CHUBB®

Understanding special terms

Insurance

Acceptance for life

The good news is that once an application for insurance has been accepted and the policy issued, the acceptance terms for those benefits cannot be changed by the insurer even if, subsequently, a customer's health deteriorates, they change occupations or take up a new dangerous pastime.

As discussed above, a customer may request their acceptance terms be reviewed during the life of the policy and they can do so in the knowledge that the company cannot change their acceptance terms for the worse if their risk profile has changed. They can only leave the terms the same or improve them if the risk profile has indeed decreased.

Clearly any application for additional or increased benefits will be underwritten based on the customer's risk profile at the time of the increase application. Even if the company believes the risk profile has worsened since the original application, they can still only apply the new special terms to the new or increased benefits, since the acceptance terms for the existing benefits cannot be changed.

As there are many conditions or disorders that increase in significance with increasing age, it is important to put cover in place before the health risk deteriorates to the point where cover can no longer be offered. So, while being offered special terms can seem unfair, the reality is this may be the last opportunity the customer has to get cover at all.

It is also important to note that, if the customer did not make full and accurate disclosures about their risk at application time, and this failure is subsequently discovered, the insurance company has the right to reassess the original acceptance terms based on the correct information.

Premium loading examples

Loading category	Percentage loading	Per mille loading
Minor	+50 - +75%	+$2.50 - +$5.00
Moderate	+100% - +150%	+$7.50 - +$10.00
Substantial	>+175%	>+$12.50

As a person ages, conditions that were once minor can become much more disabling as surrounding muscular skeletal structures start to degenerate. So minor niggles at age 35 can deteriorate to a chronic, disabling back condition by the age of 50. At age 50, most disability policies still have 15 years to run and a 15-year claim is clearly significant to a life company.

Likewise, the latest medical research very clearly links obesity to an increased risk of cardiovascular disorders in later life. In addition, the rise in Type 2 diabetes is also being closely linked to obesity. So from an underwriting point of view, someone who is overweight does pose a statistically higher risk than the average population even if they have never had any significant illnesses or injuries.

While underwriters will take into account additional information regarding build, such as muscle bulk due to high-level sports, the reality is that even a top level athlete, who is significantly over the recommended build guidelines, may present a statistically higher risk. The additional body mass they carry is at risk of becoming excess fat as the customer ages and decreases their level of physical activity.

With this comes an increased risk of diabetes or heart disease – both significant causes of premature death and long-term disability in New Zealand.

Sometimes an underwriter will be presented with a customer who has had a recent injury – let's stick with the back example. While the customer may have never had back problems previously, the underwriter cannot yet know whether this recent injury will actually trigger a chronic back complaint. Where an underwriter cannot make a clear judgement about the long-term risk a disorder presents, they have no choice but to make a conservative decision.

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Underwriting

What is underwriting? One dictionary definition of underwriting is "to accept liability under an insurance policy". These are very simple words for a very complex process.

When companies 'underwrite' an application for insurance, they are making a judgement about the likelihood of any type of claim occurring during the life-time of the policy.

As policies for life insurance benefits are generally for very long terms, the underwriter has to consider not only the present risk of a claimable event but the risk of one happening in the future as well.

Sometimes these judgements are very simple. For example, someone who is within 'standard build' parameters (ie height, weight, etc), has never smoked, has no family history of serious or inherited disorders, is fully employed in a safe occupation, and has never had any significant illness or injury is statistically likely to have a lower risk of claiming than the average population*.

On the other hand, someone who is significantly overweight, has multiple family members with diabetes, smokes and drinks heavily, has uncontrolled hypertension and elevated cholesterol and works in a high-risk occupation is statistically likely to have a much higher risk of claiming than the average population.

Risk factors that fall between these two extremes are much more difficult to assess.

For example, someone who has had niggling back pain on and off for years does not present any additional risk of premature death than the average population. But the same person has a much higher risk of suffering a temporary period of disability caused by back pain than someone who has never had any back pain.

* Average population statistics are sourced from reinsurance data collected for the combined Australian and New Zealand population base.

Most people who do suffer niggling back pain would not consider it in this light. After all, it has not even come close to causing them a disability so far. However, remembering that underwriters must assess the risk over the life-time of the policy helps explains why their view may be very different.

In this circumstance, and indeed with many other disorders, an underwriting decision can be reviewed at some future date during the life of the policy if the customer believes their health risk has reduced or enough time has passed to demonstrate that an injury was a one-off with no ongoing symptoms. Another example where an underwriting decision could be reviewed is where a customer has been accepted with special terms as a result of their build. If that customer subsequently loses enough weight to fall within the standard build guidelines, then those special terms may be removed altogether going forward.

Underwriters must also take into account the risk that someone's occupation or pastimes pose to their long-term health. Clearly someone who flies helicopters for a hobby has a higher risk of being in a helicopter crash than someone who doesn't. Likewise a power linesman is faced with a significantly higher risk of workplace accidents than a clerical worker.

To summarise, an underwriter's job is to assess the information provided by the customer on the application form. Depending on this information, the underwriter may request additional information regarding their medical history, occupation or pastimes.

The underwriter will then calculate the sum of the customer's combination of risk factors and will compare this sum with statistical information about the risk factors for the average population.

If the customer's risk is considered to be in line with the average population, their application for cover will be accepted at standard rates. If the customer's risk is higher than the average, the underwriter can account for this additional risk by offering the customer special terms.

Unfortunately, sometimes a customer's risk profile is unquantifiable, and in these cases the underwriter may defer cover for a period of time to enable the risk to be quantified. For example, if the customer has recently had abnormal test results or is currently undergoing medical investigations, the underwriter cannot quantify the final risk until a formal diagnosis has been made.

In some circumstances, a customer's risk of a claimable event in the very near future is so high that no cover can be offered and the application will be declined.

Exclusions and loadings (additional premiums)

Where the potential outcome of an additional risk can be easily identified, an exclusion for a specific body part or condition may be offered.

For example, someone applying for disability cover with a history of ongoing lower back pain may be accepted with a lumbar-sacral spine exclusion. That means the customer pays a standard premium but will not be able to claim against the policy if they suffer a disability arising as a result of their lower back pain. All other causes of disability would be covered.

Likewise, someone who has moderate asthma may be offered medical cover with an exclusion for asthma.

However, there are a number of disorders where the outcome of the additional risk cannot be easily identified. For example, a customer with high blood pressure may be at higher risk of cardiac disease, stroke or renal failure. It is not practical or fair to exclude so many major body systems from coverage.

In these circumstances, the additional risk would be compensated for by offering cover at an additional premium over and above the standard premium.

This is called a premium loading and may be expressed in terms of a percentage, eg +100% means the standard risk premium would be increased by 100% (ie doubled).
A premium loading may also be expressed in terms of an

additional dollar amount per 'mille', eg +$5 per mille means the standard annual risk premium is increased by $5 for every thousand dollars insured.

While exclusions are fairly simple to understand, loadings are less obvious. A customer who has well-controlled blood pressure and no other risk factors may be accepted at standard rates. Likewise, a customer who is only slightly overweight but is otherwise very healthy may also be accepted at standard rates.

However, a customer who presents as slightly overweight, combined with well-controlled blood pressure, may be offered a premium loading of +50% as the combination of these two risk factors has pushed the risk profile above that of the average population.

It can therefore be quite difficult for a customer to understand how an underwriter has determined their individual risk profile given they may consider each of their medical conditions to be minor.

Generally, the customer will be aware of any health issues they may have; it's just that they are not aware of how these health issues might manifest themselves in the future.

Clearly everyone hopes that the customer will disprove the statistics, however the underwriter can only rely on statistics to make their assessment.

There is therefore sometimes a disconnection between the customer's very personal view of their current health and the underwriter's objective view of the statistics surrounding the customer's future health risk. This can sometimes lead to customers feeling disaffected when presented with an offer of special terms.

The purpose of this pamphlet is to assist any customer who is offered special terms to understand the process by which the assessment decision was made. Knowing that the assessment is based on purely statistical likelihoods may help lessen the emotions that can sometimes arise.

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