Income Protection Task Force

The Income Protection Task Force

White Paper II

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COMPILED AND EDITED BY LE BEAU VISAGE AND CWC RESEARCH

With contributions from leading industry experts

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Introduction by Teresa Fritz, Principal Researcher, Which?

As I'm writing this, I can't help but reflect on what a different financial world we are facing now from when the first White Paper was published.

But whilst there is no doubt that the worlds of banking, property, investments, savings and credit are unrecognisable from those we knew two and a half years ago, the very changes that brought about the crisis in those markets could herald a new lease of life for the protection insurance market - and in particular for income protection.

Let's look at the facts. Whatever else may have changed, consumers still need protection insurance, in fact now more than ever. There's nothing like a recession to focus the mind on how you would manage if you lost your job or couldn't work because of illness. So, for the first time in many years consumers are looking to buy products.

But in that perverse world that is financial services, now when consumers most need them, the number of products available is reducing at the rate of knots.

Don't get me wrong. I'm truly glad to see bad value PPI products like credit card and single premium loan PPI in their death throes thanks to the FSA, OFT and the Competition Commission (with more than a little help from CAB, FOS and Which?). These products represented atrocious value for consumers and often meant that good value products were left on the shelf.

But standalone redundancy cover and even some MPPI products did offer consumers affordable, useful cover. However, having flogged PPI and MPPI unmercifully for years, just at the time consumers most need them, providers are running for the hills and withdrawing products or putting up premiums (even on existing policies) to impossible levels. Well done, industry – true to form as always.

However the good news is that the cowardice of PPI providers leaves the field clear for IP providers to fill the gap. In the words of the Walrus: 'the time has come….'.

It's not as if insurers have to reinvent the wheel. There are good value IP products out there as we found when we analysed the market last year. Unusually for financial products, many easily passed the stringent Which? Best Buy benchmarks.

There's innovation too. The new product from Fortis, Real Life Cover, offers a refreshing and affordable protection package covering all the bases. We reviewed the product in Which? Money and welcomed its introduction.

The problem, as ever, is that these great products are just not getting in front of the people who need them.

We don't want to advocate income protection providers selling direct to consumers as PPI providers often did. We still think independent financial advice when it comes to buying good protection insurance is crucial. There will always be some products that are better for some consumers than others, and only a specialist IFA can help you find the right level of cover at the right price for you.

But somehow income protection providers have got to persuade more advisers to sell income protection and have to do this now. Otherwise, before you know it, things will start to lighten up and the providers that were too scared to offer decent products to consumers when they needed them most will start to come back out of the woodwork.

Start talking to mortgage advisers. Although they are not selling many mortgages at the moment, they will be again and they'll need good products to recommend to their customers. Let it be IP instead of MPPI in future.

Bolt on redundancy cover to your income protection product, now, when consumers most need it. I know it's risky, but insurance companies are supposed to be in the risk business – aren't you?   When did insurance start to be something that providers only offered if there was little chance of someone claiming on it?

Even though you might not be able to sell direct to consumers use some of your profits to start promoting the benefits of income protection to consumers. Tell them what a great product it is, why they need it and where they can buy it.

Above all (and I make no apology for repeating myself here from the first White Paper), keep products simple, charges transparent and premiums affordable.

It might be a risky strategy in the short-term, but in the long-term it will pay dividends, for the income protection market and its customers.

March 2009

Executive Summary

1 White Paper I – The nine point plan

Income protection insurance is undergoing both a renaissance and a transformation as economic conditions change and require new solutions to the problem of protecting peoples' finances.

The first White Paper in 2006 corresponded with an upsurge in industry interest in the product but this was not evidenced in terms of sales. Sales of the individual product reached a low-water mark of around 110,000 in 2007 but have increased to just above 130,000 in 2008.The first White Paper set out a 9-point action plan if the product was to achieve greater sales. These included standardisation of non-competitive elements, a rethinking of product design, re-engineering of the application form and the underwriting process and increasing adviser awareness and knowledge of the product. Virtually all of these areas have been worked on but there is still a long way to go before the 9-point plan is complete.

2 Market penetration

Penetration of individual and group income protection stands at about 3.5 to 4 million people. This suggests that penetration into the market it could address has only reached around 20%.

The Task Force believes that the product should be an essential component of financial planning for the majority of working people and concerted action is necessary to improve its profile and increase awareness of the product if it is ever going to meet the goals the Task Force have set.

3 Income protection and the Welfare State

The development of the Welfare State has been one of the most important and enduring achievements in British national life but demographic strains have inevitably meant that government cannot provide adequate long-term income replacement as a state benefit. Indeed the UK Government through its reform programme initiative has been trying to develop new thinking about the value of work and this has created a new approach to providing state benefits through Employment and Support Allowance a benefit that came into force as part of the Welfare Reform Act in October 2008. The new benefit is likely to be paid to around a million less people than the previous Incapacity Benefit if government projections are realised and this should add to the potential appeal and value of income protection.

It is apparent that people are not only unclear about the value of the new state benefits but many are also unsure about their entitlement to sick pay from their employers. The Task Force believes that it is vital that each employed person should be given an annual statement reminding them of their sick pay entitlement.

4 The Essential Protection Index

The lack of awareness of both the incidence of disability and the relative importance of the various generic protection products is such that the Task Force believes that an independent classification of protection products should be available. The recommended option is the Essential Protection Index a star rating classification, devised originally by

Munich Re. Individual income protection emerges at the top of this Index underlining its primacy in the hierarchy of consumer needs that should illustrate the relative priority of protection products.

5 Adviser roadshows

At the moment adviser awareness of income protection is low and there is an urgent need to increase it. The Task force believe this is best achieved by a series of national roadshows, sponsored by Task Force members, aimed at increasing awareness of the value of the product rather than promoting individual product solutions.

6 Payment of claims

One adviser concern is whether income protection claims will be paid. In reality this is not a problem but to heighten consumer and adviser awareness of the product the Task Force suggest an annual report, possibly compiled by the ABI, which shows the level of claims paid by the industry and gives case studies of real claim situations to bolster confidence in the product and to illustrate how the product provides real support to families. This could be constructed as part of a general report on protection insurance.

7 The Competition Commission report on PPI

The recent Competition Commission report on PPI has largely discredited the product because of the high commissions paid to lenders and the poor ratio of paid claims. Nevertheless a product that has outsold conventional income Protection by 20:1 in recent years clearly had appeal and underlines public interest in covering large loans and other financial commitments. As a result of the fallout from the report and as a response to criticism of PPI, companies are seeking non-toxic versions of an income protection product that address the concerns that the Commission highlighted on margins and claims payment ratios.

There are clear lessons for the product that a streamlined approach to underwriting and a simpler product design may lead to greater public confidence in short-term income protection products. The Task Force is very keen to restore public confidence and suggest that one option may be to award a form of “kitemark” to products that conform to satisfactory product design in the short-term income protection area.

8 Group income protection

One of the most important parts of the income protection market is the group arena. Group business accounts for some 50% of the income protection sales in the UK, but sales have not increased in the last few years. There has been real uncertainty in the group market as a result of European Union legislation on age discrimination, which could be potentially disastrous for group income protection writers.

The group income protection market is transforming itself into wider risk management propositions and group providers are involving themselves in absence management, employee assistance programmes and providing portals for brokers as the emphasis moves more towards health education and management in a wider context. Dame Carol

Black's report on the health of Britain's working age population is one of the key influences on thinking in the group market.

There is also likely to be an increased interest in the voluntary group market, which is currently much more developed in the USA and there is a possibility that a State Income protection scheme could be pooled among protection writers to provide cover to small companies or self-employed people.

9 Consumer awareness

Currently, the lack of awareness of the value of income protection and the scale of state benefits creates real customer detriment. This is exacerbated by the appropriation of the term "Income Protection" by writers of PPI and ASU. Currently Google searches using these key words throw up references to PPI writers that cause public misunderstanding and confusion.

Another massive problem is the inadequacy of current distribution channels in the UK to reach the mass market that has traditionally bought PPI not income protection. We have to radically broaden the distribution base in the UK and ally this with a simpler product design so that the product can be sold over the Internet and in Bank branches.

General awareness must be promoted and one possibility could be the creation of a UK organisation similar to the CDA (Council for Disability awareness, a US based organisation). Their website www.disabilitycanhappen.com is an extremely effective tool for underlining the possibility and impact of disability.

Increasing sales of income protection will not be achieved by any one development or innovation. Currently the majority of UK consumers remain acutely vulnerable to massive financial problems if they become ill or unemployed; the industry has failed to educate them about the risks, and provide acceptable products for them. There are clear signs that this is changing and the Task Force hopes that the publication of this White Paper will be the catalyst for a major change in this regard.

1 Income protection – The story so far

1.1 Progress on the 9-point plan

Just over two years ago the Income Protection Task Force looked at a 9-point plan it believed would help to revive the product. Any plan of this sort can look dated upon return two years later but it is heartening that real progress has been made as a result of some of the ideas suggested although others still remain a problem.

Let us look at the work that has been done in each of the areas identified by the original White Paper to see what has been achieved.

Application and underwriting re-engineering

Underwriting has always been cited as one of the problems that income protection has to contend with. More rating factors apply, more aspects come into play and fewer lives can be accepted straightaway at ordinary rates. In the original report the comment was made "Income protection can benefit from new underwriting techniques more than any other product". It is very gratifying to note that the use of tele-underwriting (both big T and little T) is much more commonplace in the industry and rules based systems have been adapted to provide a much more flexible platform for underwriting. It is fair to say that companies are now pushing out the boundaries of what can be done with re-design of forms, reflexive rule-based questioning and re-evaluation of what matters in the underwriting process for income protection. Although there is still a very long way to go there can be no doubt that the underwriting hare is running and product designs and new business procedures are being rethought in an attempt to make the process much more user-friendly and less of a turn-off for the applicant.

The product

Our last report stated, "It is not the role of the Task Force to design products". If it was there would be something radically wrong with the industry and no doubt there would be justifiable claims that there has been real infringement of competition law. Notwithstanding this it was clear in our analysis of market issues that product design needed to be addressed. In the year before the last report was published we reckon three new income protection products saw the light of day. Since the report was published there have been many more focusing on simplification of the proposition and the process and segmenting the market more effectively. Holloway products continue to provide valuable cover, but the rest of the market, unsurprisingly, seems to prefer the white-collar market to blue.

While it is invidious to place too much emphasis on a particular product, the arrival of Real Life Cover (originally from Fortis and subsequently from Royal Liver) was a great example of product innovation driven by distributor experience and provider flexibility. The LV= product, seeking to access the old market that valued MPPI highly, produced a better product for that market than existed before. They removed the "toxicity" from the product that alarms consumerists and journalists so. Conventional income protection it is not, but that is the whole point. There is nothing sacred about the income protection product but there is a great deal to admire about the financial solutions it provides. Our original report called for "alignment with …payment protection " and this has resulted in a fairer and better product. There are many other avenues that can be explored but this does represent a positive way forward.

Regulation

In the original White Paper, we bemoaned the regulator's unwillingness to implement ICOB rules or to apply the spirit of TCF to this aspect of the business. As TCF begins (quite correctly) to bare its teeth we have still not seen a willingness to confront a proper assessment of needs during disability. It is not best served by a product that is both short-term and as likely not to pay out as to meet a claim (ASU); nor is it not best served by a product that provides a lump sum when income is more important and where the most common causes of disability are not covered (critical illness). While these situations still persist the consumer is being led astray and is not receiving the right sort of financial protection. This must not be allowed to continue.

We asked two years ago that ASU/MPPI distributors should make clients aware that long-term income protection also exists and for all providers to identify their product as either short-term or long-term. We re-iterated these comments in our recent letter to the Competition Commission and believe they are taking this suggestion seriously.

Move to essential expenses

We identified the selling of maximum cover (typically 75% of income) as a potential drawback. A product designed to meet utility bills or major household expenses is likely to prove more saleable, easier to underwrite and process and a more straightforward concept than a lot of the IP that is sold now. It should also be considerably cheaper.

Our original suggestion was to have "a default of essential expenses". We urge the industry to consider this approach for any product that they hope to appeal to the mass-market.

Mortgage adviser outsourced process

We identified the likelihood that sales of MPPI /ASU would "fall dramatically as a result of DTI and FSA intervention". The super-complaint made by the Citizens Advice Bureau in fact produced a referral to the Competition Commission. The PPI industry is drinking in a very narrow strip of the Last Chance Saloon!

Our belief from discussions with a number of mortgage advisers suggest they wish to look for a cleaner and more appropriate alternative and many mortgage brokers are re-training to deal with a new era. For the product to work, underwriting must be simplified, the application form slimmed right down and the pricing made transparent and straightforward. ASU did this brilliantly and would be one of the success stories of the last decade if it had represented real value for money. The Insurers now need to find a way to combine ASU's accessibility with a slicker process so that mortgage advisers can sell the product effectively as cover for the mortgage (even if this does not occur at point of sale) because of new regulation.

Consumer awareness

We wanted consumers to be made aware of the potentially disastrous consequences of having to rely on long-term state provision if unable to work. We are repeating our suggestion of "a compulsory annual statement of sickness and other employee benefits" produced to an agreed format. Our market discussions tell us there is much more interest in this idea now.

We also need to engage better with the media to make the public aware of big protection issues. As we write, a campaign is being orchestrated elsewhere in the industry to try to make this happen. The concept has our full support.

We also need better case studies (hence the IPTF site www.protectingmyincome.co.uk) and more celebrity involvement to make people aware that "Disability can happen". This is a huge social issue and the industry must engage with it better.

Adviser awareness and training

Our words in December 2006 were "It is essential distributors are aware of the incidence and impact of illness and disability and the consequences of financial hardship such as social drift. Thus we need to agree a way forward with PFS, IFP and AIFA to create and deliver a plan to ensure distributor competence and consumer benefit"

We are delighted that this dialogue with those associations continues and expect to hold a series of roadshows for advisers funded by IPTF members later this year. This marks a very important step forward.

Collaboration with government

We were keen to align the new Employment & Support Allowance system with the way income protection could work and stated "there is a common interest in rehabilitation, counselling and re-training, suggesting co-operation between the State, NHS and industry".

We have tried to understand how this might work and how we can energise MPs of all political denominations, as well as civil servants to consider this issue very seriously. We hope to make real progress with this in the next few months.

Standardisation of non-competitively sensitive aspects

This has proved perhaps the most divisive of the measures suggested in the last White Paper. The "S" word has been applied with great success and sensitivity by the ABI in respect of critical illness but they tell us that the same opportunity does not appear to exist for income protection because the current product does not cause "consumer detriment". Our contention is that consumer detriment must exist where people do not buy an immensely important product because so much of the distributor base in this country finds it very difficult to compare products because of different policy conditions and formulae that make miniscule differences to the product.

Our report stated that "the ABI Protection committee should examine the case for sensible standardisation of product conditions where it would help consumers and advisers make comparisons and where competition would not be impaired."

We re-iterate this sentiment and hope that the industry can agree to compete on areas that matter having standardised those which only serve to confuse and obfuscate.

Conclusions

Time never stands still in financial services but we believe that the need to revive and enhance income protection as a proposition through a raft of measures, some of which were in the old report and some of which have emerged since is irrefutable. We believe that a momentum has developed which will persuade key bodies to take this issue more seriously and which will make a strong and undeniable case for increasing the sales of income protection coverage in the UK market.

1.2 Overall market penetration and potential

Income protection insurance quite simply provides money each month for an individual who is too sick or disabled to work. Who should buy it?

The answer is everyone who is dependent on earned income, unless they are able to pay essential expenses* from:

- State Benefits
- Salary continuation from their employer
- Savings and investments
- Family and friends

In addition, where the sickness or disability of an individual impacts on the ability of another to work, there is also a need for insurance. Typically, this would be a spouse/partner caring for children or other dependants. Alternatively, this situation commonly occurs in the small business environment.

The greatest need is for those with the most financial dependants who are furthest from retirement. This is not to say that a single man or woman with good income but high levels of debt in their late forties or early fifties does not have a pressing need.

There are those within the industry who believe that those earning less than average income (some £27,000 per annum) should rely on state benefits. Considerably more would suggest that those with an income in excess of around £15,000 per annum should consider purchasing income protection cover.

State benefits do not offer much help with credit card payments!

What is the size of this market? There is no right answer. We need to look at the various data that are available, none of which tells the whole story, and attempt to estimate a reasonable figure from which to work.

Population

The working population in mid 2007 was quoted as 37.8 million**. Of these, we know that 52% were below age 40. Out of this working population, around 2 million were unemployed and 2.6 million were claiming Incapacity Benefit.

The number of people in jobs in September 2008 was quoted as 31.5 million. About 70% are under 50.

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* Essential expenses include mortgage/rent, loans/credit card payments, utilities, groceries, essential clothing and household maintenance
** All statistics in this section are from ONS unless otherwise sourced

Income

In the year to April 2008, median weekly income was £521 for men (£27092 p.a.) and £412 for women (£21,424 p.a.). The bottom 10% earned less than £262 per week (£13624 p.a.). (Source: Annual Survey of Hours and Earnings (ASHE))

Household income

Average household income in 2006/7 was just under £30,000 (final – after tax and including benefits). Average household expenditure for the same period was quoted as £23,869. There is no indication of why there is such a large difference.

The market for income protection insurance

Whilst there is no precise way of calculating anything like true market potential, it is possible to make a reasonable estimate. It can be argued that, assuming insurance is desirable on incomes in excess of £15,000, 75% of those would have a need. We could assume that 1 million are too close to retirement and, let us assume, a further million have other resources.

On this basis, the potential size of the market is some 21 million.

Current market penetration

The number of lives covered under group schemes is about 1.75 – 2 million.

It is estimated that the number of those covered by individual policies is about the same, although this includes policies to cover mortgage payments. It is estimated that such policies accounted for 40% of new sales when the mortgage market was buoyant. Thus the total number of policies in force appears to be between 3.5 and 4 million.

This means that over 80% of the total estimated market of 21 million is uninsured. This ignores potential to increase cover of existing policyholders. Notwithstanding the crude manner of calculation, it is very clear that penetration in the market is extremely poor, especially when it is remembered that there are some 20 million PPI policies in force.

Income protection-current market issues

It is easy to find reasons for not writing income protection and the arguments are well rehearsed about why it has sold so poorly despite the seeming belief throughout many parts of the industry in the inherent virtue of the product.

While there has not been a huge explosion in IP-related activity, the progress referred to in the 9-point plan indicates that steps are being taken to write the product in a more user-friendly and effective way. Big process improvements have been made and perhaps most encouragingly, a range of interesting new products in the Individual and group markets has emerged.

The most important message that any group interested in the subject needs to understand is that it is the concept of protecting income that is important, not an adherence to any product design or way of writing business. Thus, the re-thinking by, for example, Fortis and LV= in their new plans is indicative of product designers trying to solve problems rather than remain unswervingly loyal to a product that clearly needs to be adapted despite its many virtues.

The criticism that in many cases rightly attaches to some PPI products should not overshadow the fact that these products are easy to write, clearly persuade people that they have a need for them and are a simple sales proposition. The opportunity for a less "toxic" product to emerge which is much more appropriate for protecting income and which replicates the sales attraction of PPI is a very important challenge which the protection industry must not flunk.

If the history of income protection tells us anything it is that we have failed as an industry to convince people of the value of the product and this means that millions of people run the very severe risk of massive financial meltdown if they are unable to work through sickness or accident.

The huge publicity surrounding the current economic problems focuses inevitably on the likelihood of widespread unemployment and the consequent threat to household finances across the country. This is a very understandable concern; yet one real frustration is that neither we the industry, nor the Government, are willing to spell out the consequences of long-term sickness absence. Nothing underlines our inability to explain people's vulnerability to this very real risk than the yawning size of the 'Income Protection Gap' which approximates to something like £180 billion.

It may be that a government can be forgiven for failing to emphasise the inadequacies of its welfare system, particularly when it has manifestly tried to introduce real and rational reform but can we excuse an industry that exists to provide help and support through its products, yet which chooses too often to emphasise its commitment to alternative products that provide higher margins or simpler sales.

The biggest problem that income protection faces is that the industry that exists to provide it is largely apathetic about the product's existence and unconcerned about meeting the needs of millions of potential customers. All of the focus on Treating Customers Fairly sounds like empty rhetoric when a major need is so blithely ignored.

This is the really important challenge that the industry faces. Does it want to rise to a huge challenge that it has ignored for so long or is it content to continue to ignore it and see income protection remain a niche product and an afterthought for most advisers in the UK?

2 The impact of welfare reform

State benefits - back to the future

Recent changes to the state welfare system have seen a return to some of the principles first outlined by Sir William Beveridge when his recommendations were published in 1942.

Beveridge stated that “social security must be achieved by co-operation between the state and the individual” and in the report’s conclusion, he wrote that the plan was “not one for giving to everybody something for nothing” but involved “contributions in return for benefits.”

In describing the principles behind the government’s latest reforms, ministers now talk about a “something for something” system transforming benefit claimants from “passive dependents” to “active job seekers” and when launching its White Paper[1] in December 2008, Work and Pensions Secretary, James Purnell said that, “In future virtually everyone will be expected to do something in return for their benefits.”

More controversially, some would argue that we are also seeing a return to other Beveridge principles when he wrote that “The State in organising security should not stifle incentive, opportunity, responsibility; in establishing a national minimum, it should leave room and encouragement for voluntary action by each individual to provide more than the minimum for himself and his family,” and that “to give by compulsory insurance more than is needed for subsistence is an unnecessary interference with individual responsibilities.”[2]

Background to the current reform process

To reach this point has been a long and difficult journey for the present government since it first appointed Frank Field to ‘think the unthinkable’ as Minister for Welfare Reform in 1997.

In truth, the need for change within the state welfare system and, in particular, sickness benefits, had been apparent to both sides of the House for some time.

Heavily influenced by a series of social changes including,

- Greater economic prosperity
- The changing nature of the labour market and patterns of work
- Patterns of retirement
- The role of women
- Increased life expectancy
- Changing attitudes to work, sickness, disability and the receipt of state benefits,

[1] “Raising expectations and increasing support: reforming welfare for the future”, DWP - December 2008
[2] The basic weekly rate of benefit under Employment and Support Allowance is £84.50 for those in the work related group and £89.50 for those in the support group (due to rise in April 2009 to £89.80 and £95.15 respectively)

the State welfare system had already moved well away from Beveridge's vision in both its scope and emphasis to one where:

- His ideal of 'universal' entitlement had been replaced by the selective 'targeting' of benefits at those most in need and
- There was a strong emphasis on the protection of the chronically sick on the grounds that they were in greatest need and therefore entitled to benefits, rather than looking at what role they could continue to play in the workplace and society in general.

A range of new benefits had been introduced (including Attendance Allowance in 1971 and Mobility Allowance in 1976) and existing benefits enhanced where the claimant was sick or disabled, based purely on the nature of the condition and the level of disability, not on what was required to return the individual to the workplace.

By 1995 the costs were seen to be out of control. In just 15 years the number of Invalidity Benefit claimants had increased to more than 2 million from less than 750,000 in 1980 at a time when general life expectancy had improved considerably.

In reality, the number of new claimants had remained more or less constant but the problem was that fewer people were moving off benefit and achieving a successful return to work. Invalidity Benefit had also become a cover for hidden unemployment and a route to early retirement.

The replacement of Invalidity Benefit with Incapacity Benefit in April 1995 was the first step in trying to curb such trends by focusing benefits on those claimants who were 'genuinely and medically incapable of work' to be achieved via the introduction of a new medical test of incapacity, the "All Work Test".

At the same time, however, the nature of the health conditions underlying incapacity claims was changing. The social security system had been designed for people with severe medical conditions and obvious physical disabilities where objective evidence of that condition was easily available. Now claimants were presenting with more common and less severe conditions where objective evidence was more difficult to identify. A much greater proportion of claimants were reporting mental/behavioural disorders or musculo-skeletal conditions, due not so much to an increase in those conditions in the population as a whole but to the relative lack of success in dealing with such disorders in comparison to the progress made in other areas.[3]

It became increasingly clear that the replacement of Invalidity Benefit with Incapacity Benefit and the introduction of the All Work Test did not go far enough and with the arrival of the new Labour government, the Department for Work and Pensions embarked on a wider consultation process embracing the public, private and voluntary sectors.

The basis for reform

The consultation process concluded that a great many improvements were needed in the way that Incapacity Benefit claims were handled including:

- Earlier intervention
- A more personalised approach to claimants, not formulaic form filling
- Better and more targeted rehabilitation and re-training services

[3] Note: Considerable progress has been made with the treatment of musculo-skeletal disorders in more recent years

- Financial incentives to return to work
- Greater responsibility on claimants to seek work as a pre-requisite for payment of benefit (conditionality)
- Better co-ordination of benefits and services across government departments
- Greater recognition by health professionals of the importance of work
- Better engagement with employers in improving workplace health
- A need to improve the rights of disabled people

The insurance industry was an important part of the consultation process and many of the ideas listed above came from interaction with the leading insurers and reinsurers, reflecting both those things that best practice providers were doing well at that time in order to control their claims experience and things that they would like to do better in the future.

In reviewing its conclusions, however, the government realised that it was not possible to achieve all this immediately. Conditionality could not be introduced for claimants unless services able to help them back to work were in place and evidence of what constituted effective rehabilitation was limited. The government therefore opted in the short term to improve both its own administrative processes and the rights of disabled people, whilst piloting service changes to see what worked and what did not, in order to create a better business case for both the Treasury and employers.

This led to a series of initiatives including New Deal for Disabled People (1998), Securing Health Together (2000), NHS Plus (2001), Job Retention and Rehabilitation (2003), Pathways to Work (2003) and Workplace Health Connect (2006).
Of these, the most successful and far-reaching was Pathways to Work. Its major characteristics are shown below:

Characteristics of Pathways to Work

- Initially, mandatory for new and repeat claimants (existing claimants could volunteer). Later extended to existing claimants of up to 2 years duration
- Claimants dealt with by more highly skilled Personal Advisers
- Access given to a wider range of job related services (the CHOICES package embracing: rehabilitation, retraining, assistance schemes, in work support etc) co-ordinated by Personal Advisers at JobCentre Plus
- NHS designed Condition Management Programmes with a particular focus on mental health, musculo-skeletal and cardio-vascular conditions; aimed at improving patients' understanding and self-management of their condition and increasing their confidence in dealing with it via self-help, pain management, diet, exercise etc.
- A series of 6 Work Focused Interviews at monthly intervals commencing 8 weeks after claim, leading to an agreed action plan
- Earlier medical assessment
- Benefit sanctions for non-compliance where action is mandated
- Financial incentives to return to work including:
    - Job Preparation Premium - £20 per week for 26 weeks on completion of an action plan
    - Return to Work Credit - £40 per week for 52 weeks for those earning less than £15,000 per annum
    - A Discretionary Fund for use by Personal Advisers to help claimants prepare for work (e.g. clothing, tools, transport etc)

These pilots have delivered a clear financial return to the Treasury. For new and repeat claimants this has so far been calculated to be £1.51 for every £1 spent and this return will grow the longer former claimants remain in work.[4] For existing claimants, evidence is more limited and a full financial analysis is not due until later in 2009 but early indications appear positive for this group too[5]. Whilst the current economic situation will not make continued progress easy, the incentive remains to invest in this area because the Treasury, already aware of the huge financial impact of large numbers of benefit claimants, can now also see that investment in such services pays.

As a result, Pathways to Work has now been rolled out nationally as part of the new Employment and Support Allowance and, from a peak of 2.82 million in November 2003, the total number of Incapacity Benefit claimants has reduced steadily to 2.63 million in November 2008 and plans are now afoot to move existing claimants onto the new regime.

Employment and Support Allowance and beyond

Employment and Support Allowance was introduced on October 27, 2008 as a replacement for Incapacity Benefit. Initially, this applies to new and repeat claimants only but there are plans for a phased transfer of existing Incapacity Benefit claimants to the new regime between 2010 and 2013 to include a complete re-appraisal of their condition and capability to work.

Key features of the new benefit are shown below:

Characteristics of Employment and Support Allowance

- A 13 week assessment period to include a face to face Work Capability Assessment with a health professional and a Work Focused Interview with a Personal Adviser (earlier intervention)
- The Work Capability Assessment will act as a gateway to the benefit (pilots suggest that around half of new claims will be rejected at this point) identify what the claimant can do as well as what they cannot and what help and support is needed to return them to work
- Two benefit levels depending on whether successful claimants are considered capable of work related activity (estimated at 90% of new claimants) or not and thus in need of support
- Two benefit qualification streams:
    - Contributory (entitlement based on National Insurance contributions)
    - Income related (incorporating means tested Income Support as a result of ill health)
- Failure to provide information necessary to assess the claim, attend a Work Capability Assessment or follow medical advice may disqualify the claimant from benefit entirely
- Benefit reductions (sanctions) if the claimant fails to attend a Work Focused Interview or fails to assist with devising a work focused action plan without good reason

[4] "A cost-benefit analysis of Pathways to Work for new and repeat incapacity benefit claimants", DWP Research Report 498 – May 2008
[5] "Evidence on the effect of Pathways to Work on existing claimants", DWP Research Report 488 – May 2008

And the reforms are not intended to stop there.

Following a Consultation Paper in July 2008[6] and two specialist reports[7], the government has announced a series of further changes[8] of significance for individual Income Protection insurance. Many of these will be piloted first and may initially be trialled with claimants for Jobseekers' Allowance. Further details are contained in a new 2009 Welfare Reform Bill.

These include:

- A tightening of the qualifying rules for National Insurance contributions from 2010
- A new electronic 'fit note' in 2009 to replace paper based GP sickness certification, with the emphasis on work capacity not incapacity
- Further improvements to the Work Capability Assessment and its extension to re-test existing claimants on a regular basis (a minimum of every 2 years)
- Supplementing the medical assessment process with an assessment of the claimant's working skills and, where necessary, requiring those with skills gaps to attend for appropriate training as a condition of benefit from 2010
- Extending Work Focused Interviews so that claimants of 6 months duration are then interviewed quarterly for up to 2 years
- Extending conditionality from the requirement to attend Work Focused Interviews and agree an action plan, to requiring the engagement of claimants in at least one of the work related activities in their action plan, with an escalating scale of benefit sanctions for non-compliance – to be piloted from late 2010
- Piloting a requirement for long term claimants of more than 2 years duration to engage in community work in order to maintain their benefit
- Devolving the responsibility for providing rehabilitation and retraining services to long term claimants to private and voluntary sector providers, rewarding them from the benefit savings achieved – to be piloted from 2010/11
- Piloting a requirement for claimants with drug or alcohol problems to enter a rehabilitation programme as a condition of benefit or face benefit sanctions
- Extending the assessment of capability to work to the partners of benefit claimants claiming means tested support from 2012/13
- Temporary improvements to means tested Mortgage Interest Relief support payments reducing the waiting period from 39 to 13 weeks and increasing the capital limit on which it is based from loans of £100,000 to £200,000, which took effect in January 2009
- A disregard for child maintenance payments in the calculation of means tested support from April 2010
- Establishing an employer led national campaign to engage more employers in recruiting and retaining disabled people

[6] "No-one written off: reforming welfare to reward responsibility", DWP – July 2008
[7] "Working for a healthier tomorrow", Dame Carol Black's Review of the health of Britain's working age population for the Departments of Health and Work and Pensions – March 2008 *and* "Realising Potential: A Vision for Personalised Conditionality and Support", Professor Paul Gregg for DWP – December 2008
[8] "Raising expectations and increasing support: reforming welfare for the future", DWP - December 2008 *and* "Improving health and work: changing lives, The Government's Response to Dame Carol Black's Review of the health of Britain's working age population", DWP and DH – November 2008

Implications for income protection insurers

There are both positive benefits and important challenges to the income protection industry as a result of these government reforms.

For example:

- The reforms draw attention to the importance of protecting income in the event of inability to work through ill health as a protection issue
- For most potential purchasers of insurance, the level of benefit paid by the State, assuming that the claimant passes through the assessment process successfully, is unlikely to meet their needs and offers an opportunity for insurers and intermediaries to emphasise the potential shortfall in income that could occur
- Action taken by the State system at a time before the expiry of most private insurance deferred periods may encourage many IP claimants to return to work
- Through a system of pilot programmes, dedicated budgeting and robust financial analysis, the Treasury has shown that investment in early intervention and rehabilitation services pays
- Much useful evidence on different approaches to rehabilitation is emerging which will undoubtedly improve its effectiveness and lead to the establishment of best practice standards which will also assist insurers

However:

- The industry will have to provide clear messages to consumers about how effectively income protection products and services integrate with and enhance the State proposition

    - In comparison to Incapacity Benefit, Employment and Support Allowance is simpler in structure but offers variable benefit levels more related to individual need. Can insurers produce clear and simple benefit formulae to take account of this?
    - In addition to its early interventionary nature (acknowledged by all as being of primary importance) the key success factors for Pathways to Work are seen to be financial incentives to return to work, access to Condition Management Programmes provided by health professionals and the personalised nature of the service provided by JobCentre Plus Personal Advisers. In the light of this enhanced range of services offered by the State, can insurers still demonstrate added value from the services that they provide?

- The increasing introduction of 'conditionality' as a pre-requisite for payment of benefit in the State scheme and the absence of any requirement for insurance claimants to engage in any form of work related activity, potentially leaves insurers more exposed to poor experience.

    - In describing the relative merits of private insurance to augment the State scheme, the industry should be careful not to give the impression that it is much easier to claim benefit from private insurers, with no need to demonstrate any willingness to return to work
    - At the levels of benefit often paid by insurers, might some claimants simply give up on the State benefit process in the belief that insurers are a comparative 'soft touch'?
    - Would insurers really be happy to make payments to many claimants rejected by the State scheme or assessed as capable of work related

activity but facing benefit sanctions for non-compliance with the back to work regime?

- State benefits and services are becoming more integrated and 'joined up', whilst the insurance proposition in the event of ill health is still fragmented (income protection, payment protection, critical illness, private medical etc) even where some measure of choice is provided through menu plans. Are the needs of modern day consumers being met effectively?

As described earlier, the insurance industry was an important contributor of ideas to the reform of State sickness benefits and the question needs to be asked as to what degree the industry has moved on and whether it is now being overtaken by the State sector in terms of effective claims management, ensuring that benefits are paid to those in genuine need and offering a range of services which enable those claimants capable of returning to work to do so.

Opportunities for further co-operation with the State

The insurance industry shares many common interests with the State in terms of educating the public about the risks that they run and how to protect themselves both physically and financially, as well as in the development of effective evidence based services able to return as many claimants as possible to the workplace.

If it is to achieve its target of 80% of the working age population in work, the government needs to return 1 million IB/ESA claimants to the workplace by 2015. Equally, alleviating financial loss sustained by families in the event of ill health is not only important in reducing the level of means tested benefit but also to achieving the government's target of eliminating child poverty by 2020.

Opportunities still exist for insurers to contribute to and benefit from government pilot programmes and a better integrated public/private protection system which clearly illustrates where State protection ends and private protection begins and the choices that are open to consumers to tailor private protection plans to better meet their own individual needs, would be of benefit to everyone and should provide a key element of the Money Guidance advice scheme being designed by the FSA for potential insurance customers.

An idea to develop with government and help provide better advice to consumers

One of the greatest barriers to providing good advice to consumers is their lack of knowledge about what alternative protection is provided by the State and by their employer in the event of being unable to work through ill health.

The replacement of Incapacity Benefit with Employment and Support Allowance provides a perfect opportunity to highlight the level of protection afforded by the State but most employees are also far from clear about the benefits provided by their employer.

An opportunity exists to work with government to encourage the provision of a clear statement from employers of what benefits are provided to employees in the event of sickness absence. As a minimum, this should be provided to a new employee on joining an employer and at such time as the employer's policy changes but ideally should be provided on an annual basis, in much the same way that pension benefit statements have evolved.

Understanding both entitlement to benefit and the potential vulnerability from a financial perspective if sustained disability should strike is, we believe, a fundamental necessity to enable individuals and families to arrange their financial planning. The outstanding job that the Welfare State has done over the last 60 years to provide, nurture and support has perhaps lulled people into a false feeling of security. The paternalism of employers has lessened in the face of commercial reality and demographic change has meant the Government has had to scale back its provisions.

The annual statement might also be issued by the National Insurance Office to self-employed people. Its purpose is to inform and make people aware of the need to take steps to protect themselves and their families if serious disability should strike.

For self-employed people an annual statement of the state allowances would be very helpful and could be distributed at the beginning of each tax year when new tax codings are provided. Whilst it could be argued that the allowances can be found by anyone seeking them from Government sources and official websites, we would argue that so great is the likely vulnerability of many self-employed people who are long-term disabled that the levels of State benefit need emphasising.

In reality the willingness to make personal provision may stop otherwise uninsured people becoming a drag on the UK economy. At the moment it is still possible to detect the belief that we exist in a “Welfare Cocoon” but in reality if this ever truly existed it was unwound many years ago.

3 Awareness of income protection

Those who want you to buy income protection have a reason for their belief in the product. It was one of the themes of the first White paper and it remains a fundamental fact:

- Protecting your income stream is the most important financial priority people have.

This simple but vital fact is not universally acknowledged for a number of reasons. Some people in the industry feel that buying critical illness cover takes care of this situation; it does not. Critical illness cover is an excellent product for ensuring that you can dispense with some capital commitments in the event of certain serious illnesses. These serious illnesses do not include the two most likely to strike you down (depression or musculo-skeletal disorders) but it fits well as part of a mortgage package.

Some feel it is unlikely that they will be unable to work for long periods; others believe they have more pressing day to day claims on their household expenditure. The simple fact remains that millions of people remain terrifyingly exposed to financial meltdown if they become long-term disabled. The other great excuse for not purchasing –"The State will provide " is patently untrue. A benefit of a shade over £80 per week is never going to be adequate to maintain a previously comfortable lifestyle. Income protection insurance is an immense priority and government, regulators, the UK protection industry and the public all need to understand this.

Unfortunately the message from a range of different research all points to an overwhelming lack of appreciation of this situation.

A Canada Life survey carried out in November 2008 highlighted this very well. They carried out a study to determine how people would try to fund a period of long-term absence.

When asked how they would fund their current lifestyle if they were unable to work, only a small minority said they would use their individual (9.7%) or group (5.6%) income protection policies; nearly half of respondents said they would rely on their savings alone.

It is hard to argue with Canada Life's conclusions:

"These results highlight the worrying statistic that 85% of consumers would suffer financially should they be deemed unable to work through illness or injury as they do not have any form of income protection in place. With the current unstable economic environment, those who believed they would use savings alone to fund their lifestyle could find their "rainy day" pot is already stretched."

The Protection Review survey released in mid-2008 also highlighted a worrying number of people who haven't purchased health insurance.

The reasons given were as follows;

Q What is the main reason why you have not purchased health insurance?

- I haven't thought about it - 22%
- Can't afford it - 21%
- The State will look after me - 15%
- Other priorities - 13%

- I don’t trust insurers to pay claims - 8%
- Other/Don’t know - 19%

It is interesting to note the increase in people who believe that the State will provide for them, a clear case of the “NHS effect”. This clearly and unsurprisingly is much more important in health insurance than in life protection. About 46% of the sample felt they did not have sufficient health insurance.

There are some clear variances:

- 27% of women claim not to have considered health insurance but only 16% of men admit this
- Only 9% of the 35-44 age group have not considered buying health insurance
- 29% of ABs admits to not having thought about buying health insurance but the figure among DEs is only 18%.
- 34% of DEs believe that they can’t afford it (this figure drops among ABs to 11%)
- 25% of the 45-54 age group think the State will look after them
- 22% of those in Scotland also share this view (although it may in reality be a different State with the Scottish Parliament!). These figures are significantly higher than the average
- In the 45-54 age group only 5% felt that they had other priorities (a very low figure compared with the average), yet this was the group with the highest expectation of State provision
- 12% of Males don’t trust insurers to pay claims set against 5% of women
- 14% of ABs in the 25-34 age group didn’t trust insurers. This figure dropped to 4% amongst 18-24 year olds (it was 2% for life insurance in this age group)

Source: Protection Review 2008 in association with Swiss Re/ICM

Although the survey covers private medical insurance as well as income protection, it is reasonable to presume that the answers given would not vary much across these two products. The amount of individual IP and PMI in force is broadly similar.

The conclusion in last year’s Protection Review was:

“These differences suggest health insurance excites greater emotion and concerns than life insurance but some of the anomalies are surprising. The level of trust among 18-24 year olds is gratifying and there appears to be more difference in attitude between men and women regarding health insurance than life insurance.”

The survey also looked at the issue of trust and whether the public believes that insurers will pay claims.

Q To what extent do you trust companies to pay out claims?

1 Life insurance

- Trust a lot - 38%
- Trust a little - 36%
- Do not trust at all - 20%
- Don’t know - 6%

2 Health insurance

- Trust a lot - 35%

- Trust a little - 37%
- Do not trust at all - 21%
- Don't know - 8%

These figures suggested trust levels were high and, indeed, there does not appear to be a strong public perception that insurers resist paying income protection claims.

The survey also looked at why consumers did buy health insurance:

Q What is the main reason why you have purchased health insurance?

- It is part of our financial planning - 46%
- I bought it with my mortgage/loan - 12%
- I consider it a financial priority - 11%
- I was persuaded to by an insurance salesperson - 3%
- Other - 24%

Source: Protection Review in association with Swiss Re/ICM

These results were broadly similar to the life findings with a significant percentage of those who have health insurance (which was just over 50% of the sample) buying it because they considered it as a natural part of their financial planning or it was a priority. It might be estimated that many of the same people who regard life insurance as key cover also bought health insurance for the same reason. The only material difference is that the figure is lower for those who purchased it with their mortgage or loan.

The cover was bought in the greatest proportions by those aged 35-44 and by those over 55; 48% of those over 65 considered health insurance as part of their financial planning.

One of the key points from the first White paper was the establishment of a "Hierarchy of Needs". The Income Protection Task Force firmly believes that this is a priority for the protection industry in the UK and until we have a debate of this subject we will not be providing the right focus to meet most consumer's needs.

One way of looking dispassionately at the various protection products is provided by Munich Re's concept of "The Essential Protection Index". We reproduce, with their kind permission, their description of its methodology and conclusions.

The Essential Protection Index

What needs to be done?

If our product range is too extensive and confusing, then we must make it simpler and clearer. If salesmen do not understand complex definitions and overstate the breadth of cover, then we must improve our training and clarify the message or remove the potentially toxic product. If the sales remuneration creates product bias, then we must rebalance effort and reward. If consumers are uninformed and too easily influenced, then we must further improve the marketing literature and the sales process and documentation, or find a way to provide a simple guide to product suitability.

Sometimes the greatest prominence needs to be given to what the product will not do. For example:

Critical illness will not cover many of the conditions that stop you from working.

or:

Mortgage payment protection Insurance will not cover any existing medical conditions or related conditions.

Whilst we struggle with reviewing our business practices across many fronts, we should consider a fallback solution.

This should address the issues that salesmen need help in prioritising products and that consumers need a simple method of informing them of the most effective solutions to meet their needs. This issue has been given relevance, when the Treasury Select Committee suggested a standardised risk rating for investment products, as opposed to the 20 page document setting out the key facts, which MPs likened to an encyclopaedia. This was further considered in a joint report by Cicero Consulting and Brahm Research, which found that 84% of people believed that a simple risk indicator would help investors to make the right decision.

The challenge to the protection industry is to develop a rating approach that simply and effectively maps our products against the protection needs of consumers. The consumer impact of effective rating systems can be dramatic. One particularly effective example is the Euro NCAP (European New Car Assessment Programme) grading of car safety, which has improved car design and made safety an important selling point to a risk-averse public. The organisation was backed by the European Commission, five European governments and motoring groups in every EU country and provides motoring consumers with a realistic and independent assessment of the safety performance of some of the most popular cars sold in Europe.

Star ratings for insurance products

The effectiveness of protection insurance is analogous to the safety features in cars, where the risk of needing the safety feature is low, but the consequences of poor design are potentially disastrous. In the insurance world we appear to say 'what kind of crash do you want protection against?' and then sell leather seats before the brakes.

Protection insurance could therefore really benefit from a realistic and independent product effectiveness assessment system. Clearly there would be limitations to such a system, but the concept may at least help to ensure that prominence is given to the most effective financial safety net products and help consumers to avoid the worst. As an absolute minimum, it should temper unrealistic expectations and help to avoid the mis-selling or mis-buying of products. However, no simple index can replace the quality of advice given by a well-trained adviser.

At its core, life protection insurance should provide effective security against low risk serious health events, resulting in death or long-term disability, which would otherwise cause significant financial hardship. In this context, we should also consider the impact of unexpected unemployment.

In due course when we have the basics right, it could be extended to methods of reducing the risk and/or severity of these low risk events through advice and wellbeing services.

Any rating system must be able to measure the severity of these events and their financial consequences for the consumer. The approach outlined below focused on those events that result in a lost earnings capacity and is based on three key measures. These are the probability of a loss of earnings event covered by the insurance, the proportion and duration of the earnings replacement and the generic quality of insurance cover (i.e. whether it had pre-existing conditions, was cancellable by the insurer, etc). Benefits payable on events that do not result in a loss of earnings are not considered in this rating system as they are deemed to be non-essential.

The maximum five star rating is awarded for a protection package that covers all the lost earnings events (i.e. death, occupational disability and involuntary unemployment) with a benefit package that replaces net pre-disability income for the period the claimant cannot work, up to the policy expiry (but limited to one year for unemployment).

The analysis below is based on a male non-smoker, Occupation Class I, and uses Munich Re pricing assumptions but can easily be extended by age, sex, smoking status, and marital status and occupation.

Product	**Standardised**		**Typical**	
	Benefit (annualised % salary)	Star rating	Benefit (% or multiple of salary)	Star rating
Decreasing term life cover only (DTA)	65%	1.25	3 * salary	0.50
Level term life cover only (LTA)	45%	1.00	4 * salary	0.75
Family income (FIB)	60%	1.25	50% * salary until expiry age	1.00
Five year budget IP	65% for five years	1.25	50% * salary for 5 years	1.25
Full term IP	50%	1.75	60% * salary until expiry age	2.00
DTA + ACI	20%	0.50	3* salary	1.00
LTA + ACI	20%	0.50	2* salary	1.00
Involuntary unemployment	55% for one year	0.50	30% for one year	0.25
Accident and sickness	35% for one year	0.25	30% for one year	0.25
Five star rating	n/a	n/a	70% * salary until expiry age	5.00

Notes:

1. The ratings are rounded to the nearest quarter star.

2. For occupational disability products (IP, CI and AS) State Incapacity Benefits (under the previous system) have been added to the insurance covers, assuming two-thirds of claimants qualify. For an income of £35,000 this amounted to an additional 10%, or one quarter of a star.

3. In this example, five stars equates to 100% of pre-disability net income (or 70% of gross income) replacement until expiry age on death and occupational disability and one year for involuntary unemployment. These proportions apply to generic products and should be adapted to the specific plans considered by the adviser.

4. The annualised benefit is the percentage of gross income and runs to expiry age of 65, unless stated otherwise.

5. The ratings assume that all covers are necessary, which would not be correct where there are no dependants.

6. The standardised results exceed the typical cover results where the typical benefits purchased cost less than the standardised premium and vice versa.

Some other key points to note are:

Accelerated CI needed to be separated into the standalone CI disability component and the residual death component. It was then necessary to determine the percentage of standalone CI claims that would result in occupational disability. For this, two measures were used. The first was that 45% of IP (deferred 26 weeks) claims would trigger a CI claim. The second was that 30% of CI claims would result in occupational disability (using our internal claims assessments). In other words, 70% of standalone CI claims would not result in occupational disability and the corresponding proportion of the premium could be deemed to be non-essential where the purpose of the cover was to protect against occupational disability.

Two scores were calculated for each product type. The first standardised the covers purchased based on a fixed unit of premium (£300 per annum) and the second was based on typical benefit scenarios, regardless of the relative premium differences. In each case, lump sum benefits were converted into incomes. For the standardised covers, the sum insured was annualised over the remaining cover period. Income benefits were not changed. For typical covers, the sum insured was used to maximise early income replacement, subject to the point below.

The maximum income was limited to 100% of pre-disability net income. This equated to 70% of gross earnings, for the salary used of £35,000. For occupational disability, it was assumed that claimants could also qualify for State Incapacity Benefits and this sum was deducted from the maximum allowed insurance cover. However, in determining the star rating, it was assumed that only two-thirds of claimants actually qualified.

The Essential Protection Index (EPI) revealed:

The star rating is equal to the probability of a covered lost earnings event, multiplied by the weighted present value of the replacement earnings and multiplied by the generic quality of the insurance cover. The individual component product star ratings for a male non-smoker are as follows:

The factors used for the star rating can undoubtedly be improved, but the broad shape of the results looks reasonable. The likelihood of a covered event and the duration for which earnings are impacted are the key factors. Whilst the probability of disability is three times that of death, with disability there is a chance of recovery!

The relative positioning is interesting. In both the standardised and the typical scenarios, full term IP scores the highest.

Thereafter, for the standardised ratings the DTA life only, the family income benefit and the five year budget IP are equal second. For the life only covers, this is because one unit of premium (£300 per annum) purchases significant cover. This is also the reason that the standardised CI products score poorly, as their purchasing power is low. Without the additional state benefits they would have scored even lower. For the typical covers, the five-year budget IP comes second to the full term IP, with the CI products and family income benefit joint third. Full term IP scores one star above the CI products. If family income benefit life cover were also added, then it would score two stars above the CI products, which also include a life component.

With our current products, the five star rating is almost unattainable because the maximum IU benefit is normally limited to 120% of the mortgage costs. In addition, the maximum benefits for IP covers do not allow for the uncertainty of state incapacity benefits
.
A topical example from the Consumers' Association investigative report is MPPI versus a budget IP and IU package. The ranking shows that a five year budget IP solution scores significantly better than an AS plan, given the extended income replacement duration and the generic quality of the insurance.

How can the EPI be used?

The star rating could be recalculated for any age, sex, occupation and marital status. It could also be converted from generic products to specific policy terms and conditions.

However, the relative product line star ratings should remain resilient. In normal circumstances, the protection applicant should look to achieve the highest star rating, taking account of all existing covers (including employee benefits) and available budget.

Where the applicant has existing insurances or employee benefits these should be factored in, and then the increase in the star rating from any new cover should be maximised.

Where additional benefits are purchased, this will increase the rating results, until the maximum income replacement level (of 70% of gross earnings) has been reached. Thereafter, the insurance premiums must be spent on other covers to increase the total EPI star rating.

One final point that must be reiterated. There is no substitute for quality financial advice that takes account of all the applicant's circumstances. In comparison, the EPI star rating should only be informative.

In summary, insurers must regain the trust of consumers and this requires us to think and act like the best retail brands.

We should seek to have an intimate understanding of our customers, supported by exhaustive product research and testing, so that the end proposition is an effective consumer driven solution that builds on a trusted insurance brand.

However, where we are today, we do not have consumers' trust and our message is often too complex to understand.

Therefore, the EPI could provide a useful guide to prioritise products and allow consumers to avoid the wrong ones. This has been shown to appeal to investors.

We do not reproduce Munich's idea because it comes to the conclusion that we want it to; we do so because it uses an objective system to assess product worth. It is wrong that an industry like the UK life and health protection industry cannot prioritise customer need. It is wrong that we allow our customers to run huge potential risk by not outlining these priorities and the Task Force believes this situation has to be addressed. In an era of Treating Customers fairly this is an imperative for the industry.

Annual industry claims survey

One other document that will provide reassurance to the public about the value of the product they are buying is an annual claims report. This should disclose claims rates by product; this is contentious and some companies are concerned about the consistency of claim definition adopted.

If the industry does want to prove its point about the value of protection we should strive to produce figures that show the public not only how high the rate of claims payment is but also the circumstances in which claims are paid. There is a huge amount of positive news to dispense about the way that the UK protection industry supports its customers and it is high time we communicated this.

Perhaps a start would be an annual report compiled by the Task Force, or the ABI, on claims paid. Some examples could be anonymised, but would be far more effective if claimants chose to reveal details of how having income protection has helped them. Every adviser who believes in IP tells us that case studies and real-life stories would make a huge difference to their sales, so it seems to be vital that we produce a document that outlines the high claims-paid rate. Ideally this should be by company but we realise that not all companies would feel that like was being compared with like. However, we could produce a percentage of claims paid figure by each waiting period to show the public how rarely claims are turned down. In fact anonymised studies of fraudulent claims would underline the point about why some claims are rejected. This publication is one that the Task Force could produce from figures supplied by its membership. This is nearly universal on individual IP, but if this might be felt by consumer organisations to be not independent enough, perhaps the ABI could produce it.

The industry would be spurred on to increase the percentages of claims paid; the adviser would be able to show real examples of how Income protection cover has saved families' financial futures and above all, the public would feel that they are likely to be treated fairly if they buy income protection. In an era of Treating Customers fairly this would be a great opportunity for the Income Protection industry to show that it does just that.

4 Payment protection insurance and income protection

In terms of the number of policies in force, around 20 million, payment protection insurance (PPI) in its various guises has been a spectacular success story. In terms of current image and the failures that have led to regulatory intervention, it faces huge challenges and the nature of the market is set to change following the Competition Commission's final report published on 29th January 2009.

This section explores how the best elements of PPI and IP might be combined to create a range of solutions that are attractive to, and meet the real needs of, UK consumers.

PPI and MPPI sales in the UK

Much of the in-force block of PPI has been written on a short-term basis, suggesting that a significant proportion of the £4.4billion already paid out by consumers is up for grabs in the future.

The significant economic problems since 2006 have meant there is significantly less borrowing so the market was set to shrink even before the actions taken by the Competition Commission. Nonetheless, market penetration of PPI was and remains very high compared with that of long term income protection providers.

In 1999 the government issued a challenge to the industry to increase mortgage payment protection insurance (MPPI) sales to 55% of new mortgages sold by 2004. Whilst this figure was never reached and was withdrawn after it was acknowledged to be inappropriate, a significant penetration rate was achieved, standing at 20% in May 2007 according to the CML.

Key market facts:

- In 2006 customers in the UK paid £4.4 billion in premiums to be covered by PPI policies
- Of the total economic profits of £1.4 billion, Personal Loan PPI contributed £645 million, Credit Card PPI contributed £336 million, and Mortgage PPI contributed £112 million. Other forms of PPI made up the remaining £273 million
- Nearly all Personal Loan PPI policies were paid for by a single premium but this will be banned in the new regime

Source: Competition Commission Provisional Findings Report 05/06/08

- Defaqto estimated that the average price per £100 of benefit for MPPI was £4.76, for CCPPI it was £11.70 and for PLPPI was it £18.23
- The claims ratio for MPPI is 33% compared to 19% for the wider PPI market. Of those claims that are made, 89% are successful.

Source: Response by the Council of Mortgage Lenders to the OFT Report on the Payment Protection Insurance Market Study 30/11/06

MPPI has provided valuable cover for many people. According to the Council of Mortgage Lenders, over one million households (1,007,714) have claimed on MPPI between 1998 and 2007, and these households may have otherwise fallen into arrears or lost their homes.

The largest providers of PPI include Lloyds TSB, HBOS, Barclays and RBSG and about 50% of the companies are vertically integrated i.e. they provide both the credit function and some or all of the underwriting of the PPI product.

The typical profile of PPI customers is that they are likely to earn less than the national average income or come from socio-economic groups C and D, although this varies considerably depending on the type of PPI bought. Obviously, there is potentially significant cross-over between MPPI and IP customers.

Some key questions generated by recent market events include:

- How interested will distributors be in selling anything if it means greater expense and lower rewards?
- What will be available for consumers as their short-term policies come up for renewal, and at what price?
- How will consumers be aware of what is available, whether they have previously been insured or not?
- How will they access all of the new products that could meet their needs?
- How will they steer a path through the confusion of choice that may be available and ensure that they get the right product for their needs?

The questions of distribution and advice are covered extensively in other sections of this White Paper.

To get an idea of the types of product that might be available, we have examined two products launched in 2008 and the considerable market research that drove their development.

1 LV= Mortgage & Lifestyle Protection

LV= launched their Mortgage & Lifestyle Protection (MLP) in May 2008, with the aim of providing a high quality alternative to MPPI or ASU, designed specifically for the needs of mortgage advisers and their customers.

LV= carried out research with both mortgage advisers and consumers in designing the product, including focus groups, telephone interviews and desk based research.

They found that with many mortgage advisers, the time dedicated to protection sales was less than in the wider intermediary market. As a result, products like MPPI and ASU tended to be popular and sell in high volumes, as they are quick and simple to apply for. This means many advisers were unlikely to consider more sophisticated, underwritten (and therefore time consuming) menu based plans.

A primary requirement of the product design was therefore to include a quote and submission process that would take no more than a few minutes.

In terms of designing a high quality MPPI replacement, LV= looked afresh at the real needs of mortgage customers, and the key issues with MPPI.

Addressing the issues with MPPI

Some of the key issues were identified and addressed as follows:

Traditional MPPI	Mortgage & Lifestyle Protection (MLP)
Only usually provides 12 or 24 months accident and sickness protection	Pays out until the client can return to work, no matter how long that takes (LV's experience is that incapacity claims last on average 7 years, with many lasting longer than this)
Premiums and contract can usually be changed by a provider with just 30 days notice. Contract can usually be cancelled with 90 days notice.	Guaranteed premiums for the whole of the contract (accident, sickness and unemployment). LV= cannot cancel the contract on the customer.
Only usually provides accident, sickness and unemployment cover to the end of the mortgage, not covering the period between the end of the mortgage and retirement.	Can provide mortgage payment cover and living expenses cover to independent terms, for example mortgage cover to the end of the mortgage and living expenses cover to retirement.
Usually only pays out on a 'suited' definition of incapacity.	Pays out on an own occupation definition of incapacity.
Often has standard exclusions or pre-existing conditions for accident and sickness.	No standard exclusions for accident and sickness.

In addition, MLP has optional unemployment cover of up to 36 months (12 months per claim), automatic waiver of premiums, flexibility and guaranteed insurability options, benefit up to £50k per year (considerably more than traditional MPPI), and free Healthy Steps online health assessment. The product is also available at any time (not just at the time of mortgage or remortgage), and is available to clients who rent.

Meeting the needs of mortgage advisers

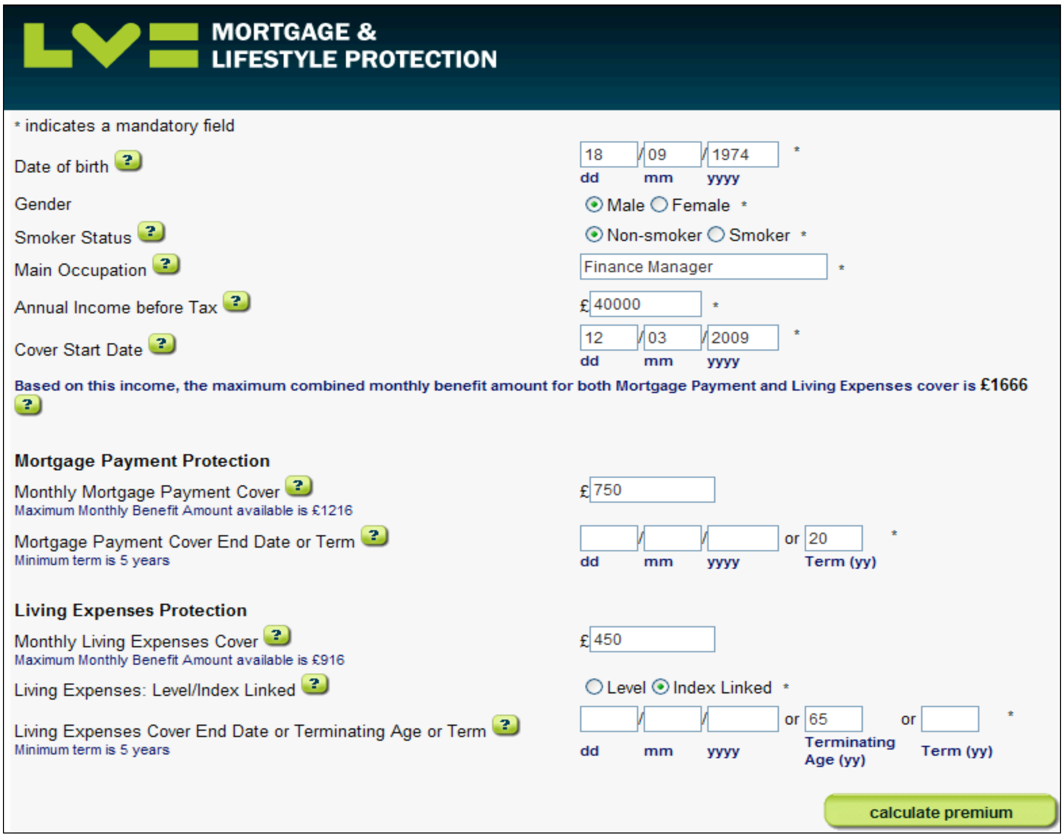
To make it possible to quote and submit in a few minutes, LV= have made MLP available online only, and tele-interview 100% of cases. This means that advisers only complete some basic details (see quote screen below), select the cover and premium that the customer wants, and then submit the case to LV= online with the client's phone number and time to call them.

The quote screen – minimal information is required from the adviser. Mortgage and living expenses cover can be set up independently to different terms, quickly and simply, providing a tailored solution for clients. See below.

In comparison to the annual commission from MPPI, LV= offer the option of upfront commission to advisers, with most cases paying £750 to £1000 commission since launch. This proved a popular option in research.

Research showed many advisers required support, with some selling little or no protection. LV= have therefore built a dedicated website www.lvmlp.co.uk and have included online interactive training to help advisers who are inexperienced in protection get started. They have also provided a marketing toolkit to help advisers revisit clients with no protection, or traditional MPPI, including a guide for beginners.

LV= believe the product will particularly appeal to clients 45 and under, in non-manual jobs and with no serious health issues. Cover is available to other clients, though premiums will reflect the risk of offering long term cover to riskier clients.



2 Fortis together with Lifesearch – Real Life Cover

Fortis, along with Lifesearch, also launched their new product in mid-2008 following extensive research. They concluded that while both traditional IP and MPPI work well for a few customer segments, the mass market needs something different.

The message received from the consumers that Fortis engaged with was that they:

- Worry about risks that are out of their control, with death as the biggest priority, followed by cancer, heart attack and stroke
- Don't think that they will suffer anything serious enough to keep them away from work, and if they did, it would not be for more than a few years
- Generally don't trust the insurance industry to pay out
- Want to avoid over-insurance and accept some self-insurance risk
- Find it easier to keep track of one product with one provider

In talking to financial advisers, Fortis also recognised that they needed to develop a simple proposition that was supported by streamlined underwriting and submission processes. As a result, they created e-business facilities with no automatic general practitioner reports (GPRs) or financial underwriting. There are just five decisions to make in order to get a quote:

- Sum assured - maximum £250,000

- Term of cover - maximum age 70
- Level cover or increasing by 5% pa
- Length of deferred period
- Whether to add optional unemployment and extended carer's cover

Their product solution was to create a single sum assured that could be used in different ways dependent on life events. Although there is no financial underwriting at outset, any over-insurance at claims stage is fed back into the pot so that the consumer does not feel cheated out of benefit that they have paid premiums for.

An analysis of the usual duration of existing IP claims in the market led to a benefit payment term of up to eight years. This does not cover every eventuality but reflects the consumer acceptance of some self-insured risk highlighted in the research with a corresponding improvement in affordability of premiums.

Real Life Cover - Differences

Product	Advantages	Disadvantages
Term	Adds much needed disability cover	More expensive
MPPI	Independent of the mortgage lender No PECs Guaranteed A&S premiums and conditions over mortgage term Benefits payable for up to 8 years Includes cancer, heart attack and stroke, plus carer's cover and recuperation benefits No IPT for A&S Unemployment cover guaranteed for policy year	Not suitable for class 4 lives More expensive for two of the following – Class 3 lives, females and ages >45 Speed of sale
ACCI	Safety net for all causes of occupational disability Multiple claims covered Easier to recognise CI conditions Benefit payable on life and death Lower cost	Limited CI coverage Lower CI benefits
IP	Presented as a lump sum Includes life cover and limited CI No financial underwriting at sale Manages over insurance	Benefit period could be more limited More expensive

In 2007 HSBC began to withdraw its PPI policies from sale and to offer its customers the chance to discuss their broader protection needs with one possible option being to take its LifeChoices product.

> 'My starting point is that the two 'markets' of PPI and IP are false and have only ever been maintained by intransigence on both sides. There is no fundamental difference that can be justified from a consumer perspective between short-term and long-term business other than some customers have a need either for immediate protection or only want cover against a liability that will cease after a specified period (eg a loan) whilst others need permanent cover.'
>
> Dennis Smith - Head of Life & Protection | HSBC BANK PLC

Further significant product development is also likely from all providers as the implications of welfare reform start to become apparent. This is discussed elsewhere in this White Paper.

One relevant finding for long term income protection providers in the Competition Commission's Final Report (29/01/09) is:

> 'The third barrier we found was the complexity of PPI policies. Variations in pricing structure (particularly, but not only, with respect to single-premium policies), policy terms and conditions, and the manner in which information is provided by firms, mean that the cost of PPI is not presented in such a way that it is easy to make comparisons, and this has a detrimental effect on consumers' ability to understand that information.'

This also applies to certain features of IP, such as the practice of quoting deferred periods in terms of days or weeks in some cases and months in others, and in the offsets included in benefit calculations for indemnity products.

This finding perhaps opens the way for the income protection industry to standardise these non-competitive aspects across each range of products targeted at different consumer groups to make comparisons easier for consumers and advisers. For example, a range of products targeted at consumers who are paid weekly could be standardised to quote deferred periods and other significant time periods in the policy in terms of weeks. The Task Force would support such a move.

The environment for any new products

The Competition Commission report will dramatically change the landscape within which any new products can be sold.

Since May 2005, consumer credit agreements (such as those applicable to a personal loan) have required the customer to sign the loan documentation twice, once to indicate agreement to the original amount of the loan and once to indicate agreement to the additional cost of the personal loan PPI associated with the loan.

The new findings will impose further obligations:

> (a) A prohibition on selling PPI at the credit point of sale. PPI cannot be sold by the distributor or intermediary arranging the credit (or any business covered by the prohibition, see paragraph 10.127) at the same time as the credit product,

nor within seven days of the conclusion of the credit sale period, or the provision of a personal PPI quote, if one were not provided during the credit sale period.

As a limited exception to this point-of-sale prohibition, the distributor or intermediary arranging the credit (or any business covered by the prohibition) may sell PPI to the consumer over the Internet or telephone 24 hours after conclusion of the credit sale period provided that the consumer has initiated the transaction and the consumer has confirmed that they have seen the personal PPI quote (paragraphs 10.34 to 10.156)

(b) Provision of a personal quote. We decided that all distributors and intermediaries who arrange credit for consumers must provide a personal PPI quote to the consumer in a durable medium (if the distributor or intermediary provides information about PPI to the consumer during the credit sale period). If the distributor or intermediary arranging the credit does not provide a personal PPI quote during the credit sale period, but subsequently contacts the consumer to offer PPI, a personal PPI quote must be provided at that time. Stand-alone providers and providers of short-term IP are required to provide a personal PPI quote to the consumer in a durable medium if the consumer asks the provider about the cost and/or features of a stand-alone PPI and/or short-term IP policy sold by that provider (paragraphs 10.157 to 10.181).

(c) Information provision in marketing materials. We decided to impose a requirement on all PPI providers prominently to disclose the following information in any PPI marketing materials that include pricing claims or cost information, any indication of the benefits of the PPI product or its main characteristics:

- the monthly cost of PPI per £100 of monthly benefit[3] (CCPPI and retail PPI providers must also show the cost of PPI per £100 of outstanding balance);

- that PPI is optional (stand-alone providers do not have to include this statement) and available from other providers (without specifying those other providers);

- and that information on PPI, alternative providers and other forms of protection can be found on the Financial Services Authority's (FSA) moneymadeclear website (paragraphs 10.182 to 10.222).

(d) Provision of information to third parties. We decided to require that all PPI providers must provide comparative data to the FSA, as specified by, and in the format requested by, the FSA. In addition to the information that the OFT may request from time to time for the purposes of monitoring and reviewing the operation of the remedies package, all PPI providers that meet a specified threshold (see paragraph 10.538) must provide the following information to the OFT on an annual basis:

- annual GWP, split by product type;

- distributor penetration rates, split by product type;

- and aggregate claims ratios for each provider, split by product type.

[3] If the benefit pays out for less than 12 months, notice of this fact must also be clearly disclosed to consumers alongside the cost of the policy.

In addition, all PPI providers must provide to any person on request, aggregate claims ratios, split by product type, for the previous year. These can be provided in the form of a range to be specified by the CC (paragraphs 10.223 to 10.242).

(e) Recommendation to use information for price comparison tables. We decided to make a recommendation to the FSA that it use the information provided to it pursuant to this remedies package to populate its PPI price comparison tables with data on all PPI and short-term IP products (paragraph 10.517).

(f) A prohibition on the selling of single-premium PPI policies. We decided that PPI cannot be charged on a single-premium basis. Subject to the prohibition on charging PPI on a single-premium basis, premiums can be charged monthly or annually. Where an annual premium is paid by a consumer, then a rebate must be paid to consumers on a pro-rata basis if the consumer terminates the policy during the year. No separate charges can be levied on a customer for administration or for the set-up or early termination of a PPI policy (paragraphs 10.243 to 10.277).

(g) A requirement to unbundle retail PPI from merchandise cover. Where distributors of retail PPI offer an insurance package containing PPI and merchandise cover, they must also offer, as a separate item, PPI cover alone (paragraphs 10.278 to 10.301).

(h) Annual statements. We decided to place a requirement on distributors, intermediaries and stand-alone providers to provide an annual statement for PPI customers (paragraph 10.302 to 10.332). Provision of this statement will be the responsibility of the company that sold the PPI policy to the consumer, other than for sales made by intermediaries where provision of this statement will be the responsibility of the underwriter or distributor or stand-alone provider with whom the consumer has an ongoing relationship.

> 10.302 We decided that an annual statement would raise consumer awareness of their ability to switch PPI provider. The annual statement should include information similar to that provided in a personal PPI quote to assist consumers to compare the cost of their PPI policy with alternative policies as well as information about consumers' rights to cancel the policy.

A sample of annual statement designs is provided in Appendix 10.2 of the report and is available via http://www.competition-commission.org.uk/rep_pub/reports/2009/542ppi.htm

Source: Competition Commission Final Report – 29/01/09

The major change for PPI providers is in the separation of sales of credit and the PPI product. These measures effectively level the playing field to some extent for sales of both PPI and IP products, but will this have a detrimental effect on the number of consumers who are covered under either form of policy?

The Competition Commission's own research stated that the most frequently cited reasons given by consumers for taking out PPI relate to 'peace of mind'. However, they stated that people are not aware of the existence of any form of cover until buying a credit product.

One barrier to entry for stand-alone PPI previously identified by the Competition Commission was high marketing costs compared to competitor PPI products. With the separation of sale of the credit product and the PPI product, all providers will be exposed to higher marketing costs to raise consumer awareness of and demand for the product.

The Competition Commission looked at the new short-term income protection entrants during the period of the investigation and concluded that they would not be able to compete with the point of sale of credit product offerings:

> '…there are significant difficulties associated with building sufficient scale to achieve a sustainable and profitable business without access to customers at the point of sale. '

In its final report, the Competition Commission has concluded that short-term IP is a form of PPI and is therefore subject to the same rules. This has implications for companies who have already developed stand-alone short term IP as an alternative to PPI.

Having said this, distributors and intermediaries are required to provide a personal PPI quote during sale of the credit product so, to some extent, this limits the impact of separating the actual sales.

Of the other remedies proposed, one implication of the concession that customers can pro-actively request the PPI product within 24hrs is that companies may start to offer incentives to prompt this.

How this is policed will depend on what is meant by 'pro-actively' e.g. if a loan provider passes on some information stating that a particular PPI product is available and that there is a price differential between taking it out in 24 hrs or waiting 7 days, will they have been deemed to be selling PPI at the time of the loan sale?

Reference is made to the FSA's website, www.moneymadeclear.fsa.gov.uk, as a source of information on alternative products. Under the heading "Protecting income or borrowing" this website contains a table listing various products that could be relevant, including various forms of PPI and income protection together with critical illness.

Whilst this is welcome, we would suggest that the contents and ordering of the table need some tweaking. For example, critical illness is the first product specified despite the fact that it is not designed to provide income replacement. Life insurance is only reached by scrolling down the page and long term income protection is not listed alongside MPPI or PPI and is in fact placed at the bottom of the hierarchy. We refer elsewhere to the Essential Protection Index which we believe is a more appropriate solution to establishing a hierarchy of consumer needs concerning protection.

There is no mention of the frequency of renewal required for any product, or the likelihood of being able to purchase future cover after making a claim, and no mention of one of the key benefits of income protection, the facility to make multiple claims during the life of the policy.

This suggests to us that the FSA has not thought through sufficiently the hierarchy of consumer needs or the way in which disability covers interact and the risks they cover. This is a very important omission and needs to be rectified as soon as possible.

There was also an earlier recommendation for the FSA to use the information provided to populate its PPI comparison tables. The Income Protection Task Force would recommend extending this to ensure that the FSA also directs consumers to ensure that they have the right type of product before entering any comparison tables.

This could be facilitated by the Money Guidance process:

http://www.fsa.gov.uk/financial_capability/our-work/money_guidance.shtml.

Consumers are asked to provide some key information before the tables are generated and we believe that the benefit payment term should feature in that key information, particularly in the case of mortgage protection. For unemployment cover, a benefit payment term of one year is standard and longer periods are not always available. For accident, sickness and disability cover, a period of not less than 5 years would be recommended by any professional adviser and it would be preferable to match the term of the mortgage repayments if that is affordable.

In many cases, consumers may be surprised at how affordable it is to obtain long-term cover that does not exclude certain causes of disability and that will match the term of mortgage repayments.

We would also like to see transparency in a number of other areas:

- **Industry claims payment ratios reported across product lines**, a key consumer concern identified by the Fortis research. We feel that the reporting of claims payment ratios across all product lines would assist the industry in general to re-establish consumer trust and to provide a benchmark for consumers to understand what constitutes a reasonable level. This should be accompanied by some commentary on the common reasons why claims are declined. The CC report requires claims ratios on PPI to be reported to the FSA and to any person on request and from the FSA's perspective, it does not make sense to restrict this only to one product line.

- **What happens after a claim is paid**, particularly whether cover ceases immediately and the availability of future cover once a claim has been made.

- **Exclusions** (we believe these are already scheduled for inclusion in the tables)

- **What services the insurer provides to assist claimants towards returning to work**.

Lastly, it would be good to move to a situation where consumers have a clear choice from the same distributor of whether they want long-term or short-term cover and are not directed to one or another according to a distributor agenda rather than their own needs.

In response to the original challenge to increase penetration of MPPI to 55% of new mortgage sales, four government departments (HM Treasury, DCLG, DWP and the FSA) worked closely with mortgage lenders and PPI insurers within the Partnership Steering Group (PSG). This met quarterly from 1999 and provided a standing forum in which issues of MPPI sales, effectiveness and competition were raised, researched and discussed. A revival of such government support and inclusion of the long-term market to consider all products that meet such a vital consumer need would be welcome.

The final requirement from the Competition Commission is for the provision of annual statements to consumers, something that has been identified as a potentially beneficial move in the long-term market. This could help to keep providers in touch with customers, remind them of the benefits they have purchased and provide opportunities for incremental sales relevant to any change in life circumstances.

The change in the market environment is not restricted to regulatory obligations. The credit crunch is biting and unemployment rates are soaring.

> ‘Lloyds TSB said it had seen unemployment claims made against loan PPI policies rise by more than 100% since January 2008 and had introduced a range of measures to support customers through the claims process.
>
> These include:
>
> - Increased flexibility in claims processes to account for individual circumstances
> - Monitoring of the external environment to identify high profile business distress and large scale redundancies - provision of immediate cash payments to those affected
> - Emergency claims surge team to handle significant call and claims volumes’
>
> Source: Insurance Age 12/12/08

Association of British Insurers (ABI) figures confirm that this level of increase is industry-wide with the release of research findings that the number of notified PPI unemployment claims, including PPI, MPPI and credit card PPI for November 2008 reached 19105, up 118 per cent on November 2007.

This rise in claims incidence and the cost of handling claims can only lead to increased premiums for unemployment cover at renewal of existing policies or for new policyholders. Historically, economic decline has also led to a rise in sickness and disability claims both in the form of welfare benefits and privately held insurance. To keep premiums affordable, cover may become more restricted, for example by excluding more causes of claim.

The recently announced changes to Mortgage Interest Relief support may have an influence on sales of MPPI. As from January 5th 2009, the waiting period is reduced from 39 to 13 weeks and the capital limit is increased from £100,000 to £200,000.

Other major developments that will have an influence in the longer term include the Retail Distribution Implementation Programme (RDIP) and welfare reform. It remains to be seen whether the implementation of welfare reform will have a positive or negative influence on consumer perception of the need for additional cover.

PPI deconstructed

Looking in more detail at the elements of a typical PPI policy that could be utilised in the construction of any hybrid offering, it is possible to isolate key elements of the cover.

PPI will typically cover either all, or a combination, of accident, sickness, involuntary unemployment and life. Some policies also offer cover for critical illness or hospitalisation. Various other options may be available such as a benefit for full-time carers.

A distinction is usually made between PPI as ‘short-term insurance’ and income protection as ‘long-term insurance’. When using the terms short and long-term, we need to be clear that we are talking about the premium payment period but for a consumer, the benefit payment period is equally, if not more, important.

Benefit periods are usually 12 months for unemployment cover and 12 months plus for disability cover up to the term of the loan but typically not more than 5 years and these can be hard to find. A search for basic Mortgage Payment Protection on www.moneysupermarket.com conducted on 02/01/2009 revealed no offers with a benefit payment period of more than 12 months and the term of the mortgage was not requested to generate the table!

There may be an exclusion period (also called qualifying or waiting period) of typically 60-90 days covering the time from inception of the policy to the time the policyholder is entitled to make a claim.

Excess or waiting periods (also known as deferred periods) for both disability and unemployment cover can be anything from 0 - 90 days from the date of occurrence of the claim event, with 60 days being typical for the cheaper covers, plus a further period covering the time it takes for the first benefit payment to be made, which under some policies is up to 30 days after the expiration of any excess period.

PPI is of course usually short-term renewable cover and once a major health event has occurred further cover is unlikely to be available.

Comparison of typical PPI and IP policies:

	PPI*	Long-term IP**
Risks covered	A, S & U	A&S only
Max. benefit payment term	12 months	Usual retirement age – selected at outset
Waiting period – A&S	28 days	Choice of 4,8,13,26, 52, 56, 104 and 112 weeks – selected at outset
Waiting period - U	28 days	N/A
Pre-existing condition exclusion period	First 12 months of cover	None
Exclusions	Fraud, War	Failure to follow medical advice
Additional benefits	Back to work service	Back to work service

[9]

It should be noted that some competing products vary considerably from the examples quoted. For example, many PPI policies impose an additional restriction on benefit payment term if the cause of claim is back pain or stress-related illness.

An attempt was made to compare prices between typical policies to get an idea of the benefits a consumer could expect to achieve in exchange for say, £50 per month. It proved to be impossible to produce a meaningful price comparison using the various quotation tools that are available online.

[9] * Product name: Paymentcare (ASU) – Abbey (obtained via FSA Payment Protection Tables January 2009)
** Norwich Union Income Protection Solutions (January 2009)

Commenting on the difficulties of advising consumers correctly, Roy McLoughlin of Master Adviser IFA Ltd said:

> "One of the stumbling blocks for consumers with income protection is obtaining accurate quotations. The comparison web-sites available to IFAs are not always entirely accurate and we tend to end up ringing the insurance company for an accurate quote. We often advise income protection as part of a multi-sale and there does not exist any accurate site for obtaining precise figures so the process can be a long and drawn out event. If this is the case for IFAs one can only imagine the problems that consumers who do not seek advice have."

Exclusions vary between PPI policies. However, as a general rule, if the cause of the claimable event is deemed to have been within the control of, or known to, the customer at the time of purchasing the insurance, the customer will not be able to claim against the policy.

The obvious failing in typical income protection policies is the lack of unemployment cover, which is likely to be at the top of most consumers' agenda in the current climate. Some of the newer policies have addressed this within the same product structure. An alternative is a strategic alliance with an underwriter of unemployment cover.

Whatever combination of features is tweaked and amalgamated to create new products, it must be remembered that a range of solutions will be needed for different segments of the market. There is no 'one size fits all' solution and consumers will need guidance, in whatever form that may take, towards products that meet their needs.

Underwriting and claims

Apart from the challenges attached to awareness and distribution of any new products, there are significant challenges in underwriting and claims handling, with simplicity and transparency being key.

PPI policies are not underwritten on an individual basis; many companies charge the same premium to all customers for the same cover, though some do charge varying premiums according to, for example, age. Pre-existing condition exclusions apply for the disability and other health related elements of the product.

The Competition Commission reported that 'underwriters appear to be making reasonable, but not excessive, rates of return on PPI business. This suggested to us that underwriters were unable to exert a significant degree of market power.'

Much of the risk selection attached to PPI is achieved through underwriting of the loan and the customer's risk factors for default, such as employment status. Monitoring of exposure to particular customer segments is an important control measure. In fact, for mortgage-related protection, a lot of the information needed for insurance underwriting purposes is collected as part of the loan application process and this could contribute to much-needed simplification of the underwriting process for both short and long-term products.

The personal approach of tele-interviewing and tele-underwriting lends itself perfectly to assessing the complex risks involved in any form of income protection insurance. This takes much of the sensitive information-gathering away from the adviser and puts it in the hands of professionals who, when it is done well, inspire confidence in applicants and are able to generate quick and accurate decisions so that cover can commence without delay.

Any development in underwriting that creates the perception of simplification for customers, however complex the processes are behind the scenes, is to be welcomed in removing one of the barriers that is often cited by advisers to writing this form of protection cover.

The Competition Commission found that between 11 and 28 per cent of GWP is paid out in claims, depending on the product. In the event that claims levels are less than expected, the resulting profit is generally split between the underwriter and distributor according to an agreed profit share percentage; typically 90 to 100 per cent in favour of the distributor. The existence of profit-sharing arrangements between lenders and PPI providers may have a considerable influence on claims philosophy.

It is understandable that insurance is not always at the forefront of a customer's mind and many people do not remember that they have cover even after a claimable event occurs. The extent to which providers take steps to encourage customers to make a formal claim when they become aware of a claimable event can vary.

The claims handling process for PPI has many similarities to that of IP insurers, with common use of telephone screening for notification and initial phases of the claim, followed by the completion of forms by the claimant and the doctor, former employer or other relevant parties.

Most companies also offer 'back to work' support and help with understanding entitlement to State benefits. This extends not only to medical rehabilitation, which is common among IP insurers, but also to help with job search and CV writing, reflecting the inclusion of Unemployment cover. For example, Cardif Pinnacle offer a sophisticated claims approach that can include workshops with a specialist Human Resources Manager for groups of claimants living in the same area.

Many of the leading PPI providers also routinely share information using the HUNTER anti-fraud system, which looks for matching information from claims records to highlight cases requiring further investigation e.g. two customers claiming from the same address.

These investigation and rehabilitation efforts have proven to be worthwhile even with short benefit payment periods. In the light of welfare reform, perhaps there is an opportunity to review the whole area of rehabilitation provision funded by insurers. This needs to dovetail with the new State provision and to separate funding from other claims expenses to facilitate detailed monitoring of the effectiveness of each claims handling intervention used.

If the marketing message for new products is focused more on return to work, it may even be that customers would be prepared to pay a small amount extra to increase their access to rehabilitation services and this could become a differentiating feature of the product itself.

A kitemarked IP/PPI product?

In terms of developing the market, much will depend on whether the product provider and distributor are one and the same entity or separate entities with different agendas and regulatory supervision. Some broad options include:

- The status quo where PPI and IP are developed and distributed by different branches of the insurance industry
- Hybrid products combining elements of both PPI and IP
- Strategic alliances between both providers and distributors of PPI and IP

- A staggered approach involving a simple initial sale of a very basic product with options and incentives to upgrade over time, similar to the incremental approach used successfully by Homeserve for utility-related insurance

Some lessons can be learned regardless of which approach prevails. Speaking in Money Marketing (3rd February), CBK Colchester principle Peter Chadborn said:

> "In truth, when it comes to income protection, some providers have been steadying the ship just when the boat needing rocking. While PPI policies have many exclusions and are far from flexible, it might be worth introducing the simplicity of the PPI application into the income protection market. The simplicity of the PPI application process is a factor which contributes to the fact that PPI sales outweigh income protection to the extent that they do. The ease of the process has got to be something which income protection providers can learn from."

What could a hybrid product look like? From a customer's perspective, the ideal requirements would need to include:

- A, S and U cover for a minimum benefit period of 12 months
- Provision for longer term A and S cover at least up to the term of any loan repayments
- Term of policy that matches term of loan repayments
- Certainty of payment for any risk that is outside the policyholder's control i.e. all causes of sickness and accident covered in the standard terms
- Certainty over the level of benefit to be paid
- Certainty and transparency over the criteria required for a valid claim to be paid e.g. the test of disability
- Choice of start date for payments to coincide with other private or employer-sponsored provisions that the policyholder has in place
- Facility to make multiple short term claims during the life of the policy without penalty
- Practical support for returning to a productive life

In line with the successful use of financial incentives for a return to work within the welfare system via the Pathways to Work initiative, perhaps now is also the time to consider such a move in insurance product development.

One or more of these fundamentals could be modified to increase affordability with up-front agreement from the policyholder.

From the provider's perspective, some risk selection would be required and modifications could be made to the basic terms to increase the range of customers that could access the product. Can this be achieved via a different balance between risk-based pricing and underwriting than is currently typical?

Although an insurance sale cannot be made during the sale of a credit product, this does not preclude the capturing of relevant customer data that could be used in a subsequent insurance application process.

Attempts have been made in the past to combine the sale of a PPI-style product together with a long-term product that provides a more comprehensive safety net in the event of severe long-term incapacity. Anecdotal experience suggests that this is still considered too complex a sale for the current distribution model, where the belief is that income protection alone is difficult to sell without adding further complexity in the form of a short-term precursor to the long-term product.

However, if the sales issues could be resolved, some gains could be made in reducing the complexity of underwriting as the short-term product can effectively act as a waiting period for the long-term product.

Integrated claims handling can also bring some benefits to claims experience and may bring operational synergies depending on the structure of the company or companies involved in delivering such a solution.

Assuming that new products will be developed and available and demand will be generated, how will consumers know whether a product meets their needs or not? In an ideal world, everyone would have access to a professional adviser, but we do not live in an ideal world.

The Task Force would suggest some form of kitemark system, perhaps under the auspices of the Money Guidance process, which covers policies of all types, whether sold in the short or long-term markets.

The key elements of the system would need to be:

- Simplicity
- A minimum standard for each of the key product features
- A measure of value for money in terms of available annual benefit versus total annual premiums and perhaps including a cap on the margins extracted by distributors
- A measure of claims payment standards

The Association of British Insurers and the Council of Mortgage Lenders have already produced a Baseline Cover Specification for MPPI, which outlines the minimum cover that should be offered. This could be reviewed, enhanced where applicable and consideration given to how it will be policed.

Companies would have the opportunity to exceed the kitemark and to highlight how they do this in their marketing material.

On its own this would not solve the issue of customers being able to source products that are appropriate for their needs. In addition, some supporting materials would be required, such as:

- Step by step guidance through the key features consumers need to consider when choosing a product
- Availability of this guidance on all relevant websites, particularly those that are not partisan to one form of insurance or another, such as the ABI, the FSA general consumer pages and www.moneymadeclear.com
- A single point of entry to all forms of IP, PPI or hybrid products so that the consumer can make a choice of the type of product that best suits them.

5 Group income protection

Political and economic background

In common with employee benefits generally, the marketing and design of group income protection products will often be substantially influenced by both Government strategy and the economy. As far as the economy is concerned, the situation is grim. Britain has officially entered recession for the first time since 1991. We have not only entered recession, but the economy is shrinking at its fastest pace in nearly three decades, and at time of writing the flow of credit to the economy remains frozen. For many employers, getting costs under control is going to be critical and employee benefit programmes will no doubt be closely examined with regard to their relevance and whether they constitute value for money, a point that will be returned to later in this paper.

Despite the economic difficulties, however, the Government has decided to press on with key reforms regarding workforce health, and these will result in a number of far-reaching new initiatives.

When considering the health of the working population, there have been a number of overarching themes in Government thinking. These have included:

- The need for strategies that aim to ensure that no one is 'written off'[10] as a result of illness or disability, and that people should not 'languish on benefits'
- The belief that work itself can play a significant role in contributing to a person's mental and physical wellbeing and that 'a healthy workforce is a happier more productive workforce'
- That individuals themselves have a key role to play in striving for better health, and in personally engaging in initiatives designed to return them to work. This is linked to the concept and practice of 'conditionality' – placing greater responsibility on claimants to seek work as a prerequisite for payment of benefit, and deepening the obligation to work
- That employers should develop and maintain sustainable business practices that encourage people with health conditions to either return to work or become employed for the first time
- A need to devolve power locally and work in partnership with others – for the Government 'to carry on working with everyone who has an interest in improving the health and well-being of the working-age population to ensure that we are all doing all we can to support disabled people and people with health conditions to fulfil their potential in work'[11].

These themes have in some cases informed legislation and in others prompted the commissioning of a number of specialist reviews by both the Department of Health and the Department for Work and Pensions.

[10] 'No one written off: Reforming welfare to reward responsibility'. DWP July 2008
[11] 'Improving health and work: Changing lives. The Government's response to Dame Carol Black's review of the health of Britain's working age population' DWP and DH November 2008

The Welfare Reform Act came into force in October 2008 in order to support some of the above aspirations along with the Government's aim of reducing the number of people claiming incapacity benefits by one million by 2015. Included in its measures were radical changes to incapacity benefits, compulsory work-focused interviews for people assessed as being able to undertake work, and the offering of appropriate assistance to help them in this endeavour.

Research undertaken in 2007 suggested that these changes were seen as 'broadly positive and an opportunity for intermediaries to approach and communicate with employers, along with positioning income protection more positively as access to state benefits becomes increasingly difficult'.[12]

This optimism was, however, hedged with concern about employers' general reluctance to invest in new benefits, a concern that has probably increased given the deterioration in the economic environment since the research was conducted.

Although not directly linked to the Government's health and welfare strategy, the 2006 Employment Equality (Age) Regulations,[13] which implemented the European Employment Directive,[14] did have a less than benign influence on group income protection marketing. A survey conducted in 2007 among 130 employers indicated that more than half of them believed that the Regulations were making the provision of risk benefits less sustainable.

The main concern, identified by approximately 60 per cent of respondents, was the increased cost of providing income protection insurance as a result of having to extend cover to normal retirement age´. One in three companies were not satisfied with their income protection element. The two main reasons cited were the increasing cost of the insurance and the length of time that an individual remained on the payroll. There is some evidence to suggest, however, that scheme closures so far have been predominantly by small firms.[15]

A key influence on government policy on health was Dame Carol Black's Review of the health of Britain's working age population, published in March 2008.[16] In the report Dame Carol stresses that recent evidence suggested that work can be good for health, but that 'much of the current approach to the treatment of people of working age, including the sickness certification process, reflects an assumption that illness is incompatible with being in work'. One of the principles at the heart of her new vision for health and work will be familiar to income protection insurers: 'early intervention for those who develop a health condition'. In going on to discuss the benefits of employer investment in health she states as follows: 'A business-led health and well-being consultancy service would offer tailored advice and support as well as access to occupational health support, especially important for smaller organisations ….. ' She also expressed concern about the challenges faced by occupational health as currently configured, including a diminishing workforce and the lack of good quality data.

[12] Group Watch Report, Swiss Re 2007
[13] The Employment Equality (Age) Regulations (SI 2006/1031) as amended by SI 2006/2408 and 2006/2931
[14] Council Directive 2000/78/EC of 27 November 2000 establishing a general framework for equal treatment in employment
[15] Research by Watson Wyatt and the CBI/Pertemps Employment trends survey 2007 cited in 'Age Discrimination in financial services : final report of the H.M. Treasury Experts 'Working Group' October 2008
[16] Dame Carol Black's Review of the health of Britain's working age population : 'working for a healthier tomorrow' March 2008 for the Departments of Health and Work and Pensions

In November 2008 the Government responded to Dame Carol Black's Review with their report 'improving health and work: changing lives'.[17]

The report outlined three key aspirations and associated plans:

- *Creating new perspectives on health and work*: these will include the replacement of the current medical certificate with an electronic 'fit note'; an education programme for GPs covering health and work issues; the appointment of local Health, Work and Wellbeing co-ordinators and the foundation of a National Centre for Working-Age Health and Well-being.

- *Improving work and workplaces:* Initiatives include a business health check tool to help businesses quantify the value of health-related investment; a National Strategy for Mental Health and Employment and an occupational health helpline for smaller businesses.

- *Supporting people to work:* Piloting early intervention services from 2009 until at least 2011 and making changes to Access to Work to improve its effectiveness.

The Freud Report (March 2007)[18] made recommendations regarding the design of welfare to work policy and the delivery and devolution of welfare (Freud has now joined the Conservative front bench in the Lords as Shadow Minister for Welfare Reform).

Another independent report by Professor Paul Gregg (December 2008)[19] considered a single personalised conditionality support regime, along with the role of sanctions. Many of the recommendations in these reports found their way into the Department for Work and Pensions White Paper *'Raising Expectations and increasing support: reforming welfare for the future*'.[20] Published in December 2008, it 'is based on a simple idea: that no one should be left behind, that virtually everyone should be required to take up the support that we know helps people to overcome barriers to work'.

The White Paper proposes:

- *A simpler benefits system*, for example considering a model whereby there is a single benefit for income replacement with 'extra costs' met through other payments

- *The devolution of power to private, voluntary and public providers* – for example, moving to an 'Invest to Save' approach which would involve private and voluntary providers investing up front in getting more people back to work, and being paid out of the resulting benefit savings

- *Personalised conditionality* – based on a 'clear bargain that almost everyone on benefits would be expected to take active steps towards work, but where those expectations are based on an individual's needs and circumstances'

- *Enhancing support and control for disabled people*, including a determination to make sure employers do not discriminate against people who are sick or disabled. The budget for Access to Work will be doubled, which helps employers meet the extra cost of employing a disabled person

[17] ibid
[18] The Freud Report: 'Reducing dependency, increasing opportunity: options for the future of welfare to work' March 2007 - DWP
[19] 'Realising Potential : a vision for personalised conditionality and support' December 2008 - DWP
[20] 'Raising expectations and increasing support : reforming welfare for the future' December 2008 - DWP

Readers of this paper will not need reminding that for many employers the current economic climate and outlook is grim and uncertain. As far as welfare reform is concerned, however, the following quotation from James Purnell sums up the Government position:

> ‘Some people say we should slow down welfare reform because we are entering a recession. The Government believes that we should do the opposite – we should increase the pace, because that means offering more support to people and matching it with the expectation that they should not fall out of touch with the world of work’.

Group income protection market development – from insurance to health risk management

There is now a remarkable potential synergy between government policy on workforce health and the way that group income protection arrangements function.

In recent years the basic income protection insurance model has developed into a more sophisticated health risk management tool that employers can utilise to help reduce the range of risks associated with long-term sickness absence. These valuable additional services (such as rehabilitation advice) are often available from insurers at little or no extra cost and recent research into their importance and usefulness is cited later in this report. It is true to say, however, that not all group income protection plans have access to such services. Their availability will sometimes depend upon the number of employees in the plan or whether the insurer believes that the results obtained will be cost effective.

What has happened, therefore, is that the ‘conventional’ transactional insurer/insured relationship has developed into a more ‘partnership-based’ model with clients, advisers and insurers working collaboratively to solve employee health related issues in an environment of enlightened mutual interest. A major objective has become the desire to create a framework that will facilitate an employee’s’ early, safe and effective return to work.

Advisers and insurers already recommend that employers behave in a fashion that is very much in line with government thinking on how health issues in the workplace should be managed.

Critical amongst these recommendations have been:

Persuading employers that it can make good business sense to invest in health: For example, emphasising that both the employer and the employee benefit from maintaining the employment relationship once an employee has developed job-specific skills. After investment in training has been made if an employee leaves or is absent long term due to sickness or disability the employer will lose this benefit. Employers may also incur other indirect costs including the cost of new recruitment, training, overtime, deterioration in customer service relationships and possible morale problems.

Promoting the positive relationship between work and personal wellbeing and persuading employers of its importance: As various Government statements have emphasised, there are significant personal losses for people who are unable to get back into work, apart from the financial implications. It has long been accepted that work is important in many ways to a person’s psychological well being, bringing as it often does personal satisfaction, status, recognition and a supportive social network. Being deprived of these aspects of life can have a very serious impact on health and contributes to the recognised fact that likelihood of return to work diminishes with the length of absence.

A recognition of the importance of the biopsychosocial model in returning people to work: This model has played a major role in Government thinking with regard to how incapacity benefit claimants can be helped to return to work. Employers are made aware of the fact that frequently the condition that prompts absence initially is no longer the condition that is keeping someone from going back to work. The biopsychosocial model recognises that the employee's health condition is only one of the factors that must be taken into account in their rehabilitation.

Equally important can be their attitudes and beliefs as well as the policies and practices of the organisation where they are employed, and there is strong evidence that symptoms and disability are shaped by psychological factors and the medical advice people have received. Insurers can also provide an important service by acting as a link between the employer and the employee. Keeping in regular contact with the workplace has consistently been identified as a major factor for improving the likelihood of return to work. Also, the insurer (or the adviser) can be a detached and unbiased player in the return to work process, which is particularly important if there are other sensitive issues associated with the absence (for example, if an injury was sustained whilst the individual was at work).

Early intervention and concentrating on ability rather than disability: Advisers and insurers emphasise to clients that getting alongside the employee early when it first appears that they may be absent for a significant time (or have a serious condition that might eventually have that effect) is of critical importance.

Using tools such as vocational rehabilitation plans insurers help in identifying the gaps between what someone can do and what their job requires them to do, along with identifying barriers that may prevent someone from returning to work. In this 'case management' approach, the key is in identifying capacity rather than incapacity, and to customise the services and professional help to each individual's needs.

Research indicates[21] that the main reasons for long-term absence remain stress, mental ill health (e.g. clinical depression and anxiety) and musculo-skeletal injuries (e.g. back pain, neck strains and RSI). There is significant evidence to show that many people suffering from these conditions can be helped more effectively by early and appropriate treatment. It is true to say, however, that some insurers have invested more in rehabilitation services than others.

Helping employers and employees get access to the right care and advice: Dame Carol Black's review specifically alluded to a shortage of suitably qualified occupational health support. Insurers have considerable in-house medical expertise along with established networks of doctors and specialists. Help can be offered, for example, to people diagnosed or suffering from complex or serious conditions by reviewing their diagnosis and recommended treatment plans. Some insurers also offer access to stress counselling and useful help lines where appropriate. Insurers and advisers often work collaboratively with the employers' own Occupational Health advisers to formulate rehabilitation plans and 'back to work' strategies, and research has shown this to be a highly valued and valuable service.

Helping to eliminate discrimination: Employers already have a duty under disability discrimination law to make reasonable adjustments in order to help a disabled person

[21] CIPD research into absence management policy and practice in the UK – 2008 Report

remain in work, and to ensure that discrimination does not take place as a result of recruitment practices. Avoiding problems and litigation requires a combination of robust processes and the deployment of suitable expertise. Many of the services offered by

insurers (for example vocational rehabilitation and access to cognitive behavioural therapy) can and do play an important part in keeping people with a disability in work.

Helping people with mental health problems: approximately 40% of people claiming incapacity benefits have mental health problems that prevent their return to work. This situation has been exacerbated by the stigma often associated with mental illness and the reluctance of some employers to recruit people with disabilities of this nature. For many years insurers have endeavoured to help employers and employees to manage mental health issues in the workplace. Initiatives have included the use of the biopsychosocial approach and the deployment of support such as cognitive behavioural therapy.

Product design and service standards

Advisers have consistently asked insurers to be more innovative in product design and responsive to employers' needs, and recent years have seen the development of many new propositions. There is, however, still a feeling among some advisers that more needs to be done.

New design features introduced in recent years have included:

- Access to employee assistance programmes
- Absence management services
- Limited term payment arrangements
- Fast track access to cognitive behavioural therapy
- Financial incentives to encourage early intervention
- Direct payment of benefits to claimants
- Support packages and help lines for employers
- Absence management assessment services
- More streamlined underwriting procedures
- Dedicated internet portals for advisers

This is by no means a comprehensive list, but does give some indication of the work that has gone into insurers' attempts to meet the changing needs of the market. It is probably true to say that additional services and insurers have also introduced product features as a means of market differentiation. Design enhancements do not, of themselves, necessarily translate into perceived added value in the eyes of clients.

Although of considerable value in certain circumstances (particularly, for example, those that mitigate the risk of mental health related claims) it is disappointing to see that, despite these new developments, the number of lives covered has not significantly increased. Conversely, of course, it could be argued that product and service innovation has helped to maintain the persistency of business and contributed to stabilising the market. Firm evidence for either argument is hard to come by and the answer is probably a combination of both.

There has been increased interest in recent years in plans under which benefit payment periods are limited to two, three or five years – sometimes incorporating a lump sum payment at the end of the period. There is a link here between group income protection product development and the continuing closure to new entrants of final salary pension schemes in the private sector, with the possible alignment of the insurance with new defined contribution arrangements.

No industry wide figures are available as to whether this interest has translated into significant volumes of new business, but hopefully this may be picked up in future research. As far as employees are concerned, the demise of final salary pension schemes potentially leaves them more financially vulnerable if they become unable to work due to illness or injury. This presents marketing opportunities for individual income protection plans through either flexible benefit plans or voluntary schemes.

One important aspect of the arrival of new product features has been the way in which they have added to insurers' databases information as to what interventions are most effective. One insurer, for example, has experienced encouraging results from its use of cognitive behavioural therapy as an intervention in cases of stress-related illness. Fifty eight per cent of claimants receiving CBT have been successfully reintegrated into the workplace in a matter of months.[22]

Insurer service delivery has come in for criticism from advisers in recent years, with particular focus on the speed of response for new quotations and for figures at renewal. This was partly attributed to merger activity, to work backlogs among some of the major players and also 'creaking' legacy systems. Articles in industry journals over the past year have made reference to a number of attempts by insurers to get these problems resolved, for example the creation of e-business portals and simplified underwriting processes.

No formal research among advisers was conducted for inclusion in this White Paper, and so it would not be appropriate to comment on whether service levels have improved to a level that advisers are happy with. However, as the recession brings increased demand for all providers of services to justify their importance to customers, it is imperative that insurers aim for the best possible standards of timeliness and accuracy.

Market size

There was a small decline, in the number of lives covered between 2006 and 2007. The following statistics and comments have been drawn from Group Watch 2008,[23] Swiss Re's report on in-force and new income protection business in the UK.

Overall, in 2007, in-force market premiums for group income protection totalled £641 million (£612 million in 2006), an increase of 4.7% over the corresponding figure in 2006.

The number of lives covered was reported as 1,723,961 (1,731,138 in 2006).

In force annual benefits were reported as £41,041,854,872 (£38,543,557,755 in 2006). The slower growth in premiums compared with benefits per annum reflects more

[22] Legal & General figures
[23] Group Watch Report Swiss Re 2008

competitive pricing, together with a very small move towards switching cover to a limited benefit term to reduce costs. Although generalisation can be dangerous, this would appear to have more than balanced increases in the market where benefit expiry dates have been extended to address age discrimination issues.

The report went on to consider flexible benefits. Total in-force income protection premiums written on this basis in 2006 and 2007 were £22,509,827 and £22,888,799 respectively. Overall, flexible income protection premiums increased by 1.7%, perhaps indicative of the relative complexity and lesser availability of income protection in flex arrangements and of the potential age discrimination difficulties as well as the greater appeal to employees of lump sum payments.

Group income protection is a specialist market in which, during 2007, the top five players wrote 90% of the business (92% measured by numbers of schemes). A new player, Zurich, has entered the market in early 2009, with the reported intention of being a top five player in the group risk sector generally by 2012.[24]

Data for the size of the market in 2008 are not yet available but the Swiss Re Group Watch Report will probably be published in late April 2009. Anecdotal evidence suggests that, even though the number of lives covered may not vary very much when the 2008 figures are finally revealed, there may be some reduction in scheme numbers. Smaller companies in particular, for example, may be reacting to the economic climate by reducing their spend on benefits generally.

Prospects for 2009/2010

About half the people who enjoy income protection cover do so under group income protection plans and, of course, whether they (and their dependants) will continue to benefit from this cover will depend upon their employer's view of the plan's cost effectiveness.

There are a number of scenarios that will affect whether one takes an optimistic or pessimistic view of the future:

Will employers who are looking to reduce costs see removing group income protection as a relatively straightforward, easy quick 'win' to save money?

The answer to this will depend on a number of factors.

If the benefit is embedded in contracts of employment it may be more difficult to remove, and considering its removal will bring into the spotlight what promises have been made to employees with regard to how they will be treated if they are unable to work. Will employers be prepared to take on the funding of the promise themselves or prefer to remove the commitment altogether? Obviously there is a need for advice here, both from their benefits adviser and their employment lawyer.

Has there been a clear demonstration of the plan benefits? There may have been satisfactory experience of claim settlement, or the effective utilisation of the insurer's early intervention or rehabilitation service. This may improve the likelihood of the plan being retained.

[24] Health Insurance Magazine – 5 December 2008

Does the plan form an integral and important part of the employer's overall strategy for workforce health? For example, in the 2007 Watson Wyatt Risk Benefit Survey 22% of respondents cited insurers' 'claims management capabilities' as being very important with 71% reporting that the service was 'good to excellent'. By far the most important and valuable part of the service was the interaction of the insurer with the employer's own occupational health services (cited by 50% of respondents). Other popular services were nurse visits to claimants and rehabilitation services.[25]

Notwithstanding the above, attrition of existing scheme membership may be the case as redundancies take place and as employers seek to reduce benefit costs. Income protection can be an 'invisible' benefit to many employees and not very high among employers' agendas when they consider the importance of benefits in relation to their business needs. Removing or reducing it as a benefit may not create as much workforce discontent as, for example, amending or removing the private medical insurance scheme. For employers who are looking to reduce the cost of core benefits, there is also the option to reduce the benefit level and allow employees to exercise options under their flexible benefit plan to use their fund to 'top up' benefits to previous levels.

Will the alignment of government thinking with the health insurer risk management approach create business opportunities?

From the point of view of marketing, it is important and positive that the government model for creating and maintaining a healthy and diverse workforce is aligned so well with the health risk strategies put forward by insurers and advisers.

Some of the opportunities that may now present themselves are as follows:

- Working with government and appropriate regional bodies on the various pilot programmes that will be coming on stream over the next few years. Group income protection insurers hold valuable data on workforce health and also employ people with significant expertise in the management of health-related risk. Participating in pilot programmes (which will often be locally organised) is a rich opportunity to take the message of the positive nature of insurance to a much wider audience. Insurers may be able to play a significant role in the National Centre for Working-Age Health and Well-being. The Centre's functions are going to include the gathering and analysis of data enabling the identification and monitoring of trends to help in determining the impact of interventions and initiatives.

- In her review, Dame Carol Black expressed concern about the shortage of suitably qualified and experienced occupational health professionals. Insurers may consider tendering for some of the work that may be occupational health related and work alongside, for example, GP practices, primary care trusts, or existing contractors to deliver these services. The helpline that is planned for small firms may be an opportunity, along with the further development of NHS Plus and its services to small to medium sized enterprises.

- Perhaps there is an opportunity now to break away further from a conventional insurance based approach with the establishment of local health funds, managed by insurers but funded by employers (with government help). Are there possibilities for founding collaborative local ventures whereby a large local employer (or an alliance of numerous smaller employers), GPs, a primary care trust and an insurer work together to help people stay in work? Can similar

[25] Watson Wyatt : 2007 Risk Benefit Survey Report

- initiatives be put in place for employers in the public sector who want more help to address long-term absence, and who will be under particular pressure from government to participate in strategies that will return to the workplace people with health conditions (whether or not they are benefit claimants).

- One of the concerns expressed by Dame Carol Black, and other government advisers, has been with regard to small to medium sized enterprises (SMEs) and how they access the most appropriate services. Given the fact that most enterprises operating in the UK fall into this category, they have long been a target for advisers and group income protection insurers, but with fairly mixed results. Perhaps the time has now come to consider again how these potential customers can be accessed, particularly in view of the disproportionate effect the long-term absence of a key employee has on a small business, and their statutory duties under health and safety and disability discrimination legislation.

- There are obstacles to be overcome: the current economic climate, the need to persuade small businesses that a group income protection plan should be a priority at all, and issues around the need for underwriting and concern about anti-selection. Despite current worries, however, this may be a good time to do some future planning. One idea for consideration may be the prospect of a group income protection, which is available to all organisations, of say up to 50 employees, within a specified geographical area. The plan may be linked to other segmentation features apart from geography, such as commonality of occupations or to the availability of services, such as NHS Plus and its focus on Occupational Health support for SMEs. If an accurate risk profile can be established of the types of occupation to be covered, and the support that can be utilised to get people back to work, then maybe insurers will be able to feel confident enough to offer a more simplified approach to underwriting and possibly the granting of free cover for smaller groups than at present. This idea of a 'default' scheme that employers could subscribe to may possibly be developed alongside some of the pilot projects that are planned by government over the next few years and that are linked to the SME sector.

- As part of Dame Carol Black's Review, analyses were commissioned to help build the necessary evidence base and, as part of this exercise, PricewaterhouseCoopers (PwC) were commissioned to consider the wider business case and specifically the economic case for employers to invest in wellness programmes for their staff. Their report, 'Building the case for wellness' (4 February 2008), states that the evidence they have examined supports the idea that wellness programmes have a positive impact on intermediate and bottom-line benefits such as reduced sickness absence. Insurers have in the past been wary of investing in wellness programmes (for example, health promotion) because the rewards may often be slow to materialise. In the meantime, they may be vulnerable to losing clients as a result of market reviews at the end of rate guarantee periods where price has become the primary criterion for provider selection. If the potential overall benefits to the business through wellness initiatives can be demonstrated with clearer evidence (such as that available in the PwC report) perhaps longer business partnerships can be developed that will be judged on service quality and performance rather than simply price. The Government may be able to help here by offering tax incentives for accredited health management systems that support the range of health-related objectives they have outlined in their Health and Welfare policy statements.

Conclusions

In difficult economic times employee benefits come under rigorous scrutiny, and group income protection insurance is no exception. A top priority for many employers during the next few years will be to ensure the survival, and hopefully the development, of their business and a case will have to be continuously made for any expenditure. If the group income protection product that they bought has continued to deliver in line with expectations (whether simply by paying claims or by helping manage health-related risk) it may still be seen as a critical business asset that should not be disposed of too readily.

Even if that is the case, however, price will play an important part in the decision – so there may well be a significant increase in market reviews, with all the extra work that this will entail for both advisors and insurers. Advisers will be looking to insurers to deliver high levels of service standards at review times – with clients pressing for important advice at renewal, the process can only be completed as fast as the slowest quote.

It is difficult to see many ‘green shoots’ with regard to a growth in lives covered during 2009. It is hard to imagine employers expressing much appetite at the moment for new benefits of any kind that carry with them significant extra costs. Even if some growth is accomplished (for example, by the more effective marketing of income protection under flexible benefit plans) this may well be counter-balanced by membership attrition due to redundancies and smaller businesses simply deciding that they can no longer afford the premiums.

More optimistically, however, some insurers have reported interest from employers who are currently self-insured and who are reconsidering their position given the potential unpredictability of long-term absence claims and the difficulty this poses in budgeting for future expenditure.

It remains important to look to the longer term.

Firstly, used strategically as part of a health risk management approach, group income protection Insurance can help organisations achieve a virtuous circle of practices which will help protect not only the financial well being of the business but also contribute to the morale and well being of the individual members of their workforce. This in turn impacts positively on the financial well being of the business. In difficult economic times, employers must continually be presented with the evidence they need to justify expenditure on benefits. One of the most critical factors in this effort are the risk management features that form part of the group income protection proposition and how they can be co-ordinated effectively with other health initiatives. These will often include wellness and absence management programmes, employer’s liability coverages, private medical insurance and occupational health.

Secondly, as this paper has endeavoured to point out, the alignment that now exists between government strategy on health and insurer (and adviser) expertise is incredibly important. If it is to open up new avenues of income for all, however, it will mean existing players deciding whether it is worthwhile to develop new paradigms of distribution and product design. Of great importance is the decision as to what role ‘insurance’ will play in this new world of collaboration, conditionality, and tendering for services.

There was a time when insurers might have stated their business mission as ‘paying all valid claims promptly’ – is there a new role on the horizon: ‘helping to manage workforce health for the benefit of clients, their employees and for society as a whole’?

6 Reaching the consumer

It is often said that life assurance is sold and not brought. This is even more the case with income protection (IP). Regardless of the attitude of potential customers, there are hurdles in the way of the would-be buyer.

The market for income protection is predominantly in the younger age groups, 25 to 40. A potential buyer would probably “Google” income protection. On the day of writing, Googling ‘income protection’ produced the offerings shown below. Whilst the Google offering will vary from day to day, this is typical.

Tesco Life Insurance (www.TescoFinance.com)
Tesco Finance offering life insurance

Income Insurance (www.helpucover.co.uk)
Pinnacle offering ASU

Income Protection Cover (Endsleigh.co.uk/Income-Protection)
Endsleigh Insurance offering genuine IP

Compare Income Protection Insurance
(www.moneysupermarket.com/asu/)
Moneysupermarket.com offering Mortgage Payment Protection and Payment Protection

The poor consumer will be utterly confused and may not make the purchase intended.

It also appears to be difficult to find a suitable adviser. Whilst IFAs personally rate income protection highly, they tend to place critical illness above income protection in the hierarchy of protection needs. Currently, it is hard for the would-be customer to find an IFA that is both keen and competent to advise on income protection.

Even when specialist providers/advisers can be traced, it appears to be impossible to obtain a quotation without providing contact details. Many people do not wish to talk to an adviser until good and ready.

Here are some examples:

To ensure you get the cover that's right for you and your personal circumstances, our Income Protection plan can only be arranged with a qualified financial adviser.

Another firm requires these contact details:

Town/City »
County
Postcode »
Email »
Daytime telephone number »
Home/mobile telephone number »

A high street bank offers:

A plan tailored to meet your needs.
A choice of deferred periods and expiry dates.
Benefits that increase with inflation.

But there is a catch:

For more information call 0800 xxx xxxx to book an appointment or request a call back.

Whilst these organisations are clearly keen to get hold of prospects and complete a sale, it is more likely that they are frightening the customer away. It is possible to obtain a quote for motor insurance, home insurance, a holiday or a car – but not, it seems, real income protection cover.

The argument may be made that income protection is complex and advice is needed, but it is hard to argue that it is a great deal more complex than motor insurance today. Indeed, if it is more complex, perhaps that is a good reason for simplification.

High street banks have been reluctant to provide quotations for income protection. When CWC Research sent a mystery shopper into 3 high street banks, not one was willing to provide an income protection quote without a meeting with a financial adviser. One did offer MPPI.

Few products can be as hard for the consumer to purchase. It would seem that sales are dependent for the time being on providers and distributors taking the product to the consumer, when they choose to.

The market can be cut between group and individual.

Group income protection enables employers to insure the liability to continue to pay their employees when they are absent from work due to sickness or disability. Salary continuance has tended to be offered by public sector (sometimes self-insured) and other larger employers. It is generally part of an employee benefit package including pension.

On the whole, this is a mature market and is well served by benefit consultants interacting with the HR personnel at employers. However, the number of live final salary pension schemes is falling through the floor and this may not be good news for benefit consultants or group income protection providers as cost savings are sought.

However, there is much room at the smaller end of the group market for IFAs to improve the packages offered by their corporate clients. There is less competition here than there has been historically and, perhaps as a result, service standards are often very unsatisfactory. This is covered elsewhere in this paper.

The individual market can be broadly divided between conventional income protection plans from life insurers and “day one” Holloway style policies offered by friendly societies. Typically, the conventional income protection plan has focused on white-collar workers whereas the friendly societies have targeted the blue-collar workers, although this is not always the case. Both are distributed via intermediaries, IFAs and mortgage brokers.

The downside of this is that the ageing IFA market has tended to move to an older, wealthier client. RDIP is likely to encourage this drift. Many such advisers do not consider insurance to be part of their proposition. Those that might otherwise do so, may have concluded that the rewards do not justify the effort. Indeed, persuading a client to apply for income protection and discovering that he or she is not eligible for the terms quoted, or perhaps any terms, after a considerable period and much work, is hardly conducive to good customer relations.

At the same time, mortgage brokers have been too well rewarded for selling mortgages to bother with the time consuming problems incurred by adding protection covers to the mortgage. This situation has changed dramatically, as lenders are no longer offering procuration fees. On the downside, there are far fewer loans to cover.

The answer

There is no single solution.

The ultimate end goal is to inculcate into the population as a whole an understanding that disability insurance is an automatic purchase; a cover all sensible people carry. As can be seen from the introduction to this paper, Which? are great advocates of long term income protection insurance and of financial education of the public. They have been extremely active campaigning against the mis-selling of payment protection insurance. They feel very strongly that there should be a very clear distinction between genuine long-term income protection and ASU/PPI policies misleadingly branded income protection. They particularly dislike exclusions in policies, especially when these are not made absolutely clear to the customer.

Which? believes that the public will buy income protection insurance if they are made fully aware of the need. Could there be a public awareness campaign along the lines of the fire alarm campaign featuring Julie Walters, sponsored by the Home Office?

There is no doubt that many people are hopelessly optimistic about what they might receive in the form of state benefits. The IPTF believes that legislation should be enacted to compel employers to advise employees exactly how long they would be paid and how much.

Which? also believes that the banks have a role to play. They are the only institutions that have access to the vast majority of the population, a presence on every high street. Of course, a bancassurer product would have to provide satisfactory benefits and be totally transparent and easily comprehensible.

An IFA View

IFAs tend to defend poor sales of income protection by saying that customers do not want it. Historically, most advisers were sales trained in direct sales forces. For good or for bad, that is no longer the case. Direct sales forces prioritised protection and taught their recruits how to sell life cover and, to some degree, permanent health insurance as it was known.

Times have changed and most IFAs major on investment or mortgages. Critical illness cover became the disability cover of choice, largely due to very heavy provider marketing and an easier sale. Heart attacks and cancer are perceived as greater risks than stress and bad backs; a capital sum is easier to sell than income.

There has been significant product development, with hybrid products offering something different and attractive. In an ideal world, products would be simpler and underwriting could be easier. However, the real problem is adviser education.

Too many advisers do not appreciate the importance of income protection. This will only be changed by the ongoing efforts of insurers and by the trade press. The recession and the near death of the mortgage market may force advisers to sell protection whilst there is little alternative. Only education will make a long-term difference.

Many IFAs are now styling themselves as wealth managers. RDIP has encouraged this. However, the good financial planner will always ensure that income is protected as, in the vast majority of cases, all else hangs on income. Indeed, it is surprising that the Treating Customers Fairly initiative has not resulted in a big increase in income protection sales.

There may be opportunities for strategic alliances between wealth managers and protection specialists as there has been with mortgage brokers for years. Ultimately, if advisers, as a matter of course, always recommend income protection, the press will follow and customers will accept that it is good advice.

A Friendly society view

It is commonly assumed that IFAs can't be relied upon to sell income protection, that they find objections to sell it and therefore how do we go about reaching the customer? The weaknesses lie with the income protection provider, rather than the IFA. There are two:

- A lack of true B2C activity (targeting consumers directly to create that customer pull) by income protection providers.
- A lack of support and training for IFAs in order to help them find customers and create that pull themselves.

Research has thrown up IFA objections. Product providers shouldn't ignore these. They should take note, understand them and address them, as they are barriers to selling.

The greatest responsibility to reach the customer lies with the income protection provider. Once this has been accepted, there should follow a willingness to put solutions in place. An IFA cannot operate in a vacuum and create the customer pull with so many products to market. An IFA may not be able to stretch to the marketing of one particular product alone. This is why success depends on the income protection provider working hard to create that pull whilst at the same time support the IFA in the push.

Solutions

- **Providers create demand**

In the Income Protection industry, neither the product nor the need are promoted particularly well in consumer press, consumer adverts, TV, press and radio etc.

There are plenty of genuine reasons why they aren't promoted; some income protection providers do not take direct business, some do not want to encourage direct business, some are relatively small and therefore do not have the budget, whereas the larger organisations, with multiple product ranges, probably consider income protection as a less important product to focus their marketing spend on.

This does not mean to say consumer marketing is redundant. As an industry, the specialist companies should come together to promote the overall benefits of income protection to collectively improve awareness of the product. This would provide a halo effect, which would support the work of the IFAs in their own markets.

Collectively, this could be done in consumer press, through consumer PR, and through financial journalists.

- **IFAs create demand**

The most important area for income protection providers is the IFA market; this market is the main distribution channel in many cases (although not all).

At a very basic level, an IFA won't sell a product that isn't suitable or "doesn't work". They won't sell a product if they don't understand it or if they don't have the correct literature/access to literature. They won't sell the product if the process to submit an application is difficult or time consuming or the company is hard to deal with.

At a more advanced level, they WILL sell the product if the provider actively helps them identify their typical target markets and provide the literature or other marketing tools in order to reach them.

Some objections:

IFAs have moved towards wealth management and are ageing.

Not entirely true today. Whilst the IFA market may well have moved towards wealth management in the recent past, in today's economic climate IFAs are looking at alternative products. Good IFAs recognise that these customers could be wealth buyers of the future. Wealth management is okay when clients have some wealth to manage. When a client is unable to work and earn a living, what goes first, the car or the savings? A good income protection contract may well be the difference between keeping a client's wealth under management or not. Income protection has its place and IFAs need to appreciate it more.

Friendly Societies rely on IFAs for much of their distribution

Not entirely true. Not all friendly societies rely on IFAs to distribute their income protection products. Some still operate sales teams. Those that only market through IFAs are able to focus on training and support. In doing so, they can help them reach the customer.

Providers cannot assume IFAs will sell their product. It is essential to work with them on product design. Going forward it may be necessary to consider other forms of distribution to divest risk in case IFA numbers fall, as they are expected to do.

The RDR is vague on protection mentioning just enough for unease

Many reports suggest RDR will impact the IFA market by driving some IFAs out, but regardless of this situation, whichever IFAs remain and are able to sell income protection will require support, training and commitment by the provider.

Banks have focused on PPI and may not seek a replacement in a similar place

The sale of PPI as an add-on to personal loans and mortgages has been easy and a cash generator; banks will now find themselves under even greater pressure to act in the interests of their shareholders and their customers. This could mean they need to seriously consider adequate and effective protection products for those taking out financial commitments through them. This in turn could lead to product innovation or re-consideration of income protection.

That said it must be noted that banks offer a vast range of products and if income protection isn't a core activity or revenue stream, then the incentive to promote it may not be there. Simply trying to survive as a bank might be slightly higher on their agenda. On the other hand, specialist income protection providers such as friendly societies who rely on the product to exist should know income protection inside out, know how to train the IFA and help them find the right customers.

Will Holloway style plans be sold under COB?

True Holloway style plans contain an investment element or at least the right to participate in one. They are not Holloway contracts if this aspect is not present. The contract has always been categorised as an investment product because of the investment/profit-sharing element and, as a result, subject to the full personal illustration and associated investment product regulatory. If declaring total premiums on personal illustrations for pure income protection is irritating to some, having to comply with regulations aimed at pure investment products has been galling to Holloway Friendly Societies for considerably longer! It is likely that it will continue to be sold under COB because of the investment aspect.

A bancassurer view

The core challenge is how do banks deliver a proposition that customers find relevant to the 21st Century.

Firstly, let's shatter the illusion that the alleged demise of PPI is an opportunity in itself. It isn't, as income protection is under threat if only 'by association.'

There is an indirect opportunity that as an industry we should grasp, as the desire to reinvent PPI will put much greater pressure on conventional income protection, as income protection is less likely to have the same moral high ground as some argued it had previously. In other words the competition from a substitute/sister product will be much greater.

The view that there are two markets, PPI and income protection, is false and has only ever been maintained by intransigence on both sides. There is no fundamental difference that can be justified from a consumer perspective between short-term and long-term business other than that some customers are interested in immediate protection and other interested in permanent protection.

That short-term business is issued without underwriting and with pre-existing exclusions and that long-term is the reverse is not sustainable.

The emphasis should be on how do we fulfil and deliver to customer need.

The challenge is as much about process as the insurance product itself and is not easy to solve. To create a product that is simple to process and that offers comprehensive cover, will be difficult if not impossible.

All the time we have a 'brokered' solution to distribution then we have a challenge since, as an industry, we focus on price rather than on quality, i.e. simplicity and coverage. The bancassurer has an opportunity to address this in as much as they have (more) control of distribution than a split underwriter/distributor model.

Such control is not total as bancassurers offer a range of propositions, importantly wealth management in addition to protection, so that protection is too often the bridesmaid rather than the bride!

In a bancassurance world influenced by the changing approach to PPI and with a back drop of RDIP, we might see protection specialists emerging that effectively are more aligned to customers purchasing credit than customers purchasing wealth products. Wealthy customers may be more able to afford protection but arguably have less need.

As an industry, we get hung up on the argument about a full financial review for customers and interpret this as reviewing pension, investment and protection for every customer. The real world is very different, as customers rarely need all three at the same time and even when they do they prioritise.

Customers are different but too often in the past we have tried to deliver a common proposition as if they were all the same.

We have simple propositions that mass-market customers need, where price is less of an issue as the price is smaller and more tailored propositions for sophisticated needs that are necessarily more costly and, as a result, controlling cost is more of an issue.

In the past we have delivered this (almost by default) as PPI for lower and middle mass market and income protection for more sophisticated needs. Where we have failed is that HNW customers won't buy PPI and when we sell income protection to the mass market then, too often, we realise that the quality of the business is sub-standard and the persistency is poor.

We move therefore to the position where we need to take the best of income protection and the best of PPI and throw away the worst of each. What does this mean? In short, can we sensibly remove exclusion clauses from PPI and can we make the underwriting process on income protection simpler?

The answer is ‘yes, we can’, but the solution is not the same for all customers. The old solution of a non-underwritten product for mass market and underwritten solution for larger more sophisticated risks was not so flawed - we just allowed the retrenched positions of long-term and short-term businesses to conflict!

It is not the job of this paper to define solutions. Would that it was so simple. The reasons for exclusions on short-term business and more detailed medical and financial underwriting for long-term business are sound from an insurer’s viewpoint. There may be a need for some compromise. Certainly, if the market is considerably larger, anti-selection may be a lesser concern.

Clearly we cannot disregard distribution and customer channel preference. More sophisticated needs can continue to be met by a brokered model largely; for mass market, a direct model where the insurer controls distribution, i.e. bancassurance, is probably the only viable model.

What this means for income protection is that the old style long-term product is unlikely to ever grow massively if it is always pigeon-holed as it has been (brokered and underwritten), but there is opportunity to take an improved PPI proposition (may be longer term cover, i.e. more than just 12 or 24 months) with reduced exclusions and, maybe, simple underwriting.

Arguably, this is contrary to the earlier statement that PPI does not create an opportunity but in reality, as soon as we forget the arbitrary distinction between the two, then may be (and just may be) we will start to find the solution.

USA market developments

One characteristic division in the US financial services market is between insurance and investment; "financial advisors" of various types focus on mutual funds, stocks and shares, cash management, and such areas of financial planning, while brokers and insurance companies sell medical and dental plans, life and disability insurance, property and casualty, and other products. Large brokers and companies may offer both services through multiple, qualified employees.

However, such services result, in part, from a greater awareness of the need for insurance; probably the result of the absence of a comprehensive "safety net" which is more commonly seen in a welfare state. Thus, health insurance is a "must have" for all who can afford it. This, in turn, creates a greater awareness that injury and illness can happen, which results in established distribution channels for related covers that no longer exist in the UK.

Another factor raising awareness of the need for cover in the US is that long or short-term disability insurance is purely insurance for disability; while in the UK, there is a split between long and short-term cover, much complicated by marketeers. The customer is faced with income protection, permanent health insurance, ASU cover, mortgage payment protection, and the often toxic loan payment protection. Also, in the US group market, the policyholder is the employer but the direct beneficiary is the employee or claimant. In the UK, the employer is both the policyholder and the beneficiary (in effect a structure of "salary continuation insurance" for the employer, rather than disability insurance for the employee. Whoever said, "Keep it simple"?

Which doesn't mean that selling disability cover in the US is easy when the calls of medical and dental plans make very big holes in limited budgets.

The Council for Disability Awareness

In order to increase awareness of the likelihood of disability and its impact, 15 insurers have banded together to create The Council for Disability Awareness (http://www.disabilitycanhappen.org/).

The mission of the Council for Disability Awareness (CDA) is:

- *To expand public awareness of the growing likelihood of disability occurring among the working population*

- *To increase public knowledge about the financial hardship that disability can have on wage earners and their families*

- *To demonstrate the value of planning responsibly in the event disability prevents one from earning a living*

The Council for Disability Awareness will empower working Americans with the information they need to make responsible decisions to prepare for and maintain financial security should they become disabled and unable to earn a living.

The CDA website gives information on the chances of disability, preparing for disability, reducing changes and much more. Importantly, there are case studies of individuals who have had to face the impact of disability.

Another organisation, Life (http://lifehappens.org/), inter alia, promotes the need for disability insurance. Support includes Disability Awareness Month (DIAM). During Disability Insurance Awareness Month (http://lifehappens.org/diam/diam-plans), LIFE's goal is to get Americans thinking about their disability insurance needs and, hopefully, to motivate them to do something to address those needs.

There are other organizations promoting action around the causes and impact of disability. The CDA website provides numerous links and is well worth a visit.

What about the UK?

There has been little appetite for an industry led campaign to generate awareness of the causes, likelihood and impact of disability. There is some light on the horizon. Twenty-two insurers and reinsurers are funding a comprehensive planning exercise to advise on how best to get consumers to engage with the protection industry. The group is to be chaired by Lifesearch MD, Tom Baigrie, so income protection should be high on the agenda.

The Income Protection Task Force is attempting to achieve a little of what the CDA does in the US.

A web site has been created (http://www.protectingmyincome.co.uk/), which is designed to increase awareness and knowledge of all aspects of disability and the need to prepare for the consequences.

The site is directed at consumers, advisers and all with an interest in income protection. Hopefully, most is in a language that all will understand.

Online sales

Many of today's customers and most of tomorrow's will expect to compare and purchase insurance products online. This presents great challenges to providers and distributors if people don't believe that they need the cover. Assuming that hurdle has been overcome, it will be necessary to make comparison and purchase simple.

It is not the purpose of this paper to design products. Nonetheless, it is reasonable to assume that to achieve substantial online sales:

- Language must be straightforward and the product must have one accepted and unique name

- It must be easy to make accurate comparisons

This means there must be standardisatiion of those aspects that are non-competitive such as whether deferred periods are in days, weeks or months; state benefit offset and, to some extent, employment categories (as in motor car categories).

Currently, there is opposition to this on the grounds that the Competitions Act will be infringed. This now seems very unlikely since the Competition Commission enquiry into PPI (PPI being, in part, short-term disability cover) states that there is a need for standardisation as current complexity is detrimental to the customer. It can hardly be different for long-term cover.

- The customer should be offered a choice of terms to suit his or her needs

The differentiation between long-term and short-term business and the impact on the way income protection can be written goes back to various Insurance Companies Acts and was subsequently brought into FSMA through SI No 544/2001.

There is nothing to stop a long-term insurer writing short-term policies.

If one were to pose the question to the interested consumer, “In the event of long term illness or disability, for how long would you like the insurer to continue payment?”, it is reasonable to assume that first choice would be “until I am fit enough to return to work”.

Naturally, there will be those with budget constraints who choose a shorter payment period, perhaps five years, or even two.

The point, clearly, is that the consumer must be offered a very clear alternative and differences in costs and benefit must be obvious. Hopefully, the only difference would be payment term, and not exclusions.

Consumers are unlikely ever to trust an industry that attempts either to confuse, or to wriggle out of legitimate claims. Greater clarity will improve the proportion of claims paid.

7 Conclusions

Awareness of the need

In order to place income protection in context, it is interesting to compare the product with insurance covers that are regarded as essential by the majority of the population and their advisers. How essential is income protection when compared with house contents insurance?

The loss of our most prized possessions might be regarded as awful. However, it might be possible to cobble together the essentials with savings or borrowings, perhaps buying second hand goods and accepting the charity of friends, relations and neighbours.

The loss of income removes the ability to pay bills. Indeed, contents insurance might well have to be sacrificed when living on incapacity benefit of around £80 per week.

It is hardly contentious then, to argue that income protection is a greater priority than contents insurance.

Yet, nobody in their the right mind would not insure the contents of their house.

For the public to appreciate the value of income protection we need to achieve a situation where the public, advisers and the media all accept that income protection insurance is an insurance policy that any responsible individual should buy – just like house contents insurance.

The best of income protection and PPI

This White Paper began with a re-iteration of the 9-point plan that formed the action points for the original White Paper in December 2006. Progress has been made in many of these areas but much remains to be done if the product is to reach the numbers of people we believe have need of it.

When we talk about product, it is an illusory term. One of the lessons of our study is that income protection is a goal that can, and should, be achieved via a variety of routes depending on client need, occupational circumstances and affordability. The section on PPI looks at the way in which a product that has been criticised for its "toxicity" might be replaced by a more acceptable form of income protection. New ideas about income protection are sprouting regularly and it is our expectation that several more new concepts and hybrid products will tackle the income protection challenge shortly.

We anticipate distribution breakthroughs that will make writing income protection online a pipedream no longer. We believe that the move to simplify the underwriting process, which is fundamentally important to the success of income protection, will continue with more ambitious ideas being mooted. The Task Force will never design products but it can stimulate new thinking and alternative approaches and these are inexorably on their way.

The new era of TCF should increase the pressure on companies to make products clear, appropriate and unambiguous. We also believe that there needs to be both education in the adviser sector about the way protection should be evaluated and also a system for establishing protection priorities and this is the reason we recommend the adoption of the Essential Protection Index as an industry standard.

We believe its methodology and its logic are irrefutable and we hope that it will enable many more advisers to sell what their clients really need.

Statement of sick pay entitlement

There is an initiative in the industry to popularise and to publicise the value of protection insurance. Alongside this, we believe that consumer education should be supplemented by better government-sponsored information on the vulnerability of individuals as a result of income loss.

Every employer should produce an annual sick pay entitlement statement for each employer; each self-employed person should receive an annual statement of state entitlement payable if they fall sick.

Standardisation

Products being developed need to avoid unnecessary complexity. However, we would still urge the standardisation of non-competitive aspects. Some ill-informed commentators saw this as the main recommendation of the last White Paper rather than one of a series; indeed, if we see product innovation, certain aspects of the standardisation message may not be appropriate.

The need for transparency and comparability

Currently, it is extremely hard for the consumer to access comparable quotations for income protection. Anyone in doubt has only to ask a friend or relation, who is not in the industry, to try. To help advisers and consumers to compare products, we believe it is essential to eradicate unnecessary complexity that can only cause confusion on all sides.

In our perfect world, any form of income protection or disability policy would be permanent to guarantee continued insurability; it would, in the even of claim, pay benefits to the insured until they were able to return to work or until normal retirement date to meet all essential expenses. In reality, most people have to juggle their budgets in order to buy those things that they want or need most. Individuals will have differing priorities.

Thus, it is right and proper that the market produces a complete range of solutions, from short-term plans with limited payment periods to long-term plans that will pay until recovery or retirement. It is incumbent upon the industry and regulators to ensure that the potential purchaser is able to fully understand what is being offered and be able to compare costs and benefits with ease.

We would like to see web-based intermediaries offer such comparisons. Whilst the parameters are different, motor insurance has a larger number of variables and choices; the customer has to make numerous decisions. Nonetheless, there are many excellent motor insurance comparison websites.

We look forward to seeing the first, simple but comprehensive, online, disability insurance supermarket.

The name of the product

The customer is being further disadvantaged by the generic names given to products. For years, income protection was known as permanent health insurance. This was considered misleading. After much consultation and discussion, the name “Income Protection” was adopted by the industry.

Sadly, sellers of ASU/PPI products have hijacked this name. They argue that theirs is an income protection policy or that they have used the name for years. The Internet has made it much easier for ASU/PPI providers to ride on the back of the income protection name. The reality is that the nature of the search engine means that one can engage with potential customers by leading them to your site by whatever means you want.

Regardless of the rights and wrongs of these arguments, the outcome is that the customer is confused and may purchase a product that was not what they intended to buy. Regulation should not allow this practice to continue when there is clear intention to mislead; insurers collectively should ensure a distinction, otherwise they cannot expect the customer to trust them.

The solution is not simple. Labels such as long and short term do not offer a solution, as they do not make it clear whether the long or short refers to premium paying term or payment period. Moreover, there are hybrid products. Is a single premium policy with guaranteed renewability long or short term?

The arguments used within the industry have no relevance to the potential customer. Without total clarity, the product will never be truly successful.

Process

The success of PPI is, arguably, based on three factors:

- The customer identifies with the need (at least at the point of sale)
- The reward for selling the product is satisfactory or better
- The processing and administration processes are simple

Any successful, mass-market, disability product must satisfy these same criteria.

Most intermediaries say that the reward for selling income protection is adequate according to research (*Reinventing Income Protection, Le Beau Visage and CWC Research, 2005*).

However, further drill down indicates that the reward becomes unsatisfactory when the process is complex and long. Historically, it has been both.

From the intermediary viewpoint, there are two aspects to the acquisition process that have to be right to ensure a compliant and profitable transaction:

- A compliant fact find

- Application (including underwriting and initial administration)

A compliant fact-find

Advisers must employ a compliant fact-finding process that does not ‘kill’ the sale. It should be remembered that income protection is largely self-policing. Insurers are concerned about over-insurance far more than the regulator.

The adviser should only need to know that the customer has essential outgoings and relies on earning a living to meet the cost of them and is not covered elsewhere, e.g. by employer cover.

We will make it a priority to engage with leading compliance consultants and managers to develop a short, compliant fact-find process and to ensure that all advisers are aware of this.

Application and administration

Enormous progress has been made since the first White Paper on the underwriting of income protection. The adoption of tele-interviewing and tele-underwriting has enabled advisers to recommend income protection without the problems and time-cost of gathering data for underwriting.

This means that a mortgage adviser, for example, can happily recommend income protection without acquiring the competence to question applicants on complex medical and financial issues and thus avoiding potential risk where the layman carries out this process.

We are aware that not all procedures are perfect. We will continue to work with advisers and establish what works and what doesn’t and feedback to insurers.

Adviser road shows

Improving adviser awareness and competence has always been a major hurdle to be cleared. This year, we will be running a series of road shows to ensure advisers:

- Are aware of where income protection sits in the protection hierarchy
- Understand how to demonstrate the importance of income protection to customers
- Adopt processes to so that application, processing and administration are carried out effectively and within cost parameters to ensure that recommendation of income protection enhances rather than hinders the firm’s profitability

It is our intention to offer road shows to hundreds of advisers whilst establishing a formula that can continue to be used so that ultimately, thousands of advisers are properly trained on income protection

Who is responsible for advice?

Prior to regulation, insurance broking covered life and pensions as well as general insurance. Regulation not only brought a polarisation between investment advice/wealth management and general insurance broking, it allowed certain products to fall by the wayside.

The IFA has retained only certain aspects of traditional life and pensions business, whole life, term life and critical illness, whilst largely ignoring true disability cover. At the same time, insurance brokers have moved away from such products, especially true income protection.

If the customer is to be treated fairly, it should be incumbent on all advisers to ensure that income is insured against sickness and disability. Does existing regulation provide a solution?

We must engage with the regulator and compliance managers to ensure that income protection is does not fall between the two and become a victim rather than beneficiary of well-intentioned regulation.

8 The Way Forward

There is only so much the Task Force can attempt to achieve in the coming year or so. These are the actions on which we intend to focus, to help ensure income protection is seen by advisers, consumers and the media as the most important protection policy for the majority of the working population.

8.1 Welfare Reform

Welfare reform creates closer alignment between state and insurers; interests are much the same. The Task Force must look to connect with Government and identify how the similar interests of the consumer, the industry and government can best be served. A harsher regime should send a clear message to individuals to ensure that they have cover in place. Issues such as rehabilitation are equally important to all stakeholders.

We must work with the Government to encourage a clear statement from employers of the benefits provided to employees in the event of accident and sickness to ensure that consumers are as fully aware as we can make them of their financial vulnerability should sickness strike.

8.2 Awareness of the need for income protection

The Task Force will increase activity to ensure consumers and advisers are aware of the incidence of long-term illness and disability and the financial consequences thereof. The prime activity will be a series of adviser roadshows. In addition, we will continue to increase media awareness of the problem. We will also strongly encourage the use of the ‘essential protection index’ as a tool to measure the protection product need.

We will work seek to work with the ABI to publish claims statistics to demonstrate that income protection is an area where the industry really does treat customers fairly when they need it – at the claim stage.

8.3 The Competition Commission Report on PPI

Whatever else, the CC report will create a vacuum. It is essential that this vacuum is filled by non-toxic disability products that meet customer needs; that are transparent and easily comparable; that are profitable for insurers and distributors. Customers’ wants and needs are diverse, and there must be opportunities for providers and distributors who are willing to take up the challenge and address these needs. The Task Force must help to facilitate this.

We will also engage with FSA to discuss ways of improving the website, www.moneymadeclear, where income protection is currently placed last in the protection hierarchy. We will work with other stakeholders to establish some form of kite mark, perhaps under the auspices of the Money Guidance process, which covers policies of all types, whether sold in the short or long-term markets.

8.4 Group income protection

The Task Force will attempt to harness the potential synergy between Government policy on workforce health and the way group income protection arrangements function. The industry must continue initiatives to help claimants return to work.

There is much opportunity for new product development. There is equal opportunity in the SME sector; the Task Force believes investment in adviser education will attract generous payback.

Investing in health is a win, win strategy. The development of true worksite platforms incorporating DC pension plans, life and income protection and PMI, combined with health programme initiatives appears to be a very sensible way forward, addressing a number of the major financial, medical and lifestyle problems in one initiative.

8.5 Reaching the customer

The Task Force will endeavour to encourage insurers and distributors to make it easy for consumers to obtain clear, accurate and transparent illustrations of costs and benefits that are easily comparable. We will also lobby the regulator, ABI, AIFA, PFS and IFP to do the same. Sales of income protection insurance are unlikely to reach satisfactory levels, if it is hard for the customer to get the requisite information i.e. costs and benefits. In addition, we will continue to encourage reforms to application, processing and underwriting procedures that will make it easier and more profitable for advisers and other distributors.