

Protection brief

The panel

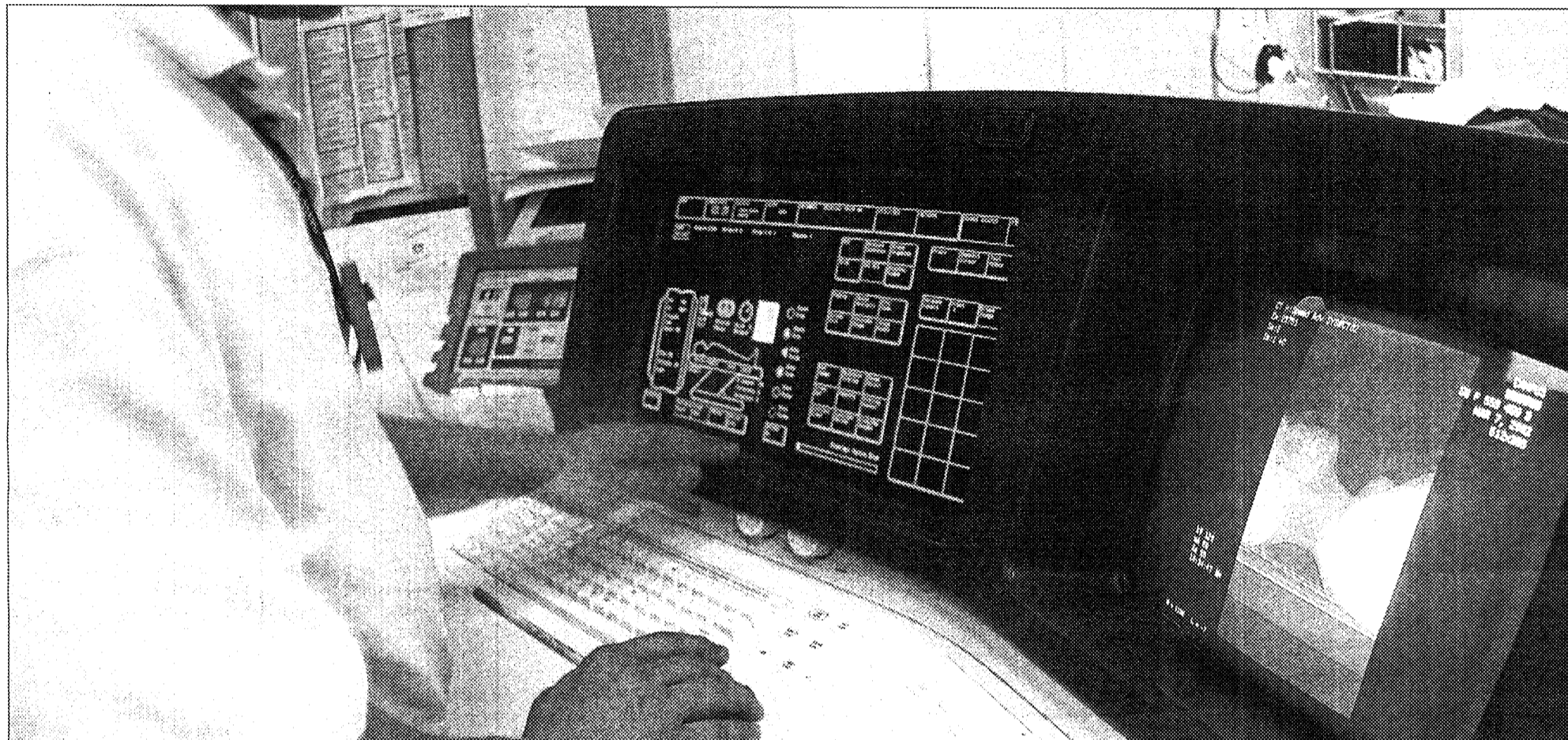
Peter Chadborn,
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Chadborn Baker & Kearle



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Bernie Hickman,
protection director,
Legal & General



Our panel of experts look at the implications of selling PTA under Icob and Cob rules and the ABI's proposed changes to CI

A clear picture

Is the FSA right to consider allowing pension term assurance to be sold under Icob rules as well as Cob?

Chadborn: PTA has played an important role in the past and it will bring a welcome breath of fresh air to the protection industry and should be a significant factor in reducing the protection gap, particularly in the corporate market.

I am pleased that PTA could be sold under Icob rules but wonder how the FSA is going to regulate how the recommendation of PTA could affect other areas under which Icob advisers do not operate, such as the potential effect on the lifetime allowance or pension contribution limits.

Bailey: As a registered individual, it makes no difference to me under which rules I operate. This is the rub, in that non-registered individuals will be able to sell pension term assurance under Icob rules.

The FSA must be confident

that anyone selling pension term assurance who is not registered understands what they are doing, particularly with pension simplification next year and the possible effect on the lifetime allowance.

Will non-registered individuals understand the implications or simply think they are selling a life insurance policy with tax relief? I think the latter. The FSA should not allow this.

Hickman: Pension simplification will enable many consumers to use tax relief to reduce the cost of the life cover they need without restricting the amount they want to save for retirement.

The benefit will obviously be greatest for higher-rate taxpayers but could also be worthwhile for standard-rate taxpayers.

There are limits and other pension details that financial advisers need to be aware of. Pension term assurance is essentially a pure protection contract rather than an

investment contract so it makes sense for the FSA to consider how the many Icob advisers, who currently sell term insurance, could be enabled to offer their customers the benefits of pension term assurance, where it is appropriate.

Will the proposed ABI changes to critical-illness cover make the product less complex and easier to sell?

Chadborn: Making a product less complex does not necessarily make it easier to sell, it still needs to be perceived as a need and be affordable.

The improving clarity objective is welcome if it introduces better information and helps consumer understanding. This will also better educate advisers regarding their understanding of when a claim is likely to be met, increasing the quality of CI sales but perhaps not the quantity.

Future-proofing, although clearly well intended, could

increase misunderstanding to what is already a complex product as some definitions appear to need proof of additional symptoms to support diagnosis and claims

Bailey: In some ways, it will, particularly its desire to improve the clarity to consumers and I do like the proposed change of definition to "specified critical illness", rather than just "critical illness".

Twenty per cent of claims are currently rejected, mainly as a result of consumers thinking they are covered when they are not. Insurance policies such as critical illness stand and fall on the claims and clarity of cover is important.

I also like the proposal to make headings in key feature documents more descriptive as there is more chance of consumers reading the heading, rather than the description underneath.

Hickman: It is difficult to see how the proposed changes

to critical-illness cover will make it less complex. There will always be inherent complexity as the product needs to use medical terminology to define the conditions covered in a legally robust way. Some of this terminology will be more familiar to some customers than others.

What the proposed ABI changes are aiming to do, is to improve the clarity of the product so customers have a better understanding of the products, which will help them make an informed decision.

If the proposed changes are accepted, can we expect the cost of critical-illness cover to fall?

Chadborn: The ABI's critical-illness working party claims that the proposals will help ensure this type of cover continues to be available at an affordable price, so that would appear to be the anticipated outcome.

I am more interested in

the quality of a product rather than the cost so I hope that reducing the cost of CI is not one of the primary objectives of the proposals.

If premiums should fall too low, we could see a raft of rebroking that would not help grow the CI market or help the consumer in the short term. Too much rebroking is already transacted based on price alone.

Bailey: Yes, as the key factor will be a degree of certainty for the reinsurers, particularly with future-proofing and the one aspect insurers hate is uncertainty.

With medical advances being made at such a pace, insurers do not have the certainty they would prefer and it does need to be remembered that such policies are meant to pay out where there has been a major life change.

It therefore seems reasonable to no longer provide cover in the future for an illness which is no

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longer going to affect an individual's lifestyle greatly.

Hickman: One of the challenges for providers, offering critical-illness cover, is the concern that advances in medical technology and treatment mean there is the potential for windfall payments to customers.

The ABI intends, through these changes, to reduce the uncertainty surrounding future medical advances. This increased certainty should allow providers to offer lower premiums to their customers. Clients should also benefit from these changes in that they should bring greater clarity to the circumstances under which they can claim.

Will the frequency and complexity of such reviews make the CI product unsustainable as we know it?

Chadborn: The more that a complex product such as CI changes, the harder it is going to be for those who are advising to keep abreast of developments.

I can see why the current model needs to evolve but believe that the more variables there are in play, the more the consumer will see their ability to claim as a moving target.

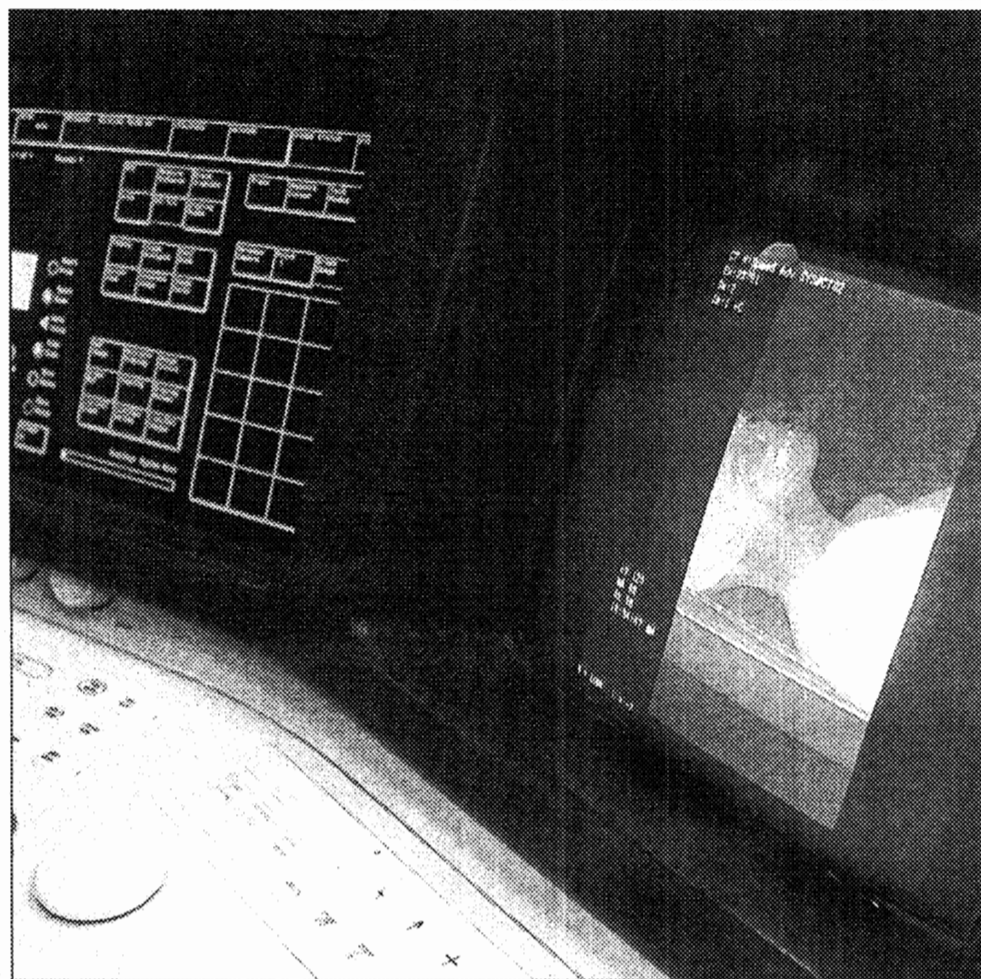
Clients want something that does what it says on the tin, which implies simplicity. If these contrasts do make CI less sustainable, then that is not necessarily a bad thing if the attention is turned to income protection which is often overlooked despite being potentially more appropriate than CI.

Bailey: There should be constant reviews as the development of medical science is so rapid, with insurers reacting to this, for example, with the recent hike in guaranteed premium rates.

The reviews serve two purposes, the first being to have a common standard of illness definitions understandable by the public and second, to shape the industry so the product is sustainable.

Critical-illness insurance is designed to pay out when there has been an illness which has a major impact on an individual's lifestyle so as long as the reviews keep this as their focus, then they are to be welcomed.

Hickman: Before the introduction of ABI critical definitions, there were many more changes happening frequently to products in the market and the product was in danger of being



unsustainable. The ABI has made every effort to make the wordings as future-proof as possible to minimise future changes but, with the pace of change in medical science happening ever more quickly, it is important that the product wordings have a comprehensive review at least every three years to ensure that the product remains sustainable.

In light of the recent FSA bulletin on the sale of critical-illness cover, do you agree with the regulator's concerns regarding the marketing and sale of the product?

Chadborn: The FSA is right to be concerned about CI marketing and sales. Issues such as "unsubstantiated claims about price and coverage", the "impression conveyed that CI is simple" and "key terms and conditions not prominent enough" are particularly prevalent with direct offer marketing.

What do the FSA expect if they allow complex products such as CI to be sold, sorry purchased, without advice and accountability?

Bailey: The regulator is right to look at the promotion of critical-illness insurance but it is the documentation and discussions that a consumer receives at the point of sale that really counts. Promotional material is to obtain an interest and should not be misleading but the FSA should concentrate on whether the information at point of sale to consumers has been given clearly and states what critical-illness insurance does rather than how the initial interest has been generated.

Hickman: Critical-illness

products are higher risk than other general insurance products, owing to the inherent complexity of the medical terminology and definitions of illnesses.

We agree that as much as possible is done to help customers understand under what circumstances the product will and, perhaps more important, will not pay out. Only then will a customer be able to make an informed decision as to whether the product is right for them.

Huge improvements have been made across the industry to ensure that literature and promotional materials are clear and not misleading. It is right that tight control is kept over the messages that are portrayed to customers to ensure the reputation of critical-illness cover is not damaged by misleading statements by a few.

Should the FSA recommend that complex products, such as CI cover and IP, either carry a warning regarding their complexity or should be sold only with advice?

Chadborn: Letting CI and IP products be bought without taking advice is like letting someone face Aussie fast bowler Glen McGrath without wearing a box. Just because they have watched the odd bit of cricket and feel like giving it a go for themselves does not mean that they should do so without taking some advice first.

Reading about the merits of receiving advice in post-sale literature is like telling our amateur cricketer about the merits of appropriate defences as he is staggering back to the pavilion with a sore head, or worse.

I fear that the heralded misbuying trend will cause much damage to the public perception of our industry.

Bailey: The ideal is to have cover a consumer understands and that falls within their budget.

The issue lies in consumers buying a product as complex as critical illness without fully understanding what they are covered for, whether this is directly or via an adviser. A warning of the complexity is therefore important.

A stage further is to ensure that only individuals who are qualified to sell such policies do so and, indeed, ensure they keep up to date with changes and definitions, ideally witnessed via their CPD records.

Life insurance companies should play a more proactive role in developing and training advisers in such definitions.

Hickman: It is vital that all financial products are explained as clearly as possible to customers by advisers and through product literature.

Most literature already contains many clear warnings, especially where products are more complex, so it is not obvious that further warning messages are needed. However, if additional wording can be devised to reduce the potential for a customer to be misled it has to be a good thing.

The focus must surely be on ensuring that literature and promotional material is clear and not misleading rather than denying customers the opportunity to buy products without advice.

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