Pella, Iowa

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Special Report

Valuation & Non-Forfeiture Interest Rates May Fall!!!

By Brad Leonard, Consulting Actuary

The maximum valuation & non-forfeiture interest rates for life insurance (more than 20 years) are established for each calendar year based on a formula and Moody's Corporate Bond Yield averages for the 12 months ending each June 30. For 2005, this formula remained steady at 4½% & 5¾%. Trends are continuing downward for the 2006 computation. Lower rates increase reserves and cash values, putting pressure on profitability. As a reference, here's the way it looks 7 months before we know for sure.

The current YTD average rate through November for Moody's Corporate Bonds is 6.10% (refer to this as 'R'), which is lower than the 36-month average (must use lesser of these two averages). The 5 months following June 2004 average 6.00%. Unless this increases to over 6.21% for the 12 months ending June, 2005, valuation maximums will drop to 4% and non-forfeiture maximums will drop to 5.0%. The 6.21% is the highest rate that will still result in a valuation rate rounding to 4.0%, and result in the minimum 0.5% change. To exceed 6.21%, the next 7 months starting December 2004 must average 6.38%. At the current 6.00%, the maximum valuation rate formula is:

=.03 + .35(R1 - .03) + .175 (R2 - .09)
where R1 is lower of R & 9%
and R2 is higher of R & 9%
=.03 + .35 x .03 + 0
=.04050 = 4% [round to nearer ¼%]

The maximum non-forfeiture rate equals 125% of the valuation rate, or 5%.

Once final, the new valuation rate is effective on January 1, 2006. The non-forfeiture rate has a one-year grace period. This allows for repricing & refiling time lags. If rates go back up during this one-year grace period, the drop in rates can even be ignored for non-forfeiture purposes, but this wouldn't be definite until the end of June 2005. This has the potential to occur in the same time frame as much of the 2001 CSO product development. This "wild card" needs to be factored into strategic planning. Traditional permanent plan cash values may have to be refiled and priced for higher cash values. Secondary guarantees may cost more. Term issue ages may be affected (to avoid cash values), which can be anticipated in current pricing. Reserves would increase. Health insurance active life reserves may be affected. The new return of premium term riders may have a double whammy due to the smoothness test. And, ...

You can follow the latest monthly Moody's rate at www.naic.org, or for more information visit www.hauseactuarial.com.

Ready for Year End?

At **Van Elsen Consulting, Inc.**, we are getting ready for year end just as you are. With new staff, however, we temporarily have excess resources. Please check with us to see if we can assist you in the year-end financial process or product development that no one ever has time for in the first part of the year.

The Van Elsen Report

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    - **Simplified Issue Products**
    - **Return of Premium Term Products**
    - **Universal Life Products**
    - **Preneed Products**
    - **Final Expense Products**
    - **LTC Riders**
- ✓ **Reserve Peer Reviews**
- ✓ **Review of "XXX" X-Factors, Significantly Reducing Initial Reserve Strain**
- ✓ **Assistance with Reinsurance Negotiations**
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