Critical illness insurance

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Last year we finished the chapter on critical illness with a quote from a Danish physicist, Neil Bohr who said: "*It is exceedingly difficult to make predictions, particularly about the future!"*. Protection Review is not renowned for quoting famous Danish physicists (or indeed physicists of any nationality) but the quote seemed particularly appropriate given the inability of our market commentators to agree on what the next twelve months might hold for the product. Despite this, when we review the last three years of chapters that we have produced on critical illness, it is possible to say with some certainty that there will be some consistent themes to our conversations. The first of these is, perhaps inevitably, the subject of a conditions race for the product. We asked a range of figures from across the industry whether too much emphasis was put on adding new conditions in CI plans. Had this gone as far as it could go or was it set to continue?

Although opinions differed somewhat on whether there was too much emphasis placed on the conditions race, there was a general consensus that although the race looked set to continue, it would not be without purpose and that conditions would not be added without a provable benefit for the policyholder. Alan Martin from Swiss Re summarises the thoughts of many very succinctly:

> *"This has been an issue, and the product is now very complex for consumers to understand, but the illness race has matured, with companies focusing on improving the depth of cover offered, and selectively adding partial payments - rather than rampantly adding illnesses that add no value as has happened in the past. "*

For Steve Casey of Ageas Protect, such a practice aligned perfectly with Treating Customers Fairly:

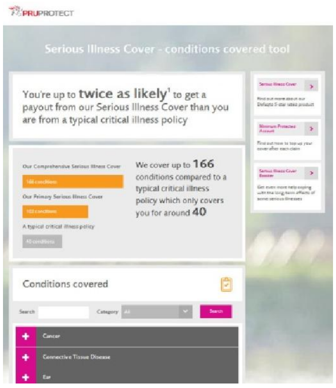
> *"We will not add a condition unless there is a risk cost being charged by our reinsurers. This means that they expect to pay claims. In our developments we have discarded conditions if they have been given 'free'. This is one of our many controls around treating customers fairly."*

This was an issue picked up on by Adele Groyer of Gen Re who felt that the adding of conditions ignored the data on what conditions accounted for the majority of claims:

> *"The Gen Re Dread Disease survey has identified that over 98% of claims arise from just the top ten CI conditions. The survey has also found that there are hundreds of conditions that are covered worldwide, many of which have never triggered a claim. This means that there is scope to add more conditions to UK CI plans but the benefit to the customer is limited and the resulting complexity is problematic both for the customer and the adviser.*
>
> *A summary of the 2004 – 2008 Dread Disease Survey can be found at http://media.genre.com/documents/Topics20_Lu_Droste-en.pdf"*

Consumer understanding is a topic we will return to below. For Phil Jeynes of PruProtect, adding conditions should not necessarily be regarded as a bad thing. Like many of our commentators, the issue for Phil was whether the new conditions would truly add value. His comments below explain how PruProtect make this work:

> *"Adding new conditions is not a bad thing. However, it becomes an issue when attached to that condition are arbitrary requirements and restrictions that make the chance of a claim being made or even paid so low (such as by putting an age restriction on diabetes or insisting on certain treatments before payouts are made on cancers). Advisers have long been sophisticated enough to see past a simple numbers game in terms of recognising a product's value and most compare on the basis of the breadth of cover combined with the likelihood of a payout. PruProtect's Serious Illness Cover for example covers clients for more conditions than any other provider on the market. Beyond these numbers however is our severity based approach. This, coupled with our breadth of cover, means that our clients are up to twice as likely to receive a payout from us than from any other provider.*



Have a look at our online conditions covered tool to find out more. "

Returning to the issue of consumer understanding Alan Lakey, who has created CI Expert, argued that the situation was clear, unlike consumer (and sometimes advisers') understanding of the product and cover provided:

> *"The illogical progress of the current condition race is that both consumers and advisers will eventually treat the concept of CI with contempt as it has trespassed far beyond its original aim of covering dread diseases or critical conditions.*
>
> *I don't believe in 'simple' products but I am all for 'simpler products' and CI is crying out for an insurer to break the mould and offer a sensible yet comprehensive plan."*

The need for the product to be understandable for the customer, or potential customer, was a recurrent theme in the answers that we received. Peter Hamilton of Zurich concurs:

> *"Anything which adds greater certainty to the customer as to whether they can claim is clearly a good thing; it's not obvious that more and more conditions helps here - I hope we see a slowdown…"*

For Blair Sievering of Hannover Re UK Life Branch, the key issue also related to consumers although perhaps less to their understanding and more to their experience of the product as a claimant:

> *"Perhaps the real test in developing additional conditions should be whether we anticipate paying additional claims through their inclusion? The industry now publishes claims statistics*

and claims ratios serve as a valuable indicator for customers and advisers alike and show that the products do work."

The issue of claims statistics is an interesting one linking as it does to the idea of consumer trust in the product which is a vital component for a flourishing market. The final word on this matter goes to Rob Quayle of Direct Life and Pensions who felt that innovation of any kind had to be a positive thing but the focus of this innovation was paramount in ensuring the right outcome:

"We should never stop innovating, or thinking we've done enough. The development of cover to expand its reach and increase the peace of mind for customer's buying should remain a continuing, but not necessarily the main, feature. Ensuring the public quickly and easily grasp the value of the product, trust us to deliver on our promises and are able to apply for and purchase it simply should be our main thrust."

Another recurrent theme in our critical illness chapter each year is the work of the ABI and its *Statement of Best Practice*. We asked our commentators if they felt that the work could continue ad infinitum or whether we would inevitably reach the point of needing to consider a new product concept? A number of our commentators were keen to applaud the work of the ABI thus far with Phil Jeynes suggesting that the work of the ABI had been 'crucial' in the development of the CI market:

"The ABI has done some really good work on the Statement of Best Practice, which should be applauded." (Peter Hamilton, Zurich)

Rob Quayle from Direct Life also saw merit in the work of the ABI but highlighted the need for a balance between standards and innovation:

"The Statement of Best Practice is a great way of improving uniformity of cover, which makes it easier for Advisers to explain the products and help customers to understand and trust the cover. There's always a balance between such 'standards' and innovation. Too much innovation over complicates, but we can't rest on our laurels or sell a common product. Where such key areas are proven not to provide sufficient value and give rise to mis-understanding it is right for the industry to step in and this is what the standards are all about. I don't think we necessarily need a brand new product concept as the ultimate product is a well-defined income replacement plan – protecting and maintaining a client's standard of living."

For Swiss Re's Alan Martin, the ABI work on the Statement of Best Practice had helped… to a point:

"It helps the contested markets to have standard definitions, but it also helps reinforce the commoditisation - which partly feeds the illness race."

Others were less certain that the ABI input could be considered worthwhile with perhaps the strongest opinion being expressed by Steve Casey:

"We do need to look at a new way of doing things. Just issuing a SoBP every three years because the ABI said they would is out of date. The latest one is very light on development/detail and does little to either progress the market or keep providers honest."

Zurich's Peter Hamilton agreed that perhaps the ABI work hadn't kept pace with other developments, citing the advancements in diagnoses and certain treatments as examples:

“There is a risk that with most providers now offering a significantly wider number and range of definitions, its relevance in providing guidance to customers and advisers that a product is of an appropriate standard is becoming devalued.

A further concern is the one of ongoing improvements in diagnosis and treatments which can result in much earlier diagnosis of certain conditions, or conditions which were once critical now being relatively minor. The classic example of this was angioplasty, which needed to be removed from CI plans a few years ago as the treatment was now so common that it was no longer serious. The SoBP attempts to keep track of these medical developments, but there does remain a risk that claims can be made for conditions which are relatively less serious, or for early diagnoses, and these could push up the price of critical illness in the future.”

For Adele Groyer at Gen Re, the Statement of Best Practice, whilst not necessarily keeping up with developments, served a useful purpose for the industry, even if this wasn’t the original intention:

“The SoBP now represents a position that a CI product cannot dip below rather than a market standard. This goes against the original intention of the SoBP, in light of an OFT finding, which was to make products simpler to understand because they were market standard.

The ABI can continue to maintain this baseline. The ABI is unlikely to drive a new product concept.”

Alan Lakey felt that the original intent of the ABI work had been lost along the way with unintended outcomes which had emerged from the research:

“The original idea was predicated on reducing confusion so that advisers and consumers could better understand and thereby interact with more confidence. With less than 50% of conditions enjoying a model wording the original intended outcome is being lost and an element of relevance with it.

I believe there is still a place for a consensus based approach to CI but if the outcome was standardisation then we will have successfully commoditised the product and argued our way out of the need for advice”.

A review of the responses that we received showed that few of our contributors felt that the work of the ABI would lead to a new product concept. Phil Jeynes argued that PruProtect’s severity based approach represented an evolution in critical illness which the ABI needed to take note of:

“The next step is for it to take into account the moves the sector is making towards severity based cover. This product concept is already taking hold and is a natural evolution from traditional CI. We’ve already extended the principle of severity based payments by introducing Serious Illness Cover Booster. This boosts payments to help clients cope with illnesses that have a long-term physical impact. Get more on Serious Illness Cover Booster here.”

Blair Sievering also argued that the new product concept had arrived already with the existence of severity based and hybrid products:

"The existing product concept continues to evolve in a number of ways and covers medical interventions as well as 'critical illnesses'. Severity based products and hybrid products involving replacement income or payment for procedures add logical elements of coverage, as do benefits which change through the lifetime of the policy to reflect the exposure and risks faced by our customers."

Whilst our question inevitably focused the minds of our commentators on what might happen with the product moving forward, Peter Hamilton was keen to ensure that we remember the difference the existing product can, and does, make to people's lives every day, something the video he shares demonstrates very concisely:

"…we shouldn't overlook the massive difference we collectively make to thousands of lives every year through the claim we pay"

Our previous question inevitably led to our industry commentators thinking about new product concepts and the direction that the product should take. We asked whether they felt that it should move towards tiered benefits or a scaled down simpler product? The question divided opinion more than any other that we asked this year. Firstly there were those who felt strongly that a simpler product was the way forward. Rob Quayle explains his thinking:

"Personally I like the concept of scaled down simpler benefits as an alternative. In other markets, gold, silver and bronze versions are common and easily understood. So if communicated and compared correctly, the public should understand they can leave out options in exchange for a reduction in premium. Limited tiered benefits could fit into this model, but I think they add a more complex, and therefore less favourable, route."

Alan Martin of Swiss Re was also in favour of simplification:

"There is some scope for severity based products, but more in the health space. Where tiered benefits are used, simpler versions make more sense to the consumer than those in the market currently"

Alan Lakey explained that although he favoured a simpler product, he didn't feel that this would be at the expense of comprehensive cover. He explains his thinking below, with the consumer clearly at the heart of his reasoning:

"I consider the most sensible method to be a reduction in the numbers of conditions offered but simultaneously and perversely, one providing a wider range of coverage. If we look at neurological conditions such as Motor Neurone Disease, Parkinson's and Multiple System Atrophy they frequently share a claims requirement of loss of motor function and/or some other linked impact. By consolidating three or more conditions into one overriding wording we not only reduce the complexity of having 50+ conditions but also drag into the plan those rarer conditions such as Devic's Disease that produce a similar impact but are not usually named as specific conditions.

It would be much more consumer-friendly to state that any condition fulfilling the claims criteria is covered. This also avoids the frequent response that insurers try to weasel out of paying genuine claims.

Tiered benefits add an additional layer of complication which works against the product in terms of both marketing and consumer understanding."

It was perhaps not a surprise to hear that Phil Jeynes of PruProtect argued in favour of tiered products. In contrast to Alan Lakey's thoughts above, he argued that simpler didn't always mean better:

> *"I've nothing against simple products but I am yet to be convinced as to what shape this could take in the context of CI. For example, our Serious Illness Cover protects customers against myriad forms of cancer which, on the face of it, can look complex but it means that our clients are better protected - so really, simpler isn't always better. Should we work to simplify our product by stripping away cover for some cancers and leave clients less well protected? I don't think so. Diseases like cancer aren't uniform and they aren't simple and our products shouldn't shy away from protection against them holistically.*
>
> *This approach need not be a barrier to sale, after all plenty of people buy new cars without fully understanding how each component works. They trust that the design of the vehicle is such that, when they press the brake pedal, it will stop."*

For a number of our commentators, choosing between and simpler and a tiered version of the product was a choice that didn't need to be made. Peter Hamilton's comments are representative:

> *"There is space for different types of critical illness product within the market, and different providers and distributors will determine which they want to offer and which they want to distribute to their customers. In some circumstances a simpler product will be more suitable, particularly where it is bought direct. This may provide a lower price for customers, and potentially be easier to understand. Where advice is available, a plan with a more comprehensive range of coverage will also make sense.*
>
> *We are likely to see increasing differentiation within the critical illness market over the next few years. We will see some providers look to retain a simple offering, while others look to differentiate through offering more tiered benefits and potentially extend further with links in to PMI type benefits and other income protection type solutions."*

Blair Sievering felt, as Peter did, that there was room for both and that distribution was the dictating factor in product design:

> *"We work with providers at both ends of the product spectrum but don't believe the two are mutually exclusive. Historic product differentiation emerged from perceived distribution needs or challenges, which includes the varying scope of the conditions covered (e.g. fewer in the direct model) and the acceptability of a more, or less rigorous underwriting process.*
>
> *It's important the industry continues to offer products that allow consumers to interact and buy as they choose to. Multi-benefit, tiered and severity based products may well benefit from advice and affordability may mean that these products will remain a good fit for the advised market but so too will simple products depending on the individual customer's circumstances."*

This was also the viewpoint taken by Ageas Protect's Steve Casey:

> *"Markets & distribution will dictate the direction the product will move. Simpler products for direct to consumer, tiered for advised distribution. Simpler does not necessarily mean*

inferior, it just means simpler. I can see more products specific to certain distributors as Providers attempt to differentiate themselves"

And also Adele Groyer of Gen Re:

"In the advised channels tiered products are possible however it is unlikely that the generous payment levels at the early stages of diseases that qualify for full coverage will be scaled back. Growth in the number of partial sum assured benefits is more likely.

Simpler products will develop in new distribution channels."

Having gathered opinions on the future direction of the product and the extent to which is might simplify, we next turned to consider the circumstances and reasons it was sold. In the majority of cases, critical illness is sold as an add on to a life policy. But how useful is standalone critical illness? We asked our industry spokespeople and on this issue they were more united in their responses. Almost everybody that we asked pointed to the question of price and the value of a standalone policy when compared to a policy including life cover:

"It has a relevance but it's difficult to sell when the true actuarial price means it costs more than accelerated CIC. Does stand-alone CIC make the returns it should if you price at 98/99% of the accelerated price?" (Steve Casey, Ageas Protect)

Phil Jeynes suggested that compliance necessitated the need to be able to offer a standalone product but that for the majority of customers, it was unlikely to be cost-effective:

"Stand alone cover accounts for a very small percentage of overall sales and it's hard to see a circumstance where the same policy with Life Cover added at little or no cost, wouldn't be a superior alternative.

I am aware that some compliance departments insist that the standalone cover is offered, where no demonstrable need for Life Cover exists (e.g. a single person with no dependants) and perhaps it is these situations which mean the option hasn't altogether disappeared." (Phil Jeynes, PruProtect)

Peter Hamilton of Zurich agreed that it was hard for consumers to see the financial sense in a stand-alone product:

"The logic behind standalone critical illness cover is that if a customer already has life cover in place then they don't need the life part again and so standalone CI is enough. This should then be cheaper. However this is often not the case and accelerated CI can often be obtained just as cheaply as standalone CI (essentially because claims experience on standalone cover has historically been markedly worse)

In this situation, there seems little point in selling standalone CI, as the customer might as well benefit from the free extra life cover."

For Rob Quayle, the existence of a standalone product could be used to demonstrate the value of a combined product:

"Pricewise it's still not as good value as combined covers, so we don't see much transacted. However without the ability to compare it and illustrate the good value that life and critical

illness represents it's difficult for an adviser to demonstrate this – so we include it on our portal, really for this reason alone." (Rob Quayle, Direct Life and Pensions)

While Gen Re's Adele Groyer agreed with the value argument she also underlined the need to see things from the consumers point of view where there may be little difference between death and serious illness when considering the need to protect your family's interests:

"It has a place but volumes are small. This is understandable. When selling to the concept of "if something happens to you protect your house for your dependants', death and illness are equal considerations. The price difference between standalone and accelerated CI is not sufficient to justify taking standalone cover only. Someone who already has life cover will have to have aged a few years to make it attractive to keep the original life cover with a separate standalone CI policy."

For Alan Lakey however, there was a compelling argument for not promoting standalone cover.

"Given the cost differential and the fact that many plans include life cover automatically one has to ask 'what's the point of it'? No CI plan should be marketed without inclusive life cover because most plans retain a qualifying period of 14 days and survival cannot be guaranteed. Consider the bad news potential of somebody dying thirteen days after a heart attack and his family being told that he died a day too soon.

There cannot be many arguments in favour of stand-alone and I am certain that none of them will stand up to a proper scrutiny."

Blair Sievering from Hannover Re UK Life Branch acknowledged the price argument but felt that it was impossible to ignore the fact that there were situations when a stand-alone product may be most appropriate, although he added that in such situations income protection might also be considered, providing a role for hybrid products:

"Although sales of standalone CI have fallen steadily over the years and remain a fraction of the accelerated product sales, there are situations where the product is the right fit for the customer. Many people will have existing life cover (e.g. employer sponsored or mortgage linked) and wish to complete their protection portfolio with the addition of some CI. There is also significant social change afoot which has seen significant rises in single households where life cover may not be a key protection need.

Many critics point to the issue of cost given there is often little difference in price between standalone CI and life and accelerated CI. This lack of significant cost differential is undoubtedly linked in part to historic industry experience to the perceived higher risk of anti-selection.

In reviewing an individual's hierarchy of needs it may be established that IP provides a better fit than standalone CI. A more comprehensive solution may be a hybrid product which has the scope of providing income and lump sum benefits."

Only Alan Martin argued solely in favour of standalone cover saying: *"It has an important role to play".*

Given the historical link that CI has to the fortunes of the life, and therefore the mortgage markets, the last of our questions asked whether our commentators felt that the market will pick up with the increase in production in the mortgage market? Once again, we saw a high level agreement among the responses that we received. The consensus was that logically the market *should* pick up but most of those we spoke to felt that there were a number of reasons why logic wouldn't necessarily prevail this time:

Blair Sievering cited evidence from the ABI showing the weakening of the link between the mortgage market and sales of protection products, a common theme in the answers to this question:

> *"The ABI's figures show that the correlation between the mortgage market and sales of protection products has become diluted over the past 10 or so years, yet it remains an important life event trigger to effecting cover. Sales of mortgage linked term products (which will include some accelerated CI products) picked up steadily throughout 2013 with accelerated growth in Q3 and Q4. Likewise standalone CI sales picked up throughout the year.*
>
> *With the financial crisis triggered by the interbank lending crash of late 2007 and compounding impact of the RDR and MMR many mortgage advisers migrated to focusing on protection sales as a means of generating income. It remains to be seen whether this will be maintained as the mortgage market picks up. Balancing the advice process to ensure protection is adequately covered has long been a challenge."*

Peter Hamilton also felt that there was little evidence that a rejuvenation of the mortgage market would filter through to the sales of critical illness:

> *"Intuitively it ought to. Mortgage lending is expected to be some 20% higher this year. That said, so far there is limited evidence to suggest the term and critical illness markets are benefitting materially from growth in the mortgage market. Ultimately this could be down to the capacity of the mortgage advisers to be able to sell protection - if there are more mortgages to keep advisers busy then protection could drop down their list of priorities."*

Peter's final point was echoed by several of our commentators who felt that the actually the recovery of the mortgage market could have the opposite effect with adviser's attention and priorities diverted elsewhere:

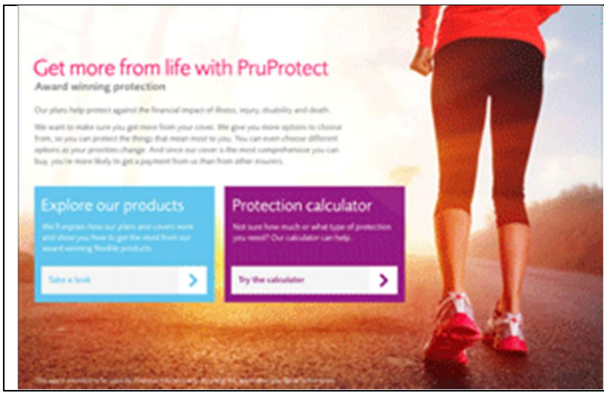
> *"It doesn't follow naturally that the CI market will pick up. In some respects there is an obvious link between mortgages and protection business in general and as one grows, so should the other. Equally we have seen how advisers have swapped debt-related sales with more personal protection during the lull in the mortgage market."(Adele Groyer, Gen Re).*
>
> *"There is potential, although often mortgage brokers work harder to sell protection when the mortgage market is falling. If mortgages are picking up they have less need for protection revenue...so difficult to judge." (Alan Martin, Swiss Re).*

Alan Lakey was in agreement suggesting that advisers needed to recognise the value of, and need for protection:

> *"Logically this should happen but it is reliant on two things – firstly, mortgage advisers selling both the concept and the plan and, secondly, consumers recognising that they have a need. There is much comment to the effect that mortgage brokers are too busy arranging mortgages to look at ancillary matters. The challenge is to make them consider protection as part of the product and process and not as some tagged on afterthought."*

While this was an argument acknowledged by Phil Jeynes of PruProtect, he suggested that providers could play a role in helping to educate advisers and provided some details of how PruProtect are attempting to do just that:

> *"Sadly, history tells us that exactly the opposite will happen; as mortgage brokers get busier, they neglect the Protection sale which, in leaner times, sat alongside their mortgage business.*
>
> *I am an optimist, however, and I believe that with the help of providers more brokers are now well placed to provide a rounded sale and both better protect their client and become better remunerated in turn."*



We recently launched the PruProtect MyPlan app which can be used by advisers with their clients to help them build a comprehensive plan providing cover for more that just the mortgage.

Download the MyPlan app for your iPad here.

Rob Quayle took a similar view, believing that providing advisers with useful tools could help to maintain their focus on the protection market. His recent experience was positive as he describes below:

> *"During the downturn the mortgage advisers LifeQuote works with have really appreciated the value of protection sales and are more skilled and successful at advising their clients. For the mortgage advisers, despite being busy with mortgage enquiries we've seen them maintain this focus. No doubt some advisers will be too busy to maintain this and will focus on the mortgage. However with time saving quote and application tools, outsource services such as LifeQuote, better compliance regimes, and the availability of self service options I would expect many advisers to improve penetration rates of protection sales in relation to mortgage completions.*
>
> *The other winner could be the online non-advised services – offering discounted services to the self directed individuals."*

For one of our respondents however, the issue was not whether the critical illness market could expect a revival in response to an upturn in mortgage sales, but whether this was the right approach for the product in the first place. Steve Casey explains:

> *"In theory yes – more mortgage business should stimulate protection sales but unfortunately it's not enough - we need to generate true 'new' protection sales by reaching the mass market in a different way with products and processes that are geared to simplicity and friendly online journeys. There is already evidence that mortgage intermediaries have forgotten about protection as they sell mortgage after mortgage."*

This is a compelling argument and one worth giving further consideration as our review of the market this year comes to an end. A couple of years ago we used the term ‘identity crisis’ in relation to critical illness. What is clearer than ever is that the product and those who are involved in selling it is that there needs to be a clear raison d’etre for critical illness, its relationship with other products and how this is communicated to potential customers.

It is very clear that the subject of critical illness divides many industry experts. We have delved into several of the arguments in this chapter. Is CI too complex or does it need to continually evolve as medical science progresses? Would a simpler product fulfil a need or would it just dumb down the cover? Is the regular review by ABI of the SOBP a good thing or have we reached a stage where we need to sit down and rethink the raison d’etre of the cover. Perhaps a big question that is rarely addressed is whether we need to explore the way in which CI and income protection interact. These are big questions and ones we need to answer when we examine the present ….and the future of critical illness. It would appear that our quote from Neil Bohr about the future being hard to predict is still as fitting now as it was a year ago!