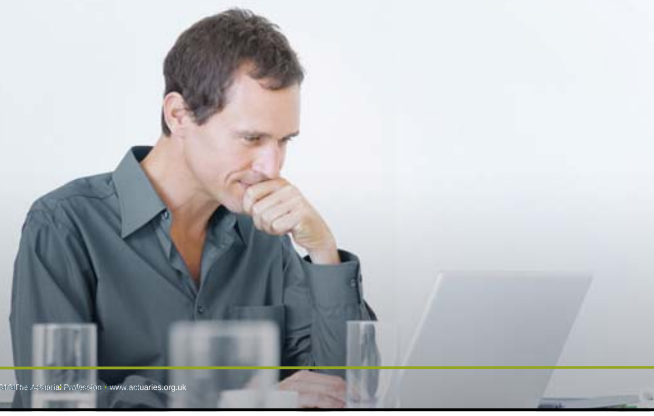
The Actuarial Profession
making financial sense of the future

E3: Effects of the ABI Non-Disclosure Code of Practice
An update from Royal London and SCOR Global Life



02 May 2012

E3: Effects of the ABI Non-Disclosure Code of Practice
An update from Royal London and SCOR Global Life

Agenda
What is TCF and when did it begin?
Claims in the old world Vs Claims in the new world
Law Commission/ABI update
What did Royal London and SCOR expect at the time?
Cost to the industry – what we thought then
Observed claims data – Facts and figures
SCOR revised TCF basis and reasons for change
Cost to the industry – what we think now
Where are we now
What next?

What is TCF and when did it begin?

- In 2001, the Financial Services Authority (FSA) launched the Treating Customers Fairly (TCF) initiative
- Designed to restore consumer confidence in the financial services industry
- Followed up in 2006 when the FSA published a set of "Six Consumer Outcomes"

  - **Outcome 1:** Consumers can be confident that they are dealing with firms where the fair treatment of customers is central to the corporate culture.
  - **Outcome 2:** Products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and are targeted accordingly.
  - **Outcome 3:** Consumers are provided with clear information and are kept appropriately informed before, during and after the point of sale.
  - **Outcome 4:** Where consumers receive advice, the advice is suitable and takes account of their circumstances.
  - **Outcome 5:** Consumers are provided with products that perform as firms have led them to expect, and the associated service is of an acceptable standard and as they have been led to expect.
  - **Outcome 6:** Consumers do not face unreasonable post-sale barriers imposed by firms to change product, switch provider, submit a claim or make a complaint.

Claims in the old world

Categories for non-disclosure

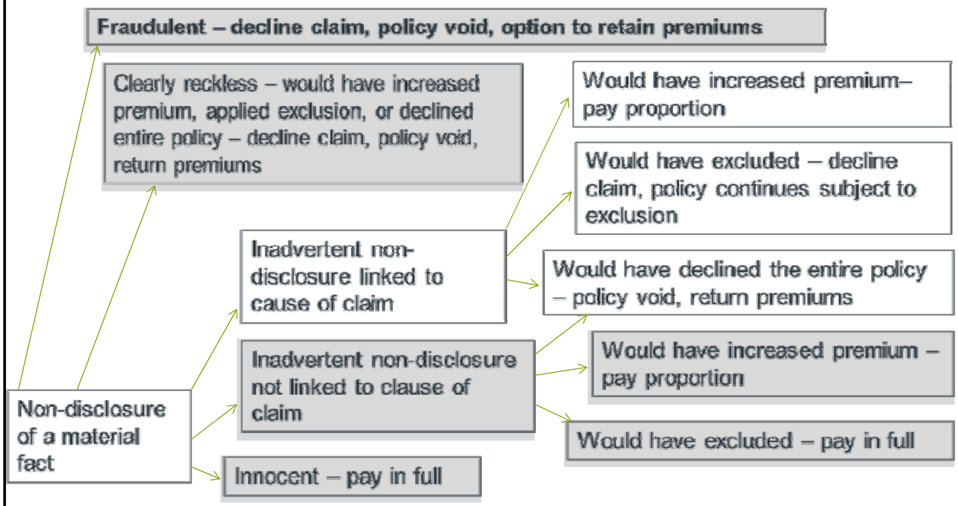
Insurance

- Innocent
- Inadvertent
- Clearly Reckless
- Fraud

Law

- Innocent
- Negligent
- Fraud

Claims in the old world



Claims in the old world

Case Study

- Male applicant, age 40, Office Worker, no medical disclosures.
- Policy to cover Life, Critical Illness (CI) and Total Permanent Disability (TPD) at Standard Rates
- Makes a claim 1 year after inception due to Testicular Cancer
- Full medical records (FMR's) obtained as a standard requirement
  - FMR's reveal a 20 history of back pain
  - Occasional time off work
  - Has had x-rays and MRI scans
  - Previous physiotherapy, chiropractor, pain management
- Retrospective underwriting terms would be to allow Life and CI at standard rates – Decline TPD
- Cancer is invasive and so medically this is a valid claim

- ***Would you pay this claim?***

Claims in the new world

ABI Guidance – Non-Disclosure and Treating Customers Fairly Claims For Long-Term Insurance Products – January 2008

Claims in the new world

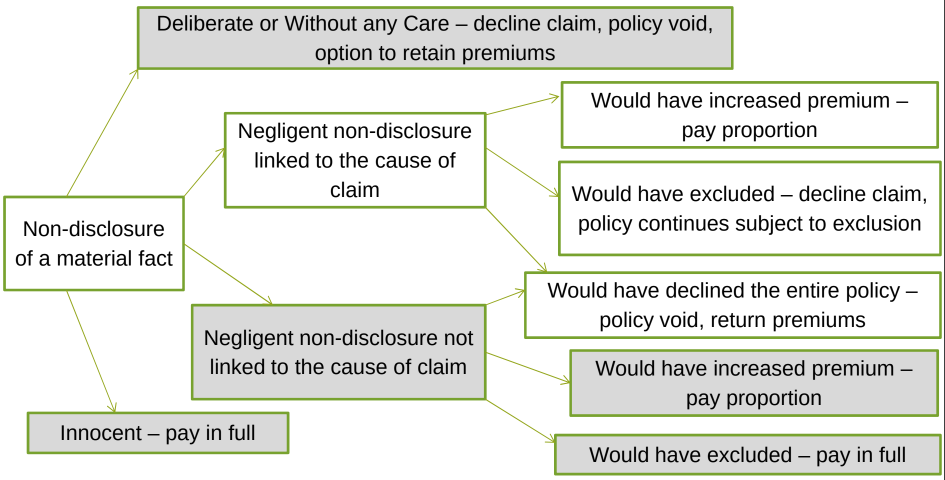
The new categories for non-disclosure:

- Innocent
- Negligent
- Deliberate or Without Any Care

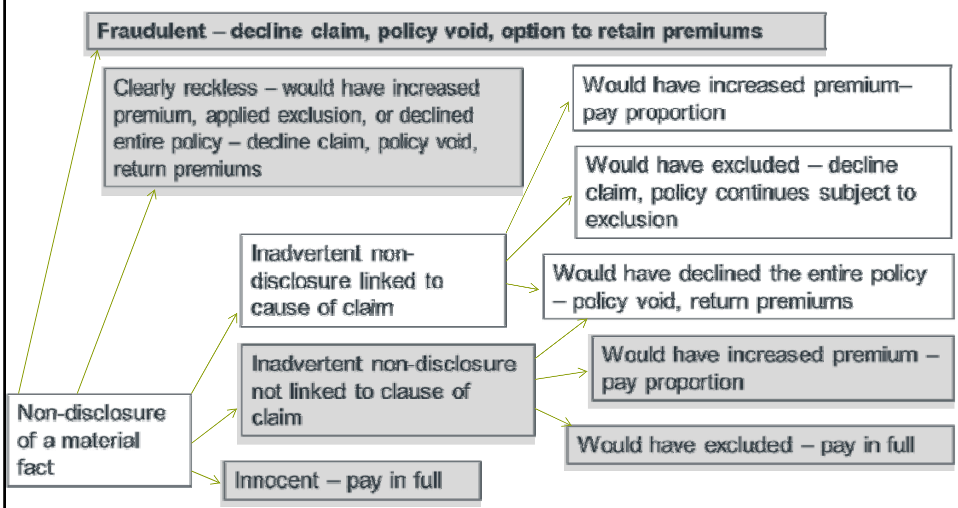
Key facts

- Target evidence
  - No fishing for evidence
- Interview of claimant
  - What do they know?

Claims in the new world



Claims in the old world



Claims in the new world

Case Study

- Male applicant, age 40, Office Worker, no medical disclosures.
- Policy to cover Life, Critical Illness (CI) and Total Permanent Disability (TPD) at Standard Rates
- Makes a claim 1 year after inception due to Testicular Cancer
- Condition specific report obtained from GP with hospital reports
  - Hospital reports give a brief mention of history of back pain
  - Evidence suggests some investigations and treatment – nothing major
- Retrospective underwriting terms would be to allow Life and CI at standard rates – Decline TPD
- Cancer is invasive and so medically this is a valid claim
- Phone call to claimant to ask why back problem not disclosed. He advised it never kept him off work so didn't really think it was an issue

- ***Would you pay this claim?***

Law Commission/ABI update

David Herzell – Law Commission

- EU looking to harmonise insurance law, therefore this new law will give the UK a good place for negotiations
- Bill received Royal Assent on 08 May 2012, likely to commence in 12 months (this is the treasury's call), therefore expected March 2013.
- Act only affects consumers, not businesses

Nick Kirwan - ABI

- Retain the ABI Code of Practice (CoP) and used retrospectively. Act will only apply to policies written from March 2013
- 3 main differences in scope between the ABI CoP and the Act:
- CoP only applies to long term insurance policies – Act applies to all consumer policies
- CoP only applies to non-disclosure noticed at point of claim – Act also applies to non-disclosure noticed at other times, e.g. policy alterations
- There are also 3 areas where the CoP offers more consumer protection than the Act:
  - Not categorising any non-disclosure as 'deliberate or without any care' when the underwriting terms would have been affected by no more than +50%/£1pm
  - Allowing minor benefits to be split from major benefits so non-disclosure under a minor benefit will not affect a claim under a major benefit
  - Only retaining premiums in the event of fraud

What Did Royal London expect at the time?

- An increase in the proportion of claims paid.
- Less claims referred to the FOS.
- A higher proportion of FOS referred claims upheld.
- A potential for increasing reinsurance costs.
- Some companies increasing prices.
- Expansion of the market.

What did SCOR expect at the time? – Part 1

- A price change because
  - Claims that were previously declined now being paid proportionately.
  - A softened claims philosophy leading to more non-disclosure being categorised as inadvertent rather than deliberate.
  - Less ‘fishing’ for reasons to decline claims. Need specific reason to request claimants medical records.
- In Force Cost
  - Life 1.25%
  - Critical Illness 1.75%

What did SCOR expect at the time? – Part 2

- Smaller Cost to New Business
  - Better Application process
    - ⇨ Less Non-Disclosure
    - ⇨ Less Impact of Non-Disclosure Code of Practice.
  - Life 1%, Critical Illness 1.25%
- Numbers impacted by spottable 'ND' assumption which assumed we stop checking for ND after 5-years for life (generally accepted) and 10-years for CI.
- Income Protection – A Higher cost than for Critical Illness
  - Lower standard rates
    - ⇨ More non-disclosure
    - ⇨ Larger Impact (1.5%)

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Cost to the Industry – What we thought then

Life

• Annual IF Premium	= £2,930 million
• Claims cost	= 1.25%
• Percentage of premium that covers claim cost	= 60%
• Total Annual Cost	= £22 million

Critical Illness

• Annual IF Premium	= £1,184 million
• Claims cost	= 1.75%
• Percentage of premium that covers claim cost	= 60%
• Total Annual Cost	= 12.5 million

Average duration of 5 years => £35m x 5 = £175m

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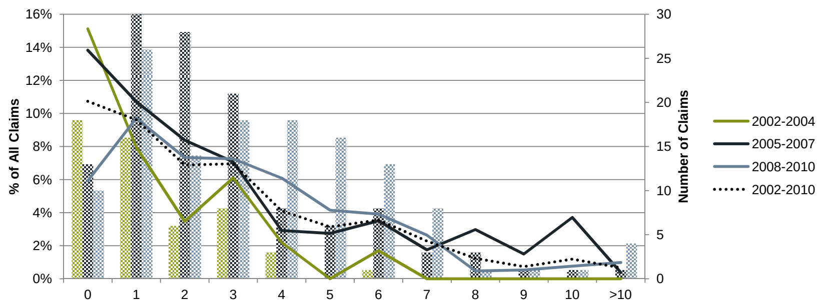
Association of British Insurers

SURVEY OF LIFE & CI CLAIMS PAID AND DECLINED	2007	2008	2009	2010
All Death and CI Claims Received	47,100	39,747	42,745	42,657
Total claims paid	43,700	37,325	40,633	40,660
Claims paid as a percentage of claims received	89.0%	93.9%	95.1%	95.3%
Claims declined as a percentage of claims received	11.0%	6.1%	4.9%	4.7%
Declined claims due to non-disclosure (% of claims received)	8.0%	3.0%	2.0%	2.0%
Death claims				
Total TA - Death claims paid	33,200	24,196	28,549	29,182
TA - Death claims paid as a percentage of claims received	97.0%	97.2%	98.0%	98.2%
TA - Death claims declined as a percentage of claims received	3.0%	2.8%	2.0%	1.8%
CI & TPD claims				
Total CI & TPD claims paid	10,500	13,129	12,083	11,478
CI & TPD claims paid as a percentage of claims received	82.0%	88.4%	88.8%	88.7%
CI & TPD claims declined as a percentage of claims received	18.0%	11.6%	11.2%	11.3%

Code introduced

Life Declines by duration – SCOR Analysis



- Not a great amount of data
- Shows cut off of declined claims around Dur 5-6
- 08-10 marginally less declines than before

Declined Clms	Total
2002-2004	5%
2005-2007	5%
2008-2010	4%
2002-2010	5%

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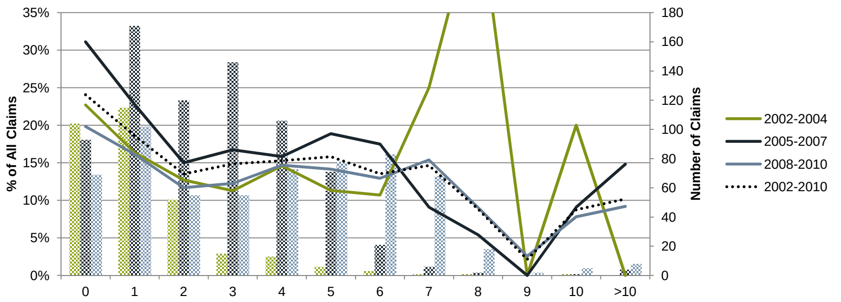
CI Declines by duration – SCOR Analysis



- Good amount of data
- No clear cut-off of decline claims after year 2
- Split be triennia shows changes in industry claims philosophy in 00's

Declined Clms	Total
2002-2004	16%
2005-2007	18%
2008-2010	14%
2002-2010	16%

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FOS Complaints – Royal London Analysis

- There has been a drop in the proportion of disputed claims that have been referred to FOS.

	2005-2007	2008-2010
Number of Cases Referred to FOS	21	29
Proportion of total submitted claims	4.1%	2.4%
Proportion upheld by FOS	86%	55%
Proportion overruled by FOS	14%	45%

- However, the success rate has also declined. Why?
  - Categorisation of non-disclosure?
  - Justified evidence?
  - Lifestyle issues?

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Impact of Proportionate Claims

- Has been difficult to obtain market statistics on this.
- Anecdotal evidence is that percentage of proportionate payments jumped from 2007 to 2008 for new philosophy, but then have reduced since.
- Royal London part-payments as a proportion of all claims paid have always been small, but a small increase was observed:

2005	2006	2007	2008	2009	2010
1.2%	1.3%	2.1%	3.5%	1.6%	2.2%

- Retrospective terms?
- Categorisation?
- Lifestyle and family history still big issues?

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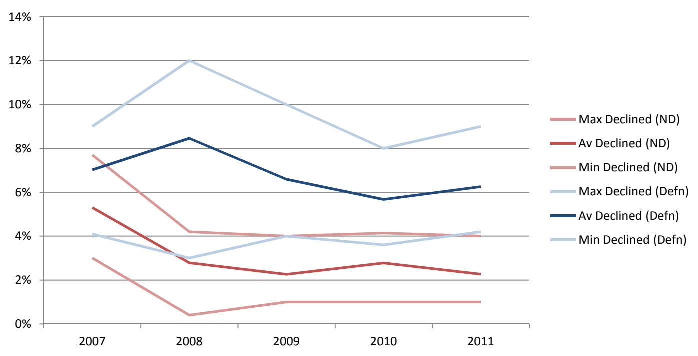
Average declined CI Claim Stats based on industry published data



- 2007 data based on only 4 companies, whereas data afterwards based on 10 UK IFA companies.
- As well as the expected decrease in declined claims due to non-disclosure, published stats also show a fall in declined claims due to not meeting the definition.
- Number of reported declinatures lower than SCOR experience - possible massaging of the numbers?

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SCOR Revised TCF Basis and reasons for change

- Weakness of original work was that it did not take account of pre - 2008 declined claims statistics
  - Differential of Declined claims due to ND between Life and CI does not support small differential of original impact of 1%/1.25%.
- Larger CI impact due to FOS interaction.
- Less durational impact of Declined claims for CI as expected.
- Revised assumptions predominately based on internal claims data, but also guided by published industry statistics
  - Life = 0.5%
  - Critical Illness = 4%
  - IP - light on data, but anecdotal evidence has led us to 7.5%

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Cost to the Industry – What we think now

Life

- Annual IF Premium = £2,930 million
- Claims cost = 0.5%
- Percentage of premium that covers claim cost = 60%
- Total Annual Cost = £9 million

Critical Illness

- Annual IF Premium = £1,184 million
- Claims cost = 4%
- Percentage of premium that covers claim cost = 60%
- Total Annual Cost = £28.5 million

Income Protection

- Annual IF Premium = £483 million
- Claims cost = 7.5%
- Percentage of premium that covers claim cost = 60%
- Total Annual Cost = £22 million

Average duration of 5 years => £60m x 5 = £300m

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Where are we now? - Insurers

- No increase in overall sales volumes.
- Prices have continued to decrease, though rate has slowed.
- Claims paid rates are up.
- Margins are level, or possibly up, depending who you believe.
- Cost of contested claims is down.
- Less honest customers have benefited more from the changes.
- Overall positive result.

Where are we now? - Reinsurers

- Decent level of post-TCF data, with fairly stable published decline rates since 2009
- Important to keep monitoring
  - Law Commission/FOS interaction could have a small impact
  - CI declines at longer durations (as experience develops)
- Target evidence requests
- Claimant interviews
- Review of sales process

What next?

- Reconsidered our assumptions for all our books:
  - Quantifying the effect is still important, particularly for reviewable business.
  - More experience allows us to examine durational effects with more confidence.
  - ...and the impact on benefits where there are fewer claims – i.e. IP.
- Continuing to use FOS liaison work to assert industry's interpretation of the Code of Practice.
- Post-issue non-disclosure sampling.
  - May lead to further application form changes.

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Questions or comments?

Expressions of individual views by members of The Actuarial Profession and its staff are encouraged.

The views expressed in this presentation are those of the presenter.

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