

WHERE IT REALLY DOES MATTER...

In our accompanying article we argued that the market can live with imperfect risk selection. And to quote from it: “No life company is going out of business because its mortality/morbidity book is a disaster...”. We stand by that, of course. Companies run far bigger risks and face tougher problems elsewhere compared with mortality/morbidity experience. But in the interests of optimising returns, life companies – and their reinsurers – might want to take a closer look at the performance of their critical illness (CI) and income protection (IP) books.

IP has long been a problem product, subject to the vagaries of national and household economics, and trends in consumer attitudes to work, leisure, value for money, honesty, insurance and insurance claiming. (Conceptually, IP is a great product but can it really operate successfully in modern, westernised societies?) Over the years claims handling and control have been improved and the lessons learned have been passed on to underwriters. But risk selection and pricing is still weak, and profitability still borderline and too volatile.

The problems of IP have recently been overshadowed by CI. We won't set out here the list of CI issues since they are known well enough, but there are real uncertainties over profitability, and opinion is sharply divided over guaranteed premium rates. If one looks hard enough one might be able to see a big question mark hanging over CI as we know it in the UK.

So here are two products for which a change in the underwriting status quo *could* just make a difference.

To take IP first, most of the areas of risk assessment are pretty well sewn up – although underwriters could usefully worry less about isolated episodes of backache and suchlike, and look more closely at how multiple risk factors – not just medical ones – interact. Occupational rating, however, is a very hit and miss affair. While occupation guides contain thousands of job titles, the groupings are very approximate and take little account of duties, responsibilities, type of employer (where relevant) or working conditions. Some occupation declarations on application forms are very imprecise and say nothing about the make-up of the job in terms of such key factors as:

- Physical work
- Position of work – sitting, standing, contorted positions, etc
- Work at heights (and not just above the traditionally crucial 40ft/12m threshold)

- Mix of outdoor and indoor work
- Use of machinery
- Manual dexterity
- Use of fine judgment
- Boring, repetitive work, with all that implies for job satisfaction and motivation.

And yet the characteristics of the occupation and the applicant's attitude to it are key risk factors.

In CI it seems odd that a product that is so very different to life cover is assessed in almost exactly the same way, albeit with a few additional questions on the application form perhaps. Given that cardiac-related events are covered, it would be useful to know about blood pressure and lipids. Diabetes is another risk factor for coronary disease, yet overweight applicants at risk for or even suffering from the metabolic syndrome and type 2 diabetes are not investigated further. So how about an accurate BMI and a check on blood sugar or glycated haemoglobin as well? Social class is a major determinant of the incidence of disease and is an additional indicator of cancer risk alongside smoking.

So one can make a reasonable case for tighter screening and finer risk pricing for IP and CI, through better application forms, tele-interviewing and additional medical evidence – and the likelihood is that the better experience would repay the higher initial costs involved. But it all runs contrary to the traditional philosophy of a simple, fast new business process. And more evidence is certainly inconsistent with lower costs, even with 'minimalist' screenings like pharmacy screenings and 'paramed lights'.

Of course, skilled tele-interviewing can elicit a lot of useful information in the context of IP and CI, especially where occupation is concerned. But there is a problem in reconciling the extra detail on application forms and from tele-interviews with a need to process the information via a rules engine for low-cost instant acceptance. This difficulty is not impossible to resolve but it does need some careful thought.

So again we ask whether things might change. In the case of IP it depends on whether life companies care enough about the profitability of the portfolio – and how much their reassurers lean on them. It should be relatively easy to introduce application process changes for a niche product like individual IP.

For CI it is more difficult: the market is competitive and, not least, innovation is inhibited by statements of best practice. But a new approach to risk selection and pricing could just be part of a bold new proposition that gave a firm a new form of competitive advantage. And it might just help secure the long-term future of CI as we recognise it now.