STATE OF NEW YORK

DIVISION OF INSURANCE

Testimony of Philip J. Bieluch at the

Public Hearing on Plan of Reorganization

Of Metropolitan Life to Convert from a Mutual Insurance Company

To a Stock Insurance Company

My name is Philip J. Bieluch. I am a resident of Southborough, Massachusetts. I am a Fellow of the Society of Actuaries and a member of the American Academy of Actuaries.

Closed blocks, in general, and as funded by Metropolitan Life, cause concern in a few areas. I would like to call the department's attention to a paper titled "Closed Blocks and Mutual Company Conversions" as published by the Society of Actuaries in the Society of Actuaries Financial Reporting Section Monograph M-AS99-1, dated October, 1999. The paper was written by Messrs. Charles Carroll and J. Peter Duran, both partners at Ernst & Young LLP. I have a copy of the paper, as published, to enter into the record. In the paper, the authors discuss a general principle of dividends after demutualization as follows:

> "This line of reasoning, we believe, leads to a general principle which could be stated as follows: when experience changes, dividends should be adjusted in the same manner that they would have been adjusted in the absence of a demutualization."

Metropolitan stated a similar purpose in their Policyholder Information Statement, Part One, page 44 as follows:

> "The Closed Block is provided for in the New York Insurance Law to ensure that policyholders' reasonable dividend expectations will be met after a mutual insurance company converts to stock form."

One area where Messrs. Carroll and Duran find this principle violated is the impact of persistency on dividends. As stated by Messrs Carroll and Duran:

> "The typical dividend formula used by most mutual companies does not have a specific factor that recognizes the effect of persistency."

They recognize that:

> "The formation of a closed block can change this situation dramatically, a fact that was recognized and commented on by the Task Force in its report. In fact, the establishment of a closed block will require at least an implicit recognition of persistency differences"

Nothing provided by Metropolitan in the policyholder mailings discusses persistency's effect on policyholders' dividend expectations. In fact they state just the opposite when they state in the Policyholder Information Booklet Part One page 45 the following:

> "The principles and methodologies used to develop the current dividend scales were not materially different from the principles and methodologies used to develop dividend scales in recent years."

Investment income creates another concern with the closed block. Messrs. Carroll and Duran state:

> "Formation of a closed block essentially mandates a form of asset segmentation. This fact has an important consequence. Since the company must honor the guarantees in closed-block policies, whether or not the closed-block assets prove sufficient, while better-than-anticipated returns on closed-block assets go entirely to benefit policyholders, there is an incentive for the company to invest closed block assets in relatively safe, but low-yielding investments."

Again nothing provided by Metropolitan in the policyholder mailings discusses this effect on policyholders' dividend expectations.

Messrs. Carroll and Duran offer a remedy to the above concerns as follows:

> "a more direct approach would be for the mutual insurer to commit as part of the plan of conversion to continue to determine dividends on pre-conversion policies using the same practices used in the past."

Dividend eligibility, which the mailings say will not be changed, is not the same as dividend amounts. Policyholders cannot evaluate worth of the stock offered as compared to lower dividend expectations created. The Metropolitan has not stated that dividend amounts will not be changed due to the demutualization. I ask the department to consider such a requirement as a condition of approval.

Metropolitan has stated that there are 600,000 policyholders for whom they do not have a current address. Many of these policyholders may be currently deceased. A company with approximately 400,000 policyholders who they could not locate, John Hancock, discovered tens of thousands of probably dead policyholders when the records of lost policyholders were matched against the voter registrations in just a few states.

Until the Superintendent is aware of how many of Metropolitan's in-force policyholders are actually found to be dead, it would be impossible to determine a mortality assumption for the lines of business. Finding these policyholders could cause Metropolitan's estimate of incurred by not reported death claims to be too low affecting their reported profit. In addition, the funding of the closed block could be inadequate as the mortality rates that Metropolitan assumed were based upon mortality experience before these policyholders are found.

Consider the following quote from the Closed Block Memorandum on page 13:

> "The 1998 mortality study was considered in determining the 1999 dividend scale. This study was based on experience in 1997. It shows that over this period actual mortality was approximately 68.2% of an expected mortality table developed by MetLife. For Closed Block funding purposes, mortality of 68.2% of these expected rates were assumed for Closed Block Funding."

A company with such a rich history of mortality studies, having published the Statistical Bulletin for most of this century, should have a very good grasp on the number of policyholders expected to be deceased.

Many of these lost policyholders probably are industrial policyholders. Industrial life premiums have been waived by the Metropolitan since 1981 resulting in a lack of yearly interaction with the policyholder.

The following is a quote from a report titled The Negro in the Insurance Industry as published by the Industrial Research Unit, Department of Industry, Wharton School of Finance and Commerce.

> "Negroes represent one of the largest consumer groups that purchase industrial insurance."

Metropolitan's own statistics bear this out. Consider statistics published by the Metropolitan in a publication of the Actuarial Society of America, Transactions, Volume XXI, Part One as follows:

> "Number of Colored Premium-Paying Policies In Force December 31, 1919 and Percentages, Respectively, of the Total Premium-Paying Policies In Force Ordinary 1.53%, Intermediate 12.31%, Industrial 11.96%."

I have a copy of both of these references to enter into the record.

Before approving the plan, I ask the Superintendent to require Metropolitan continue the search for these lost policyholders by attempting to work with government officials in all jurisdictions where Metropolitan is licensed for find these policyholders. Any remaining policyholders who are not found should be part of an outreach program. To just stop looking for these policyholders would continue the discrimination of the past.

If the closed block is implemented, I ask the Superintendent to insure that the final funding of the closed block not be determined until:

- Government officials in all jurisdiction where Metropolitan is licensed have reported the results of their search for lost policyholders,
- adjustments are made to reflect the fact that the remaining lost policyholders may all be dead,
- the impact of paying these expected claims is used to adjust the Metropolitan mortality experience on these lines of business,
- the impact of this adjusted mortality is used to calculate a new closed block funding amount.

To do otherwise would penalize policyholders in the closed block and benefit the stockholders of Metropolitan for Metropolitan's inability to maintain a minimal level of customer service with a substantial block of their policyholders.

In a paper prepared for the United States Commission on Civil Rights titled "Consultation on Discrimination Against Minorities and Women in Pensions and Health, Life, and Disability Insurance" the following is stated on page 21 concerning industrial insurance:

> "Then, for many years, lower benefits or higher rates were applied to policies issued to blacks. Several techniques were used. One was to provide a death benefit on policies issued to blacks 2/3 of that provided on comparable policies issued to whites; another to classify all blacks automatically as substandard, subject to higher premiums, and almost all whites as standard. These distinctions were abandoned in 1948 … by the Metropolitan … for new issues. [C]ompanies … began programs for equalizing benefits for existing policies"

I have a copy of this paper to enter into the record.

In a book titled <u>The Metropolitan Life – A Study in Business Growth</u> publish in 1947 and excerpted in the paper, the following is stated:

> "The same general approach as in industrial was tried in 1930, but discontinued at the beginning of '35. At that time a simpler overall rule was adopted under which the excess mortality was offset by paying only partial commissions on policies issued to Negroes.
>
> In May, 1935 the New York State anti-color discrimination law was stiffened to forbid any distinction because of race in the amount of commissions paid for writing the policy. Thereupon Metropolitan

> discontinued soliciting colored risks for any kind of life insurance in New York State."

The actuarial contribution memorandum does not discuss giving these policyholders any additional share allocations. I ask the Superintendent to review these practices to ensure that the policyholders' contributions calculated for these policyholders reflect the additional costs these policyholders were forced to incur due to this discrimination. To not give these policyholders additional shares represented by the additional premium charges, reduced benefits or reduced commissions continues the discrimination by Metropolitan Life.

This concludes my remarks.

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