SOCIETY OF ACTUARIES

Article from:

News Direct Newsletter

September 2003 – Issue No. 44

But Will They Buy?

Insurance Coverage for All...And How Insurers Can Afford To Provide It

Review by Ian Duncan

Editor's Note: Published by Actex Publications Inc., Winsted CT, at $45.00 plus shipping and handling ($7.00). Available from Actex Publications at www.actexmadriver.com *or 800-282-2839.*

Maria Thomson has done the industry a service with her new book, "Insurance Coverage for ALL…and How Insurers Can Afford to Provide It." Inside this thin book (88 pages, including notes, so you can finish it in one sitting) is a fatter book, longing to be written. It is a stimulating read, raising a number of different issue. It should lead to some lively debate, and, I hope, further analysis.

Maria's basic philosophy is that insurance is a GOOD THING, and therefore we should all have more of it. She does an excellent job of reminding us of lines of insurance in which penetration is low, and for which more coverage would be beneficial to her target population (roughly, middle-class employed people), such as disability income. The concept need for insurance coverage is one that could benefit from further analysis: all people are not equal, and the need for, type and amount of coverage appropriate for different profiles of the population varies by, amongst other factors, age, family composition, marital status, stage of life, resources and wealth, access to social and government programs, level of risk tolerance, etc. The relative aging of the population, the decrease in the (child) dependency ratio, the increase in the number of two-earner families over the past 20 years, and the increase in alternative and more attractive investment vehicles hardly make it surprising that life insurance ownership has fallen. To this list I will add the failure to develop new products to meet emerging needs. (More about this later.) Despite all these changes, the percentage of households that own life insurance was 76 percent in 1998, so household penetration does not appear to be an issue. Those households that do own life insurance appear to be able to replace between 1.8 and 4.4 years of income with their insurance amounts. I suspect that these replacement ratios are the source of the notion that the public is inadequately covered with life insurance.

Maria's thesis can be summarized briefly as follows:

1. Insurance companies have abandoned the middle-class market to focus on the affluent.
2. Most people have inadequate insurance for their needs.
3. Selling in the traditional model is becoming cost-prohibitive.
4. Traditional underwriting is slow and expensive, making buying difficult.

This leads to her recommendations for the industry:

1. Develop more simple products.
2. Focus on faster and more streamlined issue processes.
3. Develop alternative channels such as work-site marketing and bancassurance.

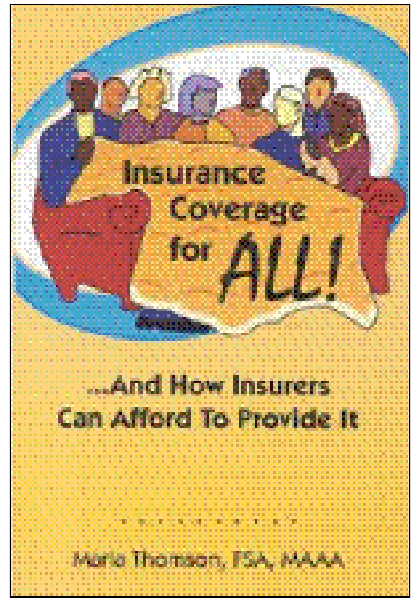
The discussion of the rise and fall of the debit market wa s, for me, one of the more interesting sections of this book. The puzzling issue, however, is why the debit insurance market died, rather than evolving to a form of distribution like the Avon, Longaberger or Tupperware models. I would have liked to read more about the bancassurance market, which has arguably not taken off in the United States Maria tells us that it has been successful in Europe; it has been tried in Canada, and some Canadian experience would be helpful.

The discussion of product development focusing on needs of the target population is a useful one that deserves expansion. One of the interesting consequences of focusing on need as the basis of product design is that you end up with rather messy products that do not fit easily into existing "buckets". I recently ran a client seminar on needs-based product design, focusing on "End-of-Life" as an event. While the financial risk of expenses at the end-of-life is not necessarily as high as that faced by young families, these expenses can be substantial and diverse (acute medical, custodial, burial, rehabilitation, lost income, etc.). There are sources of finance that offset the risk (accumulated assets, government and social programs, insurance products) but for the average consumer, "sources and uses of funds" in connection with end-of-life events is a daunting task to master in a short space of time. The good news from our seminar was that there are ways to re-engineer existing products to do a better job of serving these needs.

When it comes to finding ways to provide broader coverage for a large number of households, we should not overlook group insurance. According to Maria, about 52 percent of households own group life insurance, which is slightly more than those who own individual life insurance (Table 2.2, p. 14). The percentage of households covered by group life is higher, if you exclude those aged over 65 (as a proxy for retired workers) and those living in single households (as a proxy for "need"), who, together, constituted about 34 percent of all households according to the 1990 Census. Despite its size and relative importance, the group life insurance (and affinity group) market is the "Cinderella" of the industry, too often ignored by those who come from a more traditional background.

Although coverage of employees by group life insurance plans is broad, it is still possible to make the case that employees are underinsured (at about 1.5 times average earnings) and that segments of the market are undeserved. For example, a Conning and Co. study of Group Life[1] (1998) found that only 50 percent of employees had access to supplementary group life through their employers. Those that have access bought, on average, about $60,000, according to the Conning report. Based on an average hourly compensation of $15.09 for 1997 from the National Compensation Survey (Bureau of Labor Statistics), that works out at around twice salary, which, when combined with employer-provided group life insurance of about 1.5 times average earnings, results in fairly adequate replacement ratios (for most employees). The reasons why only 50 percent of employees have access to Supplemental Life coverage is another important topic for further discussion.

With regard to underwriting and issue, group life already meets some of the important criteria that Maria recommends for the industry ("a well-screened policy issued instantly," p. 9): group life is widely available, the products are simple, and the underwriting and issue process is simple and fast. Most employees (and dependents, in those plans that cover dependents) are covered immediately for the guaranteed-issue limit, provided the employee meets the actively-at-work test (or, in the case of dependents, the dependent non-confinement rule). Rates are reasonably competitive with those of individually underwritten products for the same reasons that Maria discusses in her modeling of the cost and benefit of underwriting. Workers who do not have access through an employer-sponsored plan can often find competitive coverage through unions or trade associations.



So why is group insurance the Cinderella coverage? Possibly, because it relies on employers for marketing, and employers have more pressing benefits issues on their minds. Possibly because the companies that sell group insurance do not do a good job of promoting the product, to either the employer (first sale) or the employee (second sale). Possibly because there has been limited product development in Group Life, although there have been some significant innovations in the last few years:

- Group universal life
- Interest continuation accounts (bank accounts for beneficiaries)
- Acceleration of benefits on terminal or critical illness.
- Portability/direct-billing on termination of employment.

I have seen my clients in the group insurance market do a fabulous job of continuous product enhancement, data-mining for target marketing and cross-selling opportunities, experimentation with alternative underwriting and issue approaches, and, as a result, enjoy excellent results. The areas where there has been less innovation are in products that depart from a simple, basic life insurance concept (which is easier to communicate and sell) and in the advisory function that has traditionally been the province of the agent—recommending a plan and an amount of coverage. No doubt this will come with time and enhanced technology.

Nevertheless, a useful and thought-provoking book, which I recommend to all non-traditional actuaries.

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1) Group Life: Different Strokes for Different Folks. Conning & Company. 1998.