

The Actuarial Profession
making financial sense of the future

Health and Care Conference 2011
Joan Coverson

Income Protection Current Topics

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Healthcare Convention 2011
Joan Coverson

Discounts for Lives with Exclusions

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Buying a Car



You want one of these

Would you buy one of these?



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Buying an IP Policy

IP Policy
Cover for all
causes

You want one of these

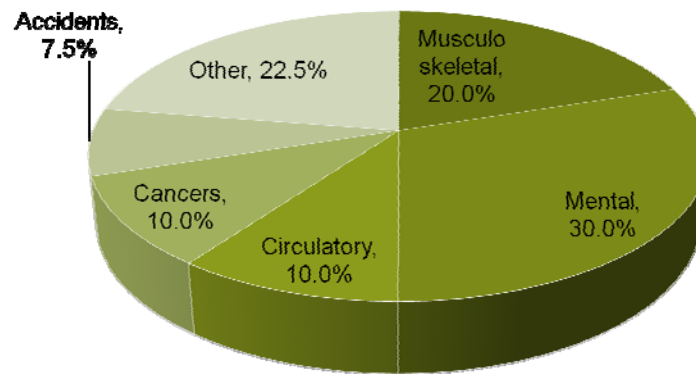
Would you buy one of these?

IP Policy
•Restricted cover
•Same price

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Sample Split of IP Claims by Cause



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The Two Viewpoints

- Consumer Benefits
 - Reduced coverage should cost less than full coverage
 - Makes product more attractive to those with pre-existing conditions
- Insurer
 - Reduction in price vs. reduction in risk

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Calculating the Discount

- Reduction in claims cost from excluded cause
- Do excluded lives have different incidence rates to standard lives from other causes?
- Do excluded lives have different claim durations from other causes?
- If excluded lives claim for a valid cause will it worsen their excluded condition?
- Possibility of fraud
 - Cannot claim on excluded condition so claim on something else

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Mental Illness

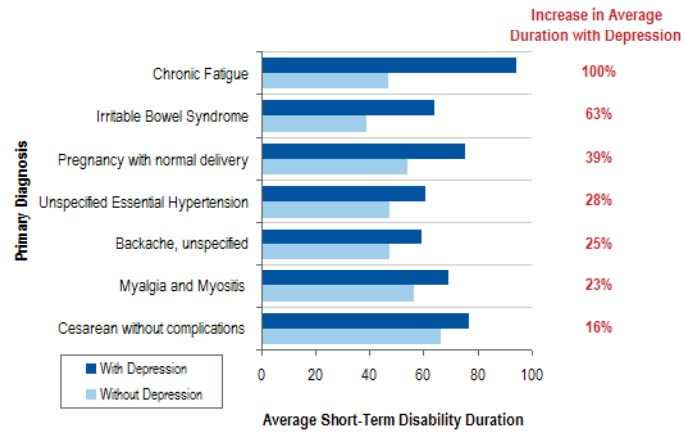
- Many studies prove links between depression and other illnesses
- Links to
 - coronary heart disease, stroke, colorectal cancer, back pain, irritable bowel syndrome, multiple sclerosis, and possibly type 2 diabetes
- Depressed patients have worse outcomes than those not depressed
- Increased incidence from non-mental causes
- Longer claims

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Claim Duration

Health Issues with Depression Lead to Longer Absences



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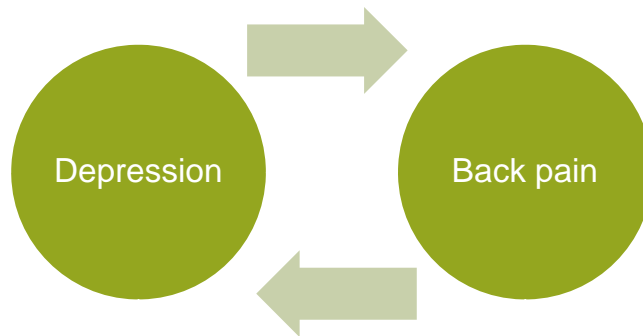
Effect on Non-Excluded Conditions

	Mental Illness
Higher incidence on other causes	Yes
Longer claim duration	Yes
Recurrence of excluded condition	Yes
Fraud	?

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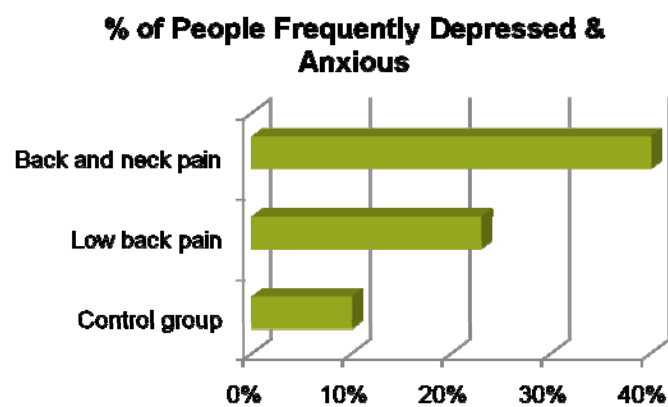
Musculo Skeletal



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Musculo Skeletal



Increased risk of respiratory, cardiovascular, stomach ulcers, inflammatory bowel problems, other forms of chronic pain, cancer and diabetes

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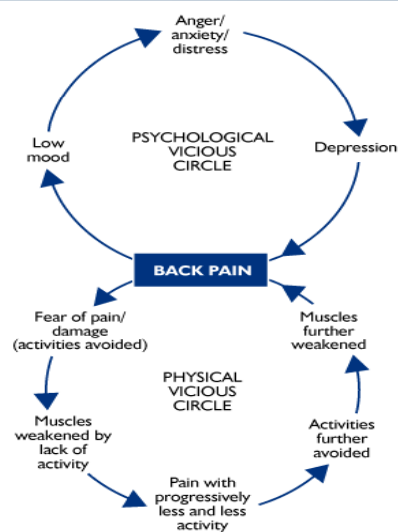
Some more Statistics

- Co-morbid problems identified in up to 87% of those with chronic spinal pain, including :
 - mental disorders (35%)
 - chronic physical conditions (55%)
 - other chronic pain (69%).
- The longer the person has experienced the back problem the more likely they are to develop co-morbid conditions

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Depression Disability Spiral



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Effect on Non-Excluded Conditions

	Mental Illness	Musculo-Skeletal
Higher incidence on other causes	Yes	Yes
Longer claim duration	Yes	Yes
Recurrence of excluded condition	Yes	Yes
Fraud	?	Possible

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Balance of Risk Example

		Relative Rates	Relative Risk 1	Relative Risk 2	Relative Risk 3
Standard Lives	95%	1.00	100%	100%	100%
Lives with Exclusions	5%	0.8	80%	100%	120%
Total rate		0.99	0.99	1.00	1.01
Loss			0	1%	2%

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Conclusion

- Lives with exclusions are not standard risks in other respects
- Standard lives cross-subsidising lives with exclusions
- Risk is not reduced by reduction in claims cost for that cause
- Smaller (or nil) discount justified
- Or even “Exclude and load”
 - US approach

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Income Protection

Guaranteed Income at Claim

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Buying a TV



You pay for this

How would you feel if you got this (same price)?



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IP - You don't always get what you pay for

- Maximum benefit formula
 - Designed to limit replacement ratios
- Benefits often reduced
 - Earnings at claim < declared earnings at inception
 - Other income
- Rationale

– Reduce potential for over-insurance	→	<i>non-disclosure</i>
– Incentive to return to work	→	<i>longer claims</i>
– Affordability	→	<i>persistence</i>



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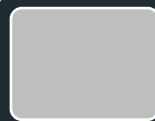
Extent of Benefit Reductions

- Typical reductions in claim amounts
 - 10% - 15%
- Less at lower benefit levels
- Largely unaffected by
 - Occupation class
 - Deferred period
- Reasons for reductions
 - Rehabilitation benefits
 - Proportionate benefits
 - Maximum benefit formula

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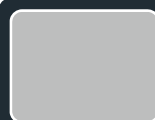
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The Alternative *You Get What You Pay For*



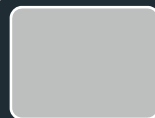
Customer Satisfaction

Benefit Insured = Benefit Paid



Advisor Satisfaction

Fair / Easier to explain to customer



Insurance Company

Can the risk be managed?

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Products Available Worldwide

- Financial underwriting at outset & claim (e.g. UK)
- Financial underwriting at outset / not claim (e.g. Germany)
- Optional (e.g. Australia and New Zealand)



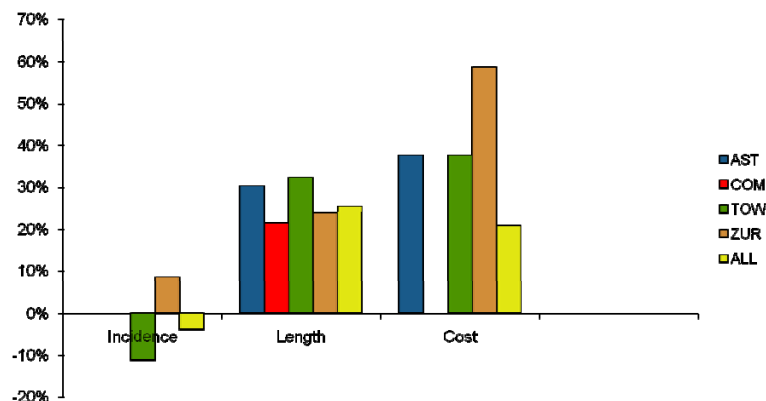
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Australia *Agreed Value vs. Indemnity*



Excess performance index for agreed value over indemnity

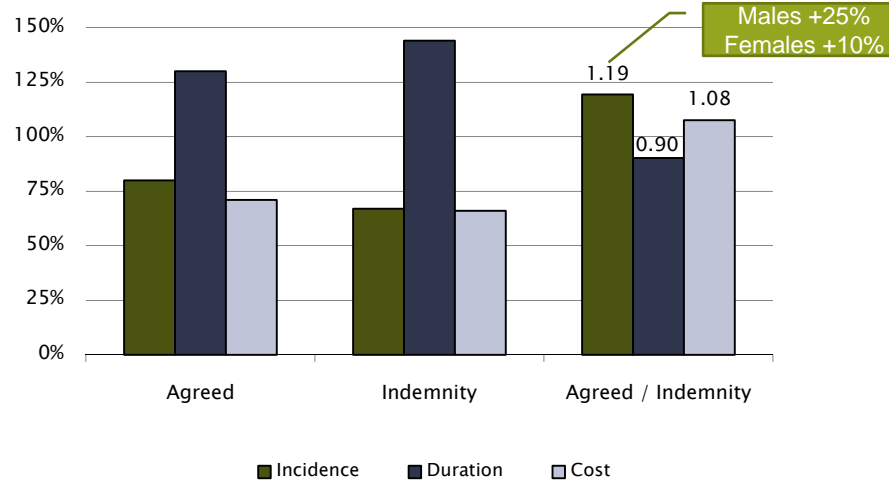


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New Zealand Gen Re IP Survey 2004 - 2008



Ratios (%) of actual to expected results by benefit type



Presentation for TOWER, July 2008

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New Zealand Gen Re IP Survey 2004 - 2008



Table 15.1 Profile of business written under each benefit type in 2004-2008

	Agreed Value	Indemnity
Occupation White-collar	73%	73%
Deferment Period 30 day	44%	39%
Deferment Period 90 day	35%	42%
Benefits to 2-10 Years	18%	19%
Benefits to Age 60, 65, LT	80%	80%
Male	73%	73%
<i>Insured Benefit</i>		
Less than \$1000/m	9%	4%
\$1000-1999/m	18%	12%
\$2000-2999/m	26%	27%
\$3000-3999/m	18%	22%
\$4000-4999/m	11%	13%
\$5000-5999/m	7%	8%
\$6000/m and Over	11%	12%

Presentation for TOWER, July 2008

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Australia & NZ



- Agreed value products have higher claims cost than indemnity
- Agreed value vs. indemnity pricing
 - Australia approx +15%
 - New Zealand approx +10%
- Link between type of product purchased and employed / self-employed

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Employed vs. Self-Employed

- Employed
 - Understand earnings at policy application
 - Generally salaries rise rather than fall
 - If employed at claim good incentive to return to work
- Self-employed
 - Can be difficult to determine earnings at outset
 - Earnings can fluctuate
 - Potential to claim / return to work influenced by performance of business

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Factors Affecting Cost



- Employment status

Employed



Self-employed

- Replacement ratio

Low



High

- Need

Mortgage



Income
replacement

- Amount of cover guaranteed

None



Total benefit

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Factors Affecting Cost

- Financial underwriting at outset and claim
 - Lowest cost
- Offer choice
 - Financial u/w at claim or outset (policyholder choice)
- No financial u/w at outset or claim
 - Use financial evidence from elsewhere (e.g. mortgage or loan)
- No financial underwriting at all



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Employed vs. Self-Employed *? Different Options*

- Different price to match different risk
- Different maximum benefits
- Different benefit levels for no financial underwriting

- But practically difficult!

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Conclusion

- Options available to make product more attractive to customers and advisers
- Most will increase price
- Management of risk important

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