On August 9, 2011, SCOR SE, a global reinsurer with offices in more than 31 countries, acquired substantially all of the life reinsurance business, operations and staff of Transamerica Reinsurance, the life reinsurance division of the AEGON companies. The business of Transamerica Reinsurance will now be conducted through the SCOR Global Life companies, and Transamerica Reinsurance is no longer affiliated with the AEGON companies.

While articles, treaties and some historic materials may continue to bear the name Transamerica, AEGON is no longer producing new reinsurance business.

Archive Materials

The End-of-Level-Period Balancing Act
Reprinted from the December 2010 Messenger newsletter

By George Hrischenko, Marketing Actuary Leader
Setting end-of-level-period (EOLP) term rates has never been an exact science in our industry. Two predominant schools of thought have emerged. One group espouses a high initial EOLP reset to induce policyholders to replace coverage. Another seeks to find an appropriate “fit” to encourage better risks to persist after the level premium period – if only for a couple of years.

This article examines the potential advantages and challenges of each approach in more detail. For this discussion we have chosen sample pricing data for a 45 year-old male, best class, 10-year level premium term. Figures are illustrative.

Pricing for the Level Period
The traditional approach to EOLP pricing has focused on resetting to yearly renewable term (YRT) rates for the duration of the policy. These reflect not only the attained-age risk but also the firm’s view that the mortality of the residual risk pool following the end of the level premium period will worsen.

As a result the EOLP can be higher than the level premium by many multiples.

Figure 1: Level Premium and EOLP Rates
Companies manage EOLP risk differently. Company C is a mutual, which likely pursues a strategy of conversion.
While some companies’ rates reflect an actuarially fair rate, in other cases companies use much higher multiples -- 15, 20 or even 30 times the level premium rate. The goal is to induce policyholders to replace their coverage with a more affordable, new level-premium term policy. Figure 2 outlines this approach.

A “shock” rate may benefit both parties. Replacing coverage with a new level term policy may result in lower premiums for the customer, even after factoring in a new attained age. In most cases, replacement allows the insurer to re-underwrite the policyholder and factor in any material changes to expected mortality.

Of course, replacement poses a critical selection issue; policyholders with deteriorating health have more need to retain their original coverage, even at much higher rates. Selection issues are aggravated with the lapse of good risks. The law of large numbers potentially fails, leaving the company exposed to volatile and significant claims from the residual book, with serious cash flow implications.

The timing of lapse is also a cash flow issue. Premiums are usually paid monthly, but many companies price on an annual mode. While some policyholders will replace or lapse their policy at the end of the level term period, most do not make a decision for several months. Companies should track post level period lapses closely to keep their expected premiums (and the attendant DAC amortization) more in line with actual experience.

Lastly, there are new acquisition costs associated with replacement: commissions, underwriting and administration. This of course assumes that the policyholder uses the same carrier to replace the product.

### Managing Beyond the Level Period

The most significant challenge is the effect on the residual risk pool. Carriers have developed pricing schedules with increases that are modest enough to encourage the better risks to retain coverage for at least a couple of years following the end of the level-premium term. This helps maintain some integrity to the law of large numbers, reduce claims volatility and improve block profitability.

Some companies have introduced lower initial EOLP increases that accelerate and converge with YRT rates further out, say in five years. In many cases the initial EOLP rates compare favorably with attained-age replacement rates, without the need for re-incurring the acquisition costs and the risk of the customer walking (Figure 3).
The key is attaining the appropriate EOLP rate (and increase) and retaining sufficient lives to meet profitability goals. Pricing actuaries should factor the impact of product features (e.g., ROP riders and conversion options) into their modeling. The more complex pricing will consume more resources. But as with the first scenario, this is a business decision that requires senior management input.

Figure 4: Managing for or beyond the Level Period
Each approach to managing the immediate EOLP can help life insurers maximize a block’s profitability.

There Is Still time to Reassess Strategies
Many companies have blocks of business that are reaching the EOLP term, which provides an opportunity to more actively manage lapse rates. The question is, how important is your term life portfolio to your business strategy? Companies that had planned to shock EOLP rates to induce high lapses may wish to reconsider potential profits they may forego by implementing such a strategy. Your reinsurer can help you assess your block of business and run scenarios on how changing your view on EOLP term may add both income and stability to your portfolio.