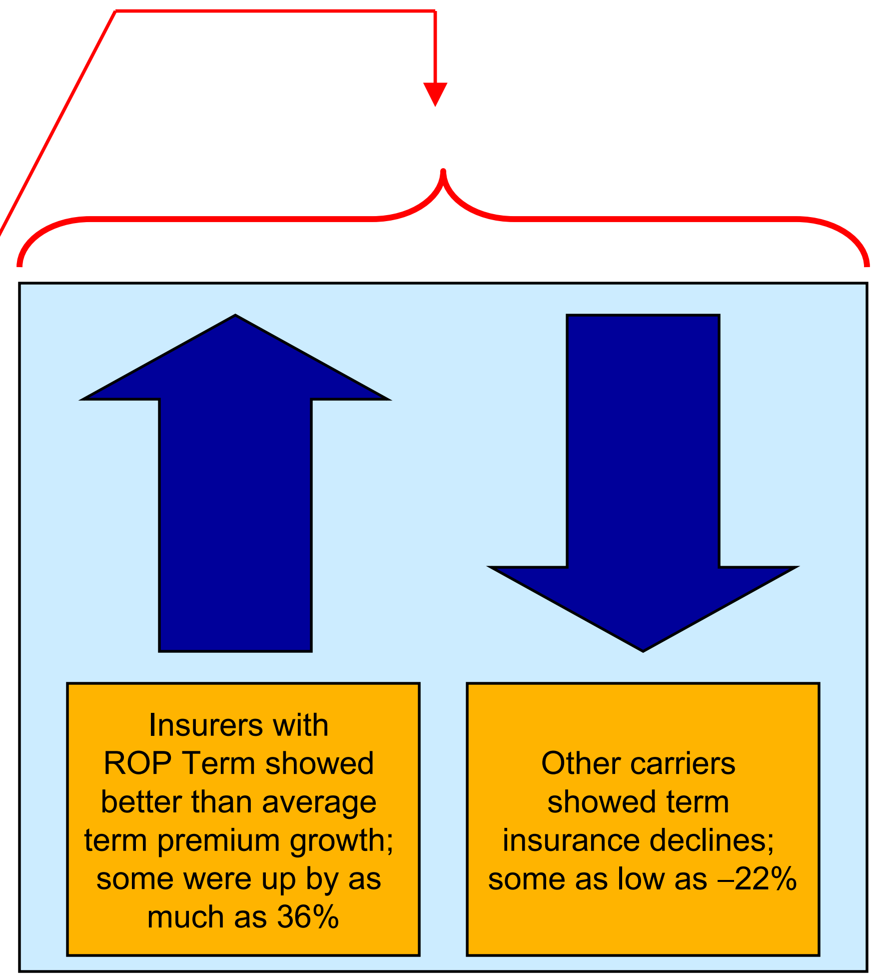
End of Policy Year	15-Year Term	20-Year Term	30-Year Term
1 – 5	0%	0%	0%
6	5	3	1
10	25	15	5
15	100	50	15
20		100	25
30			100

There is a wide range of ROP Term premium rates, especially for the shorter term periods



Term insurers reported diverse results in 2003

2003 Sales Results	
Product Line	Premium Growth
Universal Life	28%
Variable Life	-40%
Variable Universal Life	-33%
Term	**1%**
Whole Life	7%
Total	0%



For some insurers, ROP Term represents over 67% of all newly issued level term policies

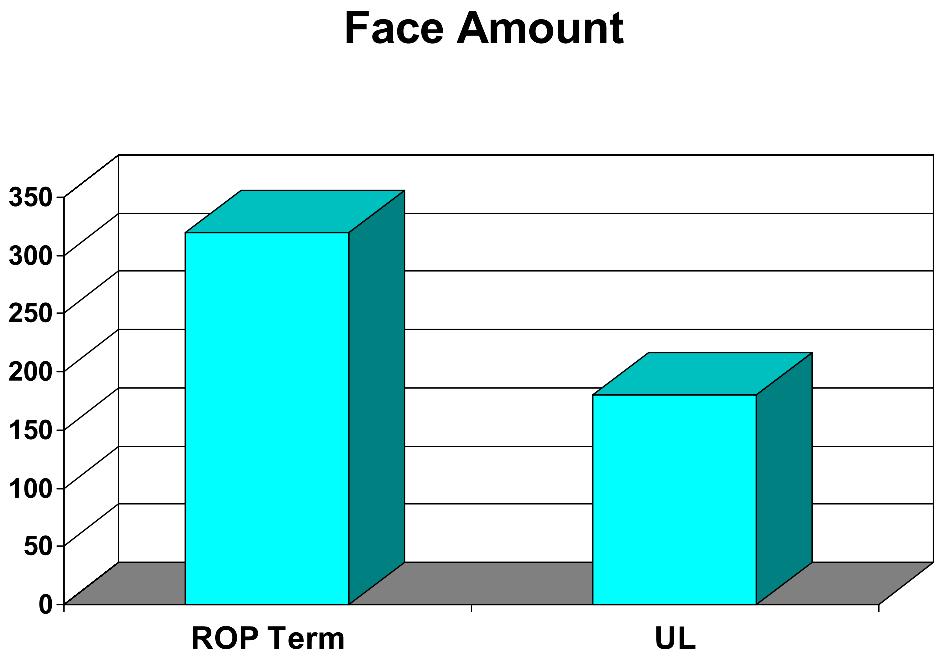
Source: LIMRA and National Underwriter

Market appeal creates sizeable opportunities for insurers

- Simple and easy for consumers and producers to understand
- Sales pitches such as:
  - "Money-Back Term"
  - "Did you know that very few policies mature as death claims?"
  - "Win-Win-Win"
- High after-tax potential rates of return are quoted (typically around 7%)
  - Higher than comparable CDs currently on the market
- Higher commissions for producers
- Mainstream media coverage:
  - *U.S. News and World Report,* October 25, 2004, "Getting a Payback"
  - *BusinessWeek,* May 10, 2004, "Premiums You Can Retrieve"
  - *Wall Street Journal,* April 28, 2004, "New Insurance Rewards Longevity"

Comparison of ROP Term to Universal Life ("UL")

- Using a sample UL product and a sample ROP Term product, we set the UL and ROP Term premiums equal and we solved for the UL face amount such that the 20th year ROP benefit and the UL account value were equal
- ROP Term buys substantially more coverage for the same premium dollars and the same 20th year cash value benefit



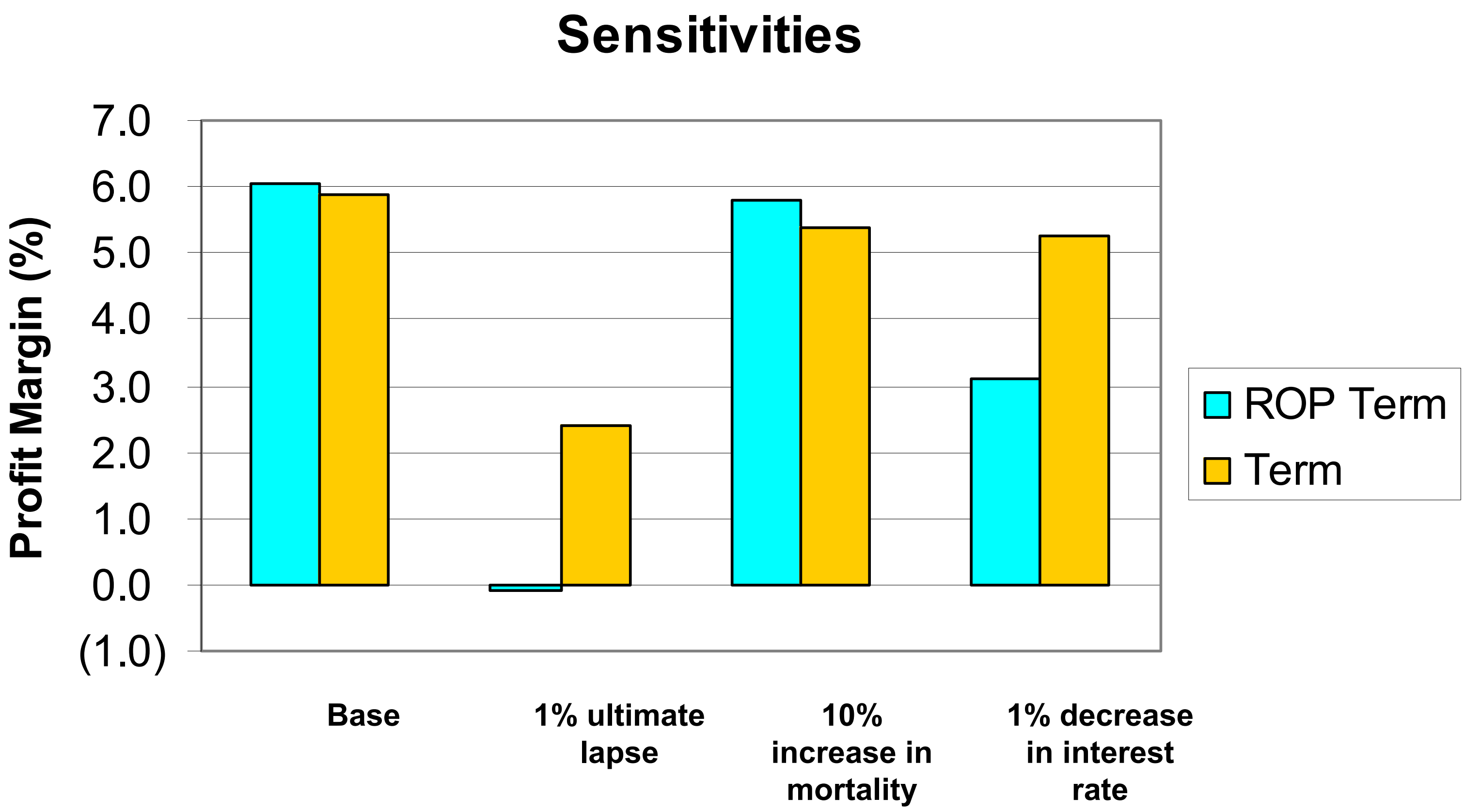
Regulatory Issues

- Most states are fine with the concept
- Some states require compliance with Section 8 of the SNFL (“Consistency of Progression of Cash Surrender Values with Increasing Policy Duration” a.k.a., “Smoothness Test”)
  - The ROP benefit can be designed to pass the Smoothness Test
  - California, Florida, Minnesota, New Jersey, New York, Utah and Washington have required a demonstration
- US Life, a NY subsidiary of AIG, recently became the first company to sell ROP term in NY

ROP Term Pricing Issues

- The ultimate lapse rate is the key assumption
  - Wide range seen in the marketplace
- A lower mortality assumption could be used
- Reinsurance is not currently available
  - Complications can arise when the base term product is reinsured, but the ROP Term rider is not
- Reserves for ROP Term are higher than for regular term
  - Reserve for pure endowment
  - Greater of XXX reserves and cash value due to steep cash value pattern
  - An improperly designed ROP pattern could require a company to hold additional statutory reserves
- More sensitive to the interest rate assumption than Term without ROP
  - Higher reserves
  - Likely have smaller percentage reinsured

Sensitivity Tests



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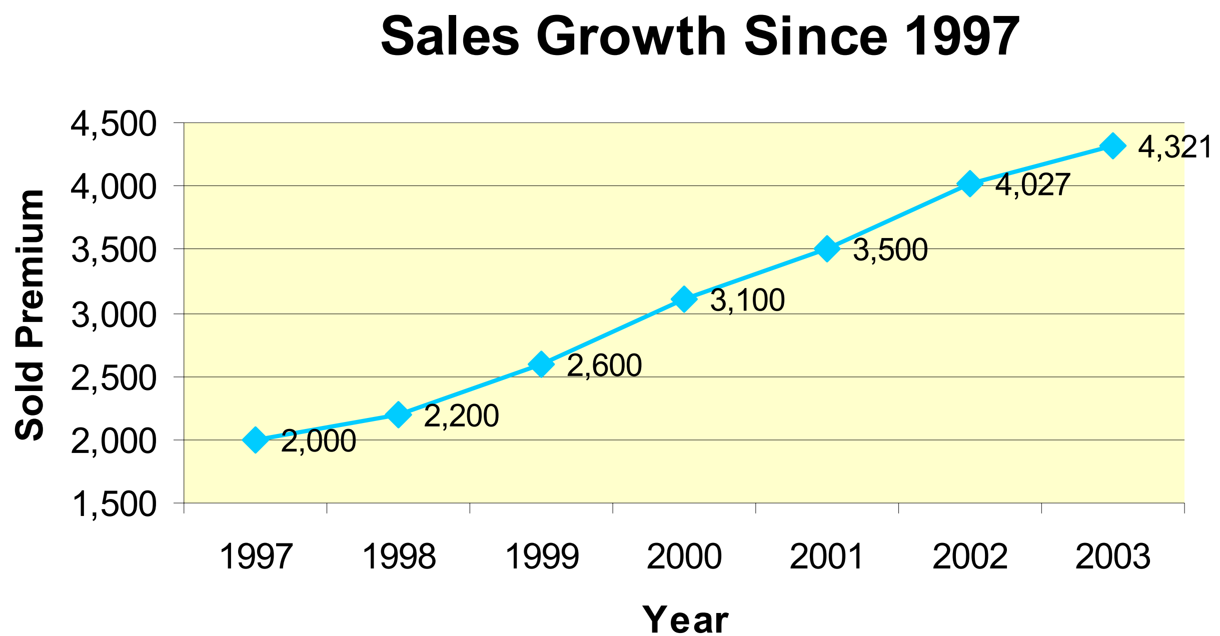
Worksite marketplace sales – All products

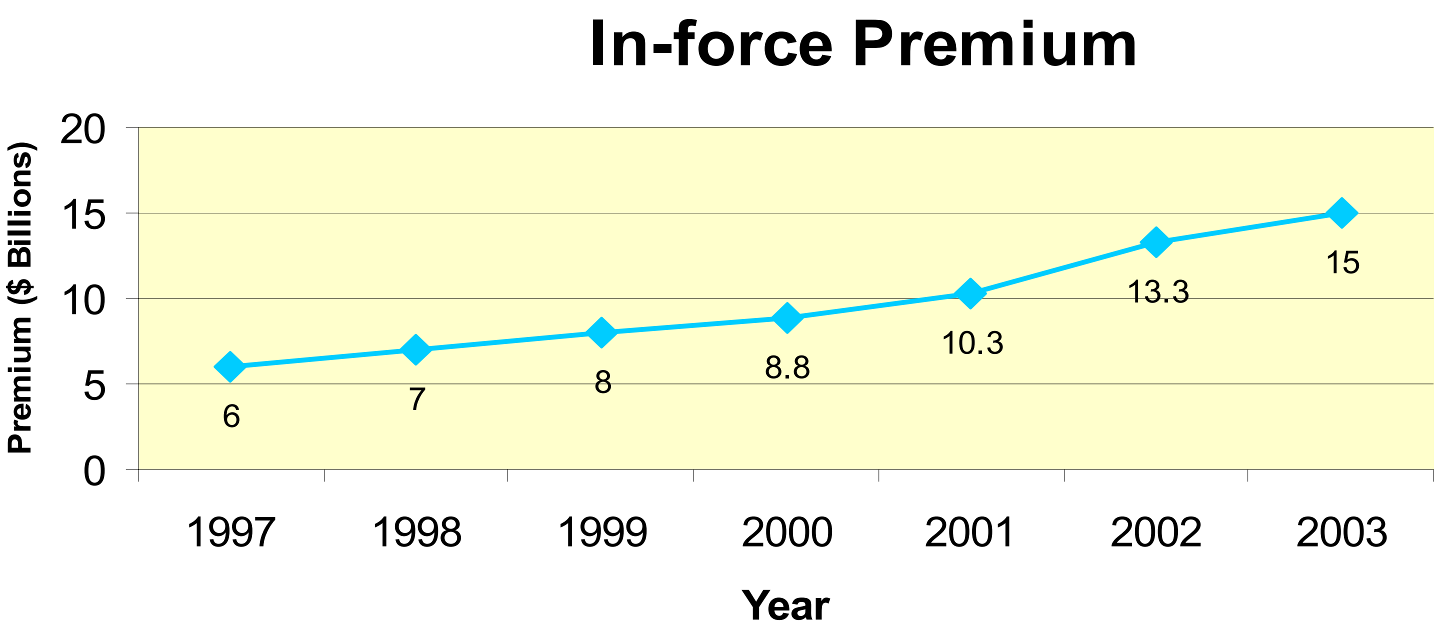
- Worksite and voluntary sales have grown significantly since 1997, from $2.0 billion to $4.3 billion in 2003
- 2003 sales increased 7% over 2002
- Historically, sales have shown double-digit growth rates year over year
- 2003 results seem to be influenced heavily by the slow sales of several of the top players
  - Problems appear to be company-related rather than market-related



Source: Eastbridge Consulting Group, Inc. Marketing Counsel To The Financial Services Industry www.eastbridge.com

Worksite marketplace in-force premium – all products

- In-force premium for worksite and voluntary lines combined increased at about 13% in 2003, a slower growth rate than we saw in 2002
- 2003 growth was more in line with historical average
- Since 1997, the in-force has grown from about $6 billion to $15 billion



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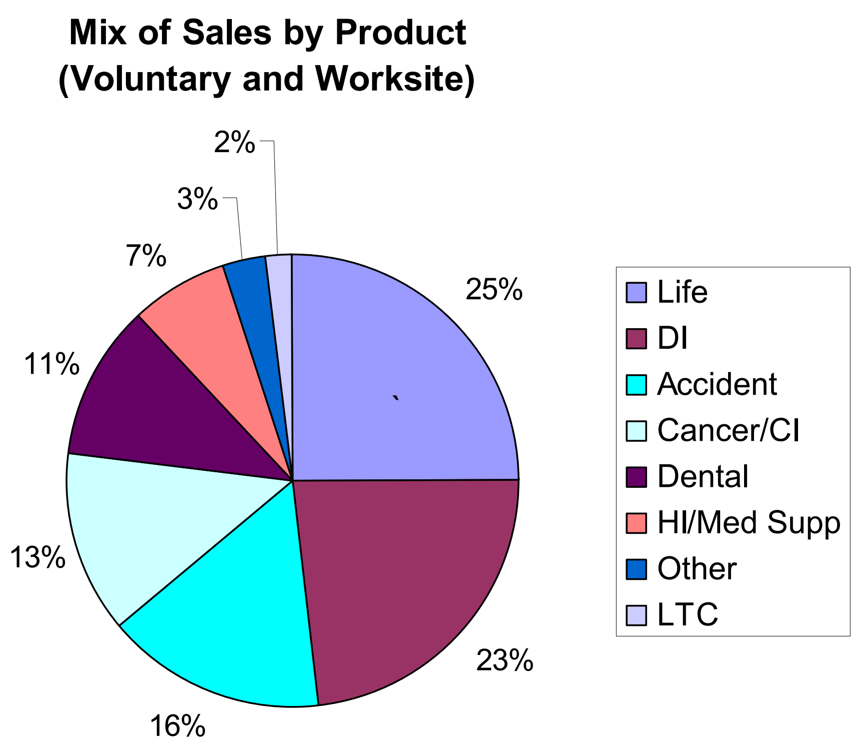
2003 worksite sales – By product

- By line of business, life insurance accounted for the largest share of sales, followed by disability
- Also in 2003, life sales grew faster than disability sales for the first time in a couple of years
- Voluntary term life sales slightly outpaced universal/whole life sales in 2003 (54% term life vs. 46% UL/WL)
- The product lines with the highest growth in 2003 were hospital indemnity/medical supplement plans, long-term disability, and universal/whole life



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Top players in the worksite marketplace

- There are about 120 players that consider themselves to be in worksite or voluntary today
- The top 15 players account for approximately 75% of the total market sales
- Many of the players have very small market shares

Top Players in 2003	
Company	**Market Share**
AFLAC	26%
UnumProvident	9%
Colonial Life & Accident	7%
American Heritage Life (Allstate)	6%
MetLife (ECG estimate)	5%
AIG (ECG estimate)	5%
Hartford Life	3%
Transamerica/Aegon	2%
Guardian	2%
American Fidelity	2%
Assurant/Fortis	2%
Jefferson-Pilot	1%
CNA	1%
Mutual of Omaha	1%

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Potential problems with worksite life

- Regular term products
  - Commissions too low to support an enroller
  - Potential participation problems; anti-selection, increased unit costs
  - Increased frequency of non-viable cases
  - High lapses may/may not threaten consumer value
- UL/Whole Life
  - Supports high commissions/enroller
  - Better participation = better case viability
  - High lapse = low consumer value

ROP Term can fill a gap

- Worksite is designed to fill gap in life marketplace; i.e., middle income market
  - Policies too small to support traditional individual agent distribution
  - Traditional employer-pay-all benefit programs often not present
- Most mid-market workers need temporary coverage; e.g., until retirement, children through college, mortgage is paid off
- UL policies relatively expensive
- Level premium term is designed to cover temporary needs
- ROP Benefits can
  - Support commissions sufficient for enroller model
  - Drive down lapses and increase value to consumer

ROP Term is a good fit for the enroller worksite market

- ROP Term concepts are attractive and more easily understood
  - Good fit for small window of opportunity common to worksite sales situations
  - UL is a complex product
- ROP Term can improve consumer value
- Flexibility is easily available
  - ROP as an optional rider
  - Availability of multiple term periods to customize to consumers’ needs

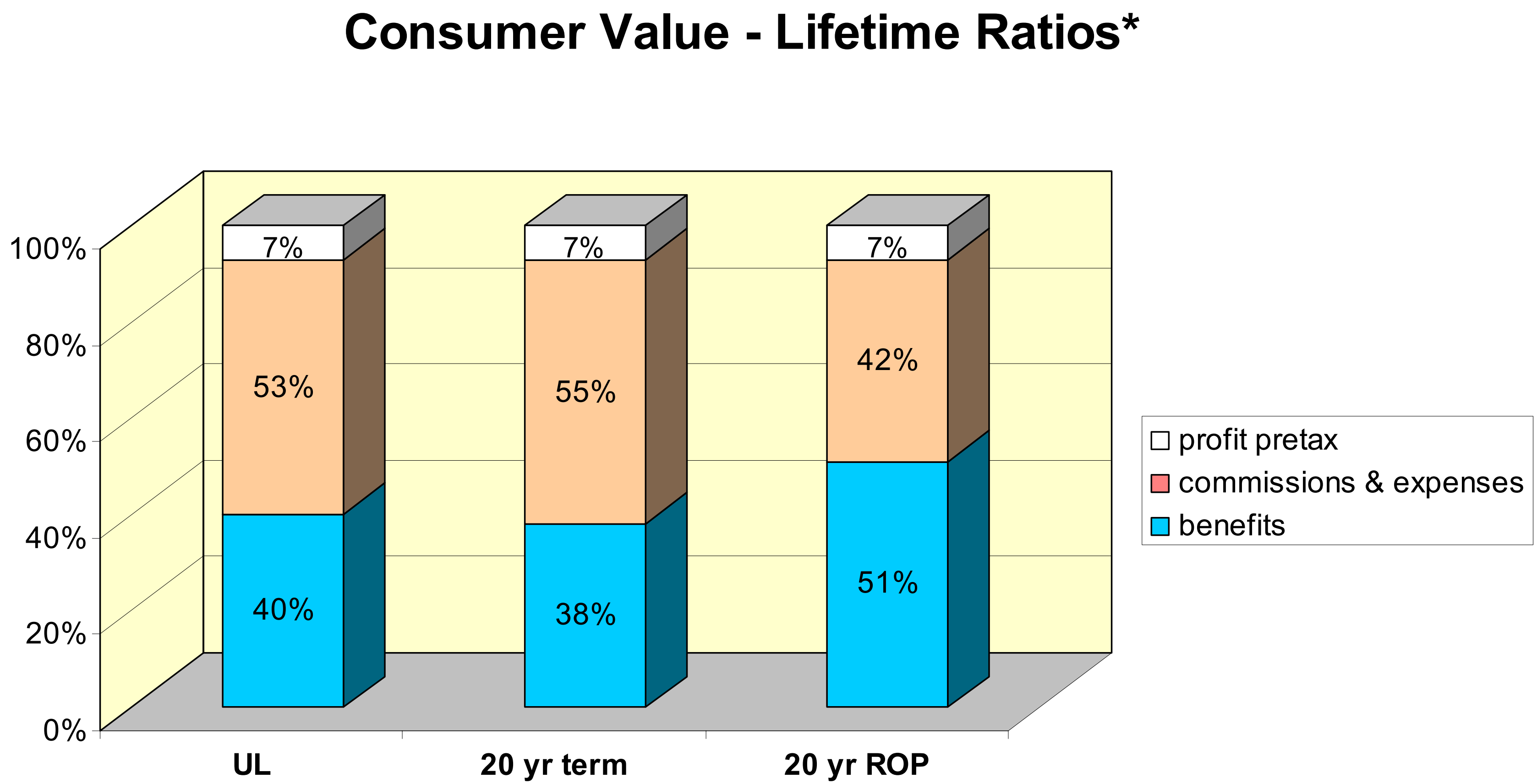
Sample policy comparisons – Male, non-smoker, issue age 40

Assumptions	UL	20-Year Term	20-year ROP Term
Face amount	$35,000	$147,000	$53,000
Level annual premium	$500	$500	$500
Lapse: 1 - 3 4 – 14 15 – 19 20 21+	 40%, 30%, 20% 10% 10% 10% 10%	 40%, 30%, 20% 10% 10% 100% N/A	 30%, 20%, 10% 5% 2% 100% N/A
Expense per policy: Acquisition Maintenance	 $250 $50	 $250 $50	 $250 $50
Commission: First year Thereafter	 85% 4%	 85% 4%	 85% 4%
Profit Margin	7.4%	7.4%	7.4%

Sample policy comparisons – Cash values

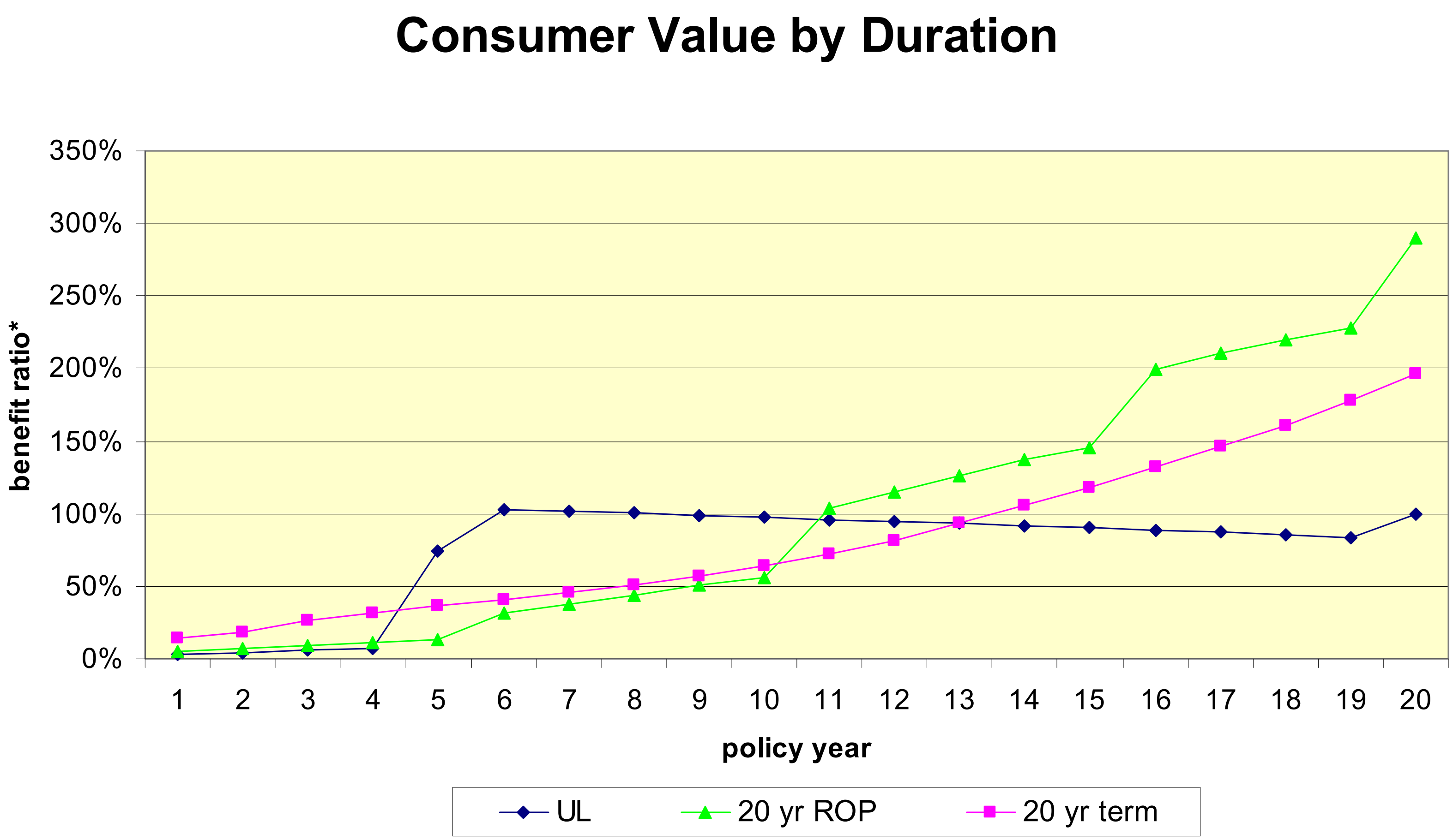
Durations	UL	20-Year Term	20-year ROP Term
5	$344	$0	$0
10	$3,088	$0	$750
15	$6,275	$0	$3,750
20	$10,029	$0	$10,000

Consumer value - Lifetime



** Present value as a percent of premium discounted at earned rate*

Consumer value by duration



** (Death + surrender benefits + Δ CV) / Premium … adjusted for interest*

Conclusions and Final Thoughts

- ROP Term is selling well
  - Consumers like it
  - Agents like it
- But you have to be careful in pricing the product
  - What is the appropriate rate of return to persisting policyholders?
    - Single digit yields (i.e. government bonds) versus double digit
  - Lack of experience on ultimate lapse rate is risky
    - We are in the risk business
    - May not be as quantifiable as other assumptions, but price it that way
      - Actuarial judgment
      - Conservative margins
      - Processes similar to other products with lack of experience surrounding certain assumptions