Life Insurance Views For 2020

by Bruno Caron

Our society has gone through significant changes mainly due to technological advancements in the past decade. The Internet has helped insurance companies promote their products and has made it easier for customers to make more informed decisions, but has the life insurance industry fully grasped the available modern technology to become as efficient as possible? On the other hand, will fundamental values such as transparency and honesty ever become obsolete? In the next decade, successful firms will, in the author's opinion, have to combine those two forces in order to do well in the long run.

Efficiency And Use Of The Internet

Through information availability and education, the author believes that, as years go by, individuals will become more aware of their life insurance needs. Also, more insurance shopping tools should be available to customers. The old saying, "insurance is sold, not bought" may not be as true as it has been in the past.

The Internet has revolutionized multiple layers of modern society. As information becomes more available and the execution of transactions becomes easier, the author anticipates an increase in the use of Web sites for selling insurance. Web sites providing insurance premium quotes are already abundant, and some Web sites have already started selling insurance online. A challenge for those Web sites is to patiently build a strong reputation, so that individuals will have the confidence to buy insurance through this distribution channel, the same way travelers now buy airline tickets through traveling Web sites, although they may have been less inclined to do so when online travel Web sites were in their infancy. Also, commercial life insurance companies would have an advantage to start selling insurance directly from their Web site. Life insurance shoppers could get the coverage they want and the appropriate riders online, similar to the way customers can customize their purchase when buying computers online. The need for agents selling insurance policies would therefore decrease, just like the use of travel agents has decreased in the past decade. This more efficient way of selling insurance would allow insurers to offer products at a more competitive price, and the necessary technology is already available. The one area where the author does not foresee a decrease in the use of agents is where the face amount purchased is very high and where there are estate planning or complex tax issues associated with the insurance purchase.

Insurance Reward System

The idea of an insurance company reward system, similar to fidelity programs offered by airline companies and major hotel chains (but hopefully more effective), could see the day. Points could be earned by policyholders in proportion to premiums paid and used to buy other insurance products or to get additional coverage or riders. From the insurance company's perspective, such a reward program would increase persistency, awareness and loyalty in policyholders. Such a reward system would benefit both parties and strengthen the relationship between the policyholder and the insurance company.

Regulatory And Taxation Issues

The individual tax treatments of inside build-up will play a critical role in the cash-value-oriented products. Although cash-value-oriented products offer multiple advantages, one of the most sought-after features of such products is the very advantageous tax treatment of the earnings of such products. Some cash value products serve as a second 401(k) vehicle. Regulators' views and future actions are very hard to predict.

Regulators serve and protect individuals by making sure that insurers have enough funds to meet their obligations. It is natural for them to impose strict requirements and use conservative assumptions to evaluate liabilities in

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order to protect the public. Having said that, proscribing unreasonable reserves and capital requirements usually does not serve the population well. It typically results in insurers finding ways such as securitization and offshore reinsurance agreements to get around such requirements. Principle-based reserving is already at the center of multiple Society of Actuaries' task forces, and implementing these requirements will be a challenge for both carriers and regulators, but the author believes that this approach will be beneficial for society in general in the long run, as the focus will appropriately be on the obligations of the insurer to meet its contingent liabilities. Currently, a great deal of effort is put in finding solutions to bypass excessive requirements. Those efforts and resources could be used elsewhere or simply removed to offer a more competitive product.

Shareholders

Shareholders of life insurance companies, just like shareholders of any other corporation, are in a constant quest for more and better information. Transparency to shareholders is definitely a positive aspect for an organization as a whole because it ultimately enables the providers of capital to make better investment and risk choices. This usually translates into more disclosure on a firm's activities. This is typically helpful for investors, but the information disseminated must be done in a manner that makes the information understood and is of value to investors and analysts. The successful insurance companies of the next decade, in the author's opinion, will disclose not necessarily more, but more concise and pertinent information, to the public.

Fraternals

In the light of the recent corporate scandals and lack of transparency, the public, rightfully or not, has a low opinion of corporate leaders in general. This may be an opportunity for the fraternal industry to surge. Usually challenged with the lack of economies of scale compared with regular insurance carriers, fraternals have an unprecedented asset: an impeccable record of transparency and honesty. Fraternals provide a valuable service to society through multiple social programs and charitable sponsorships. If the movement becomes better known to the public, some policyholders may be interested to contribute to this if they pay similar prices, and fraternals have similar ratings as commercial carriers. Also, fraternals get a special tax treatment. Can fraternals use their tax advantage and good reputation to compete with economies of scale of commercial carriers and offer similar prices as well as achieving good ratings? Can they reach out to a broader public? If the answer is yes for the two interrelated questions above, policyholders may turn to fraternals to meet their insurance needs, which would significantly increase the fraternal presence in the life insurance industry in the next decade.

Securitization

Securitization in the life insurance industry took many different shapes and served different purposes in the past. The author believes in the added value of securitization in the life insurance industry in general and sees a demand from both sides. First, the originator (in this case the life insurance company) would benefit from removing some mortality risk from their book, forgo some return in order to write more new business and make a profit on originating policies. Second, the capital markets would welcome a way to diversify equity and interest rate risk, as mortality risk is a random risk that is uncorrelated to those two risks. Past securitization arrangements have involved many parties and have been very costly. In order for securitization deals to be successful in the future, they will have to be simpler, cheaper to implement and more transparent, and target a broader market. Securitization would ultimately transfer some of the mortality risk of the insurer to an outside investor. Simplicity and cost are important because potential investors are attracted to a new risk, but obviously for a reasonable return. If the cost of the issuing security reduces the potential to earn this return, the whole securitization concept is pointless. Also, insurers always have the reinsurance option to transfer risk or hedge it one way or another. In order for securitization to be effective, it has to be done at a comparable cost to reinsuring mortality risk; otherwise, there is no incentive for the insurer to securitize. Transparency is another key element; investors want to be able to evaluate the risk into which they are getting. A black-box-type security is usually not attractive for investors. Finally, volume is another key component of a successful securitization to reduce the cost per security and add liquidity in the market in which it is traded. Successful firms of the upcoming decade will have securitization as an available option. Details and technicalities of such securitization agreements are beyond the scope of this essay.

Conclusion

Transparency and efficiency are the common denominators of this essay. In the end, both firms and customers will benefit from an alignment of these objectives. Also, reputation will always remain a crucial ingredient to the success of a life insurance company. It is not something that can be coded overnight. Transparent contracts (without overly complicated details, upfront fee schedules and no unpleasant surprises) as well as investments in technology are among matters a life insurance company will have to put efforts in to establish and sustain a strong reputation and be successful in the long run. These undertakings can be costly initially, and it is a challenge to remain competitive while assuming these costs. But these factors will ultimately draw the line between the key players of 2020 and the life insurance companies of the "past."

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