ExamOne®
A Quest Diagnostics Company

The Simplified Issue Conundrum

Conundrum: noun; anything that puzzles.

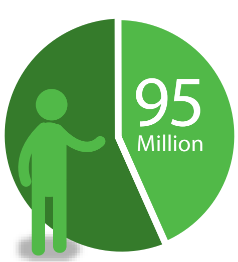
For years insurers have been looking to simplify the life insurance purchase experience. From ease of sale to "hassle free" underwriting, the goal is to make the sale a simple financial transaction. Many compare simplified issue (SI) life insurance sales to the purchase of mutual funds or 100 shares of Apple stock. The producer "drops a ticket" and the stock certificate is delivered within days rather than weeks. But how simple should the life insurance purchase process be? It can be a large, complicated financial and health-related process with significant financial implications for the consumer as well as the insurer.

One goal of SI insurance is to enable companies to further penetrate the middle market.

Numerous surveys have shown a significant percentage of middle market consumers, sometimes defined by annual household income of $35,000-$75,000, are uninsured or under insured. They may not be as financially savvy as more affluent customers and may be intimidated by the entire life insurance purchase process.

Problematic as well is selling to the "millennials", (individuals born between the early 1980's through the early 2000's). Millennials don't conform to the purchasing habits of their parents. They want to purchase on their own terms. They may not value an agent. They are computer savvy and may choose to purchase financial products online at midnight. They want to control the process.

Number of Uninsured:



According to LIMRA, there are 95 million American adults without life insurance.

For insurers, an additional goal may be to enhance utilization of underwriting engines by further automating the underwriting process. Simplified issue may offer opportunities to reduce acquisition expenses by spending less on traditional underwriting requirements and potentially reducing staff.

The industry is seeing renewed interest in SI products, but this time with a few twists.

Unlike traditional simplified issue products that reduce face amounts for the same premium as a fully underwritten policy or adjust mortality assumptions, agent compensation, product profitability, or a combination of these and other factors, the new generation of SI products may claim to have the same mortality assumptions as fully underwritten products while paying "full" agent compensation and yielding similar ROEs as full underwriting.

These products may cause some to ask, "How is this possible? Can you eliminate traditional underwriting requirements with no impact on mortality, compensation, and profitability?"

Every company must decide what level of underwriting works for them. They need to evaluate which underwriting levers can be pushed and pulled and the consequences associated with every change.

The rest of this paper provides a blueprint for items that companies must consider when developing, marketing, and underwriting this next generation of SI products. Data is the key. Companies must measure the impacts of changes from start to finish and share this data across the underwriting, actuarial, financial, and marketing operations of the company. Without data, companies may be flying blind and unintended, adverse financial consequences will be looming years down the road.

KEY POINT: Companies must break down the entire sales process, from reviewing the application questions through the underwriting final decision.

Included in this review is the actual sales process including the preferred distribution channel and the application. We'll examine each aspect of the insurance transaction and the essential items that must be measured.

The Simplified Issue Sales Process

There are pluses and minuses to each of these scenarios.

- Will agents/brokers sell the policy?
- Will policies be sold face to face?
- Over the Internet?
- Over the phone?
- If a company sells coverage from a call center will they utilize their own employees or outsource the work?

Face-to-face sales provide some comfort that the proposed insured is who they claim to be and is in relatively good health. But we also need to keep in mind that the producer in face-to-face sales has a strong financial interest in getting the policy issued and there are small minorities of agents who may be inclined to coach the applicant. "Mr. Jones, you have never used tobacco, right?"

Internet sales sometimes reduce or eliminate agent compensation, but companies must feel comfortable the customer understands application questions and will be able to provide the level of detail required in response to "yes" answers. Multiple signatures for the application, authorizations, disclosures, and consents can often stymie the internet sales process.

When sales are completed by agents, will telephone sales be allowed? Agent-completed telephone sales may create mortality issues that need to be considered in product pricing.

Sales conducted from call centers may reduce anti-selection. If companies haven't already done so, they should measure the quality of application declarations provided by agents compared to call center personnel.

This includes not only the quantity of information, but also the quality of information. This data can then be used to estimate the mortality impacts associated with each sales method. Companies should be aware that there are mortality differences based on who completes the application and by what means it was completed.

The Application

Simplified Issue sales almost always incorporate a short form application. However, the question remains, "How short can you go?" Companies must measure the potential mortality impacts of short form applications.

Assuming that regulators would ever approve a single question application (they won't!) you might just ask, "In the past 10 years, detail all visits to a physician or medical professional including date of visit, reason for visit, findings, medications prescribed, and full name and address for each medical provider."

We have learned over decades of underwriting that a certain number of application questions are required to elicit information sufficient to properly underwrite and price the risk.

Each question is intended to provide underwriting value. Some companies tout a limited number of application questions, but bundle multiple medical conditions into each question. Other companies ask a larger number of questions, but shorter questions. There is no right or wrong answer. The key is to get the necessary information.

With SI products the number and scope of application questions is reduced. But what questions can be eliminated without impacting mortality?

Remember, we're considering the new generation of SI products that assume the same mortality as fully underwritten products.

Do you eliminate the questions about epilepsy and nervous system disorders? Do you reduce the scope of the questions related to heart or coronary artery disease? If there were no underwriting or mortality impacts associated with those questions, why were they included on the full underwriting application in the first place? If there are mortality implications, companies need to measure the impact of each eliminated question and factor that into the final financial analysis. Do you have questions about the potential mortality impact of eliminated questions? Reinsurers may be able to help.

Underwriting Requirements

Critical to the success of any Simplified Issue product is the underwriting requirements. To achieve expected mortality and profitability goals the requirements must be thoroughly studied. This includes conducting appropriate cost/benefit analyses to fully understand the impact of reducing or adding underwriting requirements.

MIB/Insurance Activity Index

There is no questioning the value of the MIB/IAI in simplified issue underwriting. The MIB helps reduce anti-selection. The same is true for the IAI as it helps identify rewrites of non-issued policies by the issuing company as well as "stacking" of simplified issue or guaranteed issue policies.

Eliminating either will have devastating financial consequences.

Medical Exam

Companies need to understand the protective value of the medical exam questions. While frequently duplicative of application questions, there may be additional questions not covered by the application. Additionally, insurers have long recognized the value of a disinterested third party asking the questions and fully recording the applicant's responses. Similar to the application question asked earlier, if the exam questions are assumed to add no underwriting value, why were they required in the first place? In fact, medical history questions may be even more important now as consumers know more about their health than ever before.

Conversely, well-crafted application and drill down questions completed by a tele-app provider or call center can mitigate the loss of examination Part 1 protective value.

Vital Measurements

Do most applicants accurately report their weight on the non-medical Part 1? For those who don't provide a reasonably accurate weight, do they most often overstate or understate their true height and weight? With the exam and vital measurements "off the table" for SI underwriting will the level of understatement of weight be exacerbated?

Blood Pressure

There will be some level of anti-selection related to blood pressure, but a portion of this may be mitigated with prescription drug checks (see below). Of greater concern are those applicants with elevated blood pressure who are first made aware of their condition by the insurance exam. Mortality from those with previously undiagnosed elevated blood pressure will increase. Companies need to account for this in their overall mortality calculations.

KEY POINT: Perhaps the most interesting feature of the new generation of SI products is total elimination of blood and urine (except for cases with significant MIB information). For companies assuming SI mortality will match full underwriting mortality, this will be the one area that needs to be thoroughly measured through cost/benefit analyses.

Tobacco Use

The biggest issue with elimination of fluids is tobacco misrepresentations. One client reported the percentage of admitted tobacco users on their SI product was significantly smaller than the percentage of confirmed tobacco users in their fully underwritten book of business.

How prevalent/significant is "smoker's amnesia" with SI underwriting? The only way to establish a baseline is by measuring tobacco misrepresentation on fully underwritten products. Companies must do a robust review of recently processed applications, including issued, declined and incomplete files. Select a statistically significant sample of applications and focus on the tobacco use question on the non-medical Part 1. Ignore any exam, inspection, or APS tobacco disclosures as none of these will be required with SI underwriting.

Focus the cost/benefit analysis on applications where the applicant denies tobacco use. Then review the cotinine result on the urine specimen. Companies that have done this work report mid-single digit to low-double digit percentages of tobacco misrepresentations.

The next step is to calculate the mortality impact of tobacco misrepresentation. Assume that during the initial application review the company finds 95 percent of applicants declare themselves non-tobacco users. Assume further the urine specimen review shows five percent of these applicants were actually tobacco users. Overall, the tobacco misrepresentation for the company's full underwriting book of business is 3.8 percent (.95*.05.) Most companies assume tobacco use mortality is twice (Table 4) "standard" mortality. Then ask the actuaries to calculate the overall mortality/profitability impact if 3.8 percent of business is underpriced by four tables. This result must be incorporated into the SI product design and pricing.

It is relatively simple to calculate tobacco use anti-selection on fully underwritten products. Companies can be absolutely sure to experience even greater levels of tobacco use anti-selection on Simplified Issue products.

Short of an MIB "hit" for recent tobacco use there is virtually no way to identify "misrepresenters" on SI products. Producers know this, and so do customers.

Glucose/A1c

We're in a "diabesity" crisis in the United States. The overall and insured population has a much greater average BMI than just 20 years ago and the incidence of glucose intolerance and diabetes has skyrocketed during the same time period. Diabetes.org, the official web site of the American Diabetes Association, reports that in 2012 there were 29.1 million Americans with diabetes. 8.1 million (27.8%) were undiagnosed. Additionally, there are 86 million Americans age 20 and older with "pre-diabetes," up from 79 million just two years earlier.

Traditional insurer blood glucose testing is rapidly being replaced industry-wide with routine A1c screening. Routine A1c screening allows insurers to keep pace with the explosion in diabetes and pre-diabetes, but this protective value is lost with SI underwriting. A number of companies have found nearly 20 percent of applicants have elevated A1c levels (5.7 percent and higher) and 3 to 5 percent of these are truly protective test results. (No known indication of glucose intolerance and diabetes from any other underwriting source, including the application.)

Again, insurers are wise to calculate the lost protective value from eliminating routine glucose and A1c screening.

HIV

The HIV epidemic identified in the early 1980s led to almost universal blood testing. Few if any applicants who were HIV positive admitted their status on the insurance application. Additionally, the vast majority of HIV infected individuals were unaware of their status adding further value to the insurance blood test.

Companies need to review their last several years of blood test results (ask your lab) and determine the number and percent of HIV positive applicants. Until proven otherwise, 100 percent of these individuals are generally uninsurable and at least some will now slip through to the SI insured population. Also, one ExamOne client company that tracked Simplified Issue HIV experience reported significant levels of HIV anti-selection.

Liver Function Tests (LFT)

Elimination of blood also means loss of the LFTs. This is particularly important for HCV positive applicants with abnormal liver enzymes. Approximately 60 to 65 percent of HCV infected applicants have abnormal LFTs. Client companies have reported that similar to HIV positive applicants, few HCV positive applicants admit their status and the vast majority are unaware of their HCV status. And with overall HCV rates of infection nearly three times the HIV positive rate the mortality impacts are significant. How significant?

Asymptomatic, untreated HCV infection conveys a moderate mortality risk. At best, these applicants require a mild to moderate substandard under best-case scenarios. Only a small percentage of these applicants will spontaneously clear the virus. With an approximate . 15 percent insured population infection rate and average mortality approximately two times "standard", the mortality implications are significant. Once again, a review of fully underwritten applications will yield a rough estimate of LFT protective value for HCV positive individuals.

The same is true for alcohol abusers. Loss of blood testing will allow a number of these applicants to slip into the SI pool.

Other Blood/Urine Results

The concerns expressed above also hold true for other blood/urine test results but the mortality impacts are generally somewhat smaller. In any event, companies need to take these into account when pricing the new product.

Attending Physician Statements (APS) and Electronic Medical Records

APSs are also virtually eliminated on the new generation SI products except where the MIB or a prescription drug check discloses significant, unadmitted information. Similar to the concerns expressed above, companies need to measure and understand the impact of fewer APSs.

Does the company order a significant number of "age/amount" APSs? Virtually 100 percent of their protective value may be lost on SI products. For APSs ordered "for cause," are companies comfortable these APSs only infrequently reveal significant, non disclosed, medical impairments? Accessing electronic medical records and use of services that extract prescription histories, lab and pathology reports can help offset the elimination of the traditional APS.

Anti-Selection

It is impossible to accurately calculate the adverse mortality impacts of anti-selection. But, we know we have a very efficient life insurance marketplace. Producers spreadsheet companies and products and will most certainly gravitate to SI products if they perceive a "bargain" for their client while generating full compensation.

Prescription (Rx) Drug Checks

Rx checks provide an excellent opportunity to recapture at least a portion of the "lost" mortality detailed above. But how much?

Companies utilizing prescription drug checks on a screening or reflex basis should already have a rough estimate of their protective value. If not, adding routine Rx checks for the SI product without a cost/benefit analysis is just a shot in the dark.

Go back to the tobacco misrepresentation example from above. Remember the 3.8 percent of business underpriced by four tables? How much of that mortality can the company reasonably expect to recapture with Rx checks? Ask/answer the same question for the mortality "lost" through the short form application, loss of exam, and loss of vital measurements, APSs, and various blood/urine tests.

On the flip side, routine Rx checks may produce some mortality savings not captured by traditional underwriting requirements. Companies may learn of significant medical conditions that routine exams, APSs, and blood/urine tests won't uncover. Will these be sufficient to further close the mortality gap? The pricing actuaries and finance folks will need this data.

Companies may also consider ordering Rx checks by both the industry providers to help close gaps in available PBM data. Not all similar data is available to each of the major Rx data providers. If companies are relying on Rx screening to offset mortality from eliminated requirements, they need to understand the quantity and quality of the Rx data they will be using. New data sources are becoming available to the industry that extract prescription, lab and pathology reports from medical records.

Expenses

Reduced expenses. Significantly reduced expenses. We have discussed potential reductions in sales commissions if products are sold over the internet or through call centers. The new generation of SI products eliminates virtually all medical exams, blood/urine, and APSs. Can we assume lower lost business rates due to faster policy issue? Greater placement ratios reduce per policy costs. Greater placement rates translate to increased profitability.

Increased Sales

Is one of the goals of SI underwriting to increase sales and "placed" business? If so, a post implementation study to validate achievement of this goal is essential. Too often, the promised "plus" sales fail to materialize. Why mention "plus" sales? There is always a risk SI sales will cannibalize fully underwritten business. Companies may achieve their SI sales goals only to find sales of fully underwritten business tail off. Sales goals need to be defined and measured.

Reinsurance

Don't have the time/resources/inclination to complete cost/benefit analyses to measure the financial impacts of each step of the SI process? Companies might want to tap into reinsurance expertise. Reinsurers must obviously be involved in each step of the SI process if they reinsure any portion of the risk. This is especially true if the direct writer prices the product for "standard" mortality. However, even if a company retains 100 percent of the SI risk they would be wise to engage their reinsurer(s) in discussions regarding their underlying assumptions. It is best to identify potential mortality/profitability issues prior to product launch rather than have to react to adverse experience years down the road.

Actuaries, Claims and Sales

KEY POINT: Introduction of a Simplified Issue product, especially if "standard" or better mortality is assumed, requires total transparency with the actuarial, finance, claim, and distribution channels.

Actuaries have historic data measuring actual-to-expected mortality experience on fully underwritten products. They need to understand and embrace the tradeoffs involved in SI underwriting. This means sharing objective data related to what requirements are being eliminated and added and the underwriting department's mortality assumptions related to each change. If fully underwritten mortality is tracking much better than pricing assumptions, an aggressive SI underwriting policy may make sense. If actual-to-expected is "on target" the actuaries must agree the recommended SI protocol will not skew current experience.

Once actuarial approval is secured, the finance department must join the conversation to fully understand how underwriting acquisition expenses and financial targets will be impacted.

The claim department will need to understand the underwriting changes and assumptions in order to conduct appropriate contestable claim investigations and not panic when claims must be paid because the application and underwriting requirements may not disclose significant information that has traditionally been readily available on fully underwritten business.

The sales team will be showering their underwriting brethren with copious praise for simplifying the process and eliminating all those burdensome and unnecessary requirements, but they also need to understand their responsibility to provide a full and complete SI application and to fulfill any sales commitments required to achieve the desired corporate results.

Conclusion

KEY POINT: The Simplified Issue conundrum. It may not be quite a conundrum if companies break down the entire process from start to finish, conduct appropriate cost benefit analyses, and complete post implementation validation studies.

Assuming "standard" mortality on SI business can be a game changer provided companies can adequately answer the questions posed above.