

A response to the Sergeant Review of Simple Financial Products: Interim Report from Steve Devine

Dated 10/12/2012

This is my personal response to the Review and does not in any way involve or reflect the opinions of any company or associations that I am connected with.

Overview – I had the pleasure of being involved in the Protection working group of this review, albeit I was drafted in after the commencement and missed a number of the earlier meetings. I am disappointed that the Simple Protection Product has not made the initial suite of Products. Without it I feel the “industry” could be accused of having “limited ambition”.

That said, I am of the opinion that a protection products are often very far away from being simple. At the short term end, Creditor insurance, MPPI, ASU type product, appears to have been labelled as a “toxic” product and not considered appropriate. There was also no appetite for the Short Term Income protection (STIP) products which either originated from the Personal Accident Market, or, as the next generation of stand-alone creditor insurance products.

This product is still in its infancy, there are 40 or so products in the market but no statistics available regarding the size of the market and the number of claims being made. I believe the potential expansion of this market is currently being stifled by the delayed (until the end of 2012) Final Guidance on Payment Protection Products from the FSA/OFT. I would also not be surprised if the Final Guidance, and the new product risk approach to be taken by the FCA next year, continues to dampen any enthusiasm for developing and promoting STIP products.

I would make two points about STIP policies:

1 They mostly include unemployment or redundancy cover. The major risk to the income flows of many employed consumers.

2 STIP policies already appear on MAS comparison tables. They can be compared and purchased online.

At the longer term end of the Income Protection insurance market, apart from Bills & Things from Exeter Family Friendly, there are some very good but complicated and expensive products that have lengthy application processes and little chance of ever being termed as Simple Products. With annual sales of just over 100k policies, these will remain niche products in their current format, sold on an advised basis by IFA's and intermediaries.

Furthermore, I suspect many advisers would not welcome the opportunity to sell their clients simple, restricted cover policies, or that consumers will have an appetite for the cheapest products that don't provide sufficient cover to meet their needs.

I believe the Review should also consider the adoption of other protection products currently sold on both a group and individual basis. Health Cash Plans for instance. They provide benefits and discounts that policyholders know that they can claim on (optical/dental). They can incorporate well-being and lifestyle promotions that can help consumers lead healthier and more active lives, reducing the burden on the State, NHS and the Benefits system.

The Government too could also consider providing incentives and improving the fit that simple products insurance benefits have with the state benefits system. So that no one is penalised by losing benefit for trying to mitigate their circumstances by taking out protection insurance. (The precedent being the way MPPI benefits are disallowed under ISMI.)

I believe that Protection Insurance is fighting for its very existence. Its competing with far more attractive competitors for a share of a consumer's disposable income. We have to remove any major barriers that prevent consumer's understanding what our products do and don't do and the benefits of having them to call on. To do that the insurance industry has to start breaking down the existing product silo's, removing duplication and confusion. This review could be the start of it, I do hope it is.

In terms of answering the Consultation questions, here are my answers

1 Yes

2 No

3 No, firms should not be limited to one issue of each simple product type, per brand, per channel.

4 No, a protection insurance product should be included in the initial suite

5 See my overview comments

6 See my overview comments

7 I think MPPI, STIP and Health Cash Plan products should be considered

8 I think MAS should be the accreditation body

9 Yes

10 Yes

11 Yes

This is the end of my response.

Please do feel free to contact me if I can play any role in the next stages of this review. I did organise a workshop on this initiative for members of the Protect Association and encouraged all our members to engage with this Review.

I would be happy to volunteer my services for any future meetings in the next stages.

There is also an open invitation for anyone working on the next stages of this Review to speak at a future Protect meeting.

Best wishes

Steve Devine

Norman Digance MBE

9 August 2012

Carol Sergeant
Chair, Simple Financial Products Steering Group

Dear Carol

I have followed recent events about the development of “simple” financial products with considerable interest. The reason is itself simple: I was involved in developing the regulatory regime for ISAs, I was in the lead developing the regime for stakeholder pensions (including decision trees) and the same goes for Child Trust Funds. With this background you might guess that I was not without a smile on my face when I thought “here we go again!”

With such a list of the current great and good engaged in the exercise with you, I have not thought it worth making any contribution of my own – not least because I am not now too actively engaged in the field and much as happened since I was. However, with the consultation just launched I can see the general sense of direction. Drawing on my experience of when we went around this circle ten years and more ago, there are one or two observations I would make which you might find useful when you come to seek closure of the circle you are going around now.

I believe it is as misleading now as it was then to refer to “simplicity” as an end in itself. Now as then a life policy is a life policy whether you describe it as a simple or complicated. If you mean by “simple” something that will deliver different (and presumably, lesser) outcomes then fine but I doubt that is your intention. Nor is it helpful to infer that complexity is a modern illness in financial services. As I write, I am looking at a life policy taken out by my parents on 18 December 1944 when I was 1 month old and I can assure you that it is anything but “simple” in the sense that you are now contemplating. But at that time, it did not prevent such policies being taken out. The reason why these things now cause such anguish is one worth much deeper exploration than I seen from what has been published so far. I would strongly urge you to consider adopting a new collective adjective which better describes what it is you are aiming for – and not least it would help you to make clear that you are doing something different and than just regurgitating the past.

So much of what you are doing now and as it was before is that the “ordinary man in the street” has lost his trusted building society, friendly society and trustee savings bank. This is a difficult one to address and to quantify but I firmly believe that much of the grounds for current anguish about complexity would not exist if customers had the

range of institutional choice they had 20 years and more ago. The problem now is that the “ordinary man in the street” is forced to do business with an institution (a clearing bank) which he would previously not have countenanced and wishes he did not have to do so now. But instead of looking at himself he blames the product (and the bank). So, what you are trying to do is to recreate trust and confidence in products as a proxy for confidence and trust in institutions. The solution to the problem is as much one of social policy as it is anything else and regrettably I have not seen much written about that.

In the creation of any family of “simple” products I believe it is at all costs crucial not to have the design handed down from HM Treasury and so to which a regulatory regime has to be attached regardless. The FSA was inadequately involved (if it can be said to have had the opportunity at all) in the basic design of stakeholder pensions even to the extent that it did not have any opportunity to review the plausibility of decision trees as a buying and regulatory tool. What we found here was that the Treasury’s ideas on decision trees were far too basic for regulatory comfort so we effectively took them over. It was at this stage that I developed the concept of FSA Discussion Papers and basked in the sunshine of being described in the financial press as the “father of decision trees”! But it taught me a lot about the virtues and limitations of simplicity.

Having learnt the lesson, I was determined not to allow the same thing to happen when CTFs came along. The meant many hours of deep and complicated discussions with the Treasury and Inland Revenue (who were in the lead) but it was a price worth paying. Referring to the Revenue reminds me of another problem to be avoided – or at least not fallen into without preparation. We worked extremely hard to develop a sensible and proportionate regulatory regime for CTFs but we almost came unstuck when the Revenue produced their own voluminous “guidance” which in some parts we found cut right across what we in the FSA were trying to achieve – and this took an enormous amount of work to correct. So when there is so much focus on getting the regulator to play ball as though that is all there is to it I would remind everyone that HMRC needs to do likewise.

You have referred to CTFs as part of the “simple” range at the time but I can assure you that there was much debate as to the validity of such claim. CTFs were/are not “simple” products – they were standard products with a special label and that is all (hence the debate). I argued at the time that the market did not need a new family of products and that a “junior” range of ISAs was all that was necessary – and this all in the best interests of keeping things “simple”. I should have copyrighted “Junior ISAs” methinks! But more seriously it is all too often the range of products with hard to identify and prove variables that confuses rather than the underlying product itself.

The absence of thoughts on decision trees in what I have read is disappointingly notable. The truth is that even at the time we were far from sold on the concept as the Treasury had written it but we had no option and so just got on with the job. We doubted they would ever be used as a primary buying tool and we were proved right – albeit that there was some interesting evidence that they were used as a secondary tool. But this is not to say that the underlying idea is not a good one.

One thing I have not been able to identify in what I have read is why you think you can succeed now when so much and so many have by definition failed before. I have read lots of words but not a well reasoned and properly evidenced piece on why you can expect to complete a circle where others have left a gap. That is quite a challenge but without it where is the leadership behind which you want and need the industry to coalesce? If I may be permitted to give you two hard and fast examples: first, enough has been said about the desirability of a “simple” life policy and enough has been said about the difficulties so take the bull by the horns and produce what you consider to be the desired outcome and challenge the industry to gainsay it; second, pay more attention to advertising – as an armchair regulator I get incensed by claims from life and general companies about the “value” of 50% lower premia which must lead to so much rubbish buying that whatever you do to simplify the product will be overlaid and so with marketing hype.

Finally, I note you propose to move into product regulation and policing. I can only say good luck!

Best wishes and happy memories!

Yours sincerely

Norman Digance

Independent response to Sergeant Review of Simple Financial Products

Contents

Respondent background.....	1
Response summary.....	1
Response to interim report questions.....	1
Additional points.....	2
Life cover product design.....	4
Q5: Life cover product design comments:.....	4
Income protection	7
Q7: Product design comments.....	7
Q7: Can S.I.R. be made sufficiently straight-forward to “qualify”?	9
Income protection resources.....	9
Additional points.....	9
Some cover is better than no cover.....	9
Please remember small businesses	10
Products should do what it says on the tin – key to trust	11
Inheritance tax on pure protection is an unwarranted and damaging distraction	11
Parting shot.....	13
Appendix of handy stats	14

Respondent background

Qualifications: LLB, ACII

Professional experience: 24 years technical and product development specialist in protection

Personal experience: Claimant under both income protection and critical illness cover (but OK now, thanks)

Current employment: Self-employed involved in various projects involving innovation, particularly where progressive thinking can be applied in the spheres of protection, health and small business

Status as respondent: Not employed or paid by any organization, views here are my own, seeking outcomes beneficial to consumers (including small businesses), supportive of social policy and commercially and practically viable for insurers.

Response scope: Simple life cover and income protection (Qs 5, 6 & 7)

Response summary

Response to interim report questions

Q5: Life cover product design comments:

Chosen representative: Use of this term makes it unclear in what capacity the proceeds are to be received – if as beneficiary, better to say so, if not, then what is the representative supposed to do with the money? Both routes have challenges, beneficiary being the simplest, but both are much preferable to the current default to legal personal representatives, which leads to payment delays for the majority of cases without a trustee of the policy.

Additional features: It makes sense to exclude the additional features you list. It is disappointing but expedient to have to exclude terminal illness benefit.

Suicide exclusion: Yes, reasonable within 12 months, but is it even necessary as it is in a small way counter to the aims of simplicity? Unless it is necessary to industry acceptance of the product.

Non-standard exclusions: It is unclear whether these are to be permitted.

Independent response to Sergeant Review of Simple Financial Products

Calls caveats: The threefold repetition in the draft policy of “We may record and monitor calls. Call charges will vary.” imparts an unfortunate and avoidable flavour to what is intended as a trust-generating product.

Q6: Simple Income Replacement product design comments:

What	Why
Early intervention PMI pot	More valuable to enable people to carry on earning than to replace earnings...and cheaper
Benefit period ends 5 years after incapacity start	<ul style="list-style-type: none">• Still provides meaningful pay-out duration even for longer deferred period cases.• Facilitates more accurate price modelling as 5 year is universally used as patient outcomes benchmark in medical studies.• Allows sensible and humane time for claimants to re-design their lives
Heart-strings lump sum benefit for permanent severer cases	For non-musculo skeletal/ mental health severe impairments (so less than 20%? potentially eligible) where it seems unlikely the insured will be able to return to earning near the benefit level a lump sum benefit of say 5 times the benefit level seems a more humane and palatable way to terminate income replacement.
Own occupation needs to mean own job!!	Or else useless!
Benefit of the doubt claims stance	It's just inappropriate to expect trust where the claims process goes beyond a balance of reasonable probabilities and opinion of the medical professionals involved, to place the onus of proof on claimant as if in a court case, but where the insurer is prosecutor, judge and jury.

Q7: Can S.I.R. be made sufficiently straight-forward to “qualify”?

Yes, it has to be.

As the Swiss Re Health Watch numbers show, the gap is even greater than for life cover and that's worsened of over the last 10 years. Yet the social importance measured by impact on individuals and dependence on welfare is much greater than for the life cover gap. Especially as the welfare safety net has become less and less safe.

Additional points

Some cover is better than no cover

Making sure people get covered and that something actually pays out when expected and needed is more important than:

- the cheapest possible price for it (though affordability is important)
- regulatory / legal disclosures - less is more
- making bereaved families wait months for their insurance, on the slim chance a little tax might be missed
- an income protection claimant theoretically being able to do a job which isn't available to them

Independent response to Sergeant Review of Simple Financial Products

Please remember small businesses

Whilst protection of all shades is vastly undersold, it is especially so where most needed – amongst small business owners (and their employees). Whilst their needs are covered as well as the general public's needs in most of what is proposed there are two contexts worth bearing them particularly in mind:

- for income protection, the extra difficulty for the self-employed of getting adequate cover – both in amount and definition
- the business protection gap as a percentage shortfall of cases needing to be covered is much greater than for personal/family cover and with even greater social and economic ramifications, so my plea is that after income protection, a simplified business protection solution be considered for micro-businesses...I have suggestions.

Products should do what it says on the tin – key to trust

Currently what it says on the tin is not achieved for protection:

What it says	Reality
It pays out when you die	It pays out usually several months or even over a year after you die
It pays out if you are unable to work due to ill-health	It pays out if you are unable to work due to ill-health – maybe . That's if we are prepared to believe you haven't fooled your doctors and we can't think of a pretend non-existent job you could in theory do instead

So more strength needs to be given in this review to focus on the claims end of the process.

We are promoting the uptake of protection on the basis of peace of mind that financial difficulties arising when the medical worst happens will be solved or at least softened by the insurance. People need reason to trust that what they expect to be paid will be paid and when they expect it.

What happens at claim is therefore the most important consideration if this premise is to be consistently borne out by reality. **Currently it is not.**

So this end of the process needs as much thought as the purchasing end for the insurances, whereas the interim report looks a bit thin on addressing the pay-out side – which for life cover is down not just to insurers but also the government/Treasury as regards probate and tax complications.

Inheritance tax on pure protection is an unwarranted and damaging distraction

For the vast majority of the 19.8m target audience, IHT is an irrelevance. However, because of its theoretical relevance to a minority, in disclosures about the product far too much air space is given to the subject, with knock-on reference to the (almost) universally mis-understood area of trusts. It adds complication, but little value.

But much more importantly, the area of damage is in the delays of months (and even years) bereaved families unexpectedly find they have to endure before their financial distress is eased. The key remaining reason for this delay is down to the (low) possibility there may be an inheritance tax charge (low-ish in the greater scheme of things) to be gleaned.

Reducing (or removing ideally!) the need to touch the topic for both personal and business protection would be a significant ingredient in simplifying life cover and making it do what it says on the tin: “**when** you die, we pay”. Treasury concerns about this may be balanced, I hope, by the counter-balancing benefits to be gained.

Independent response to Sergeant Review of Simple Financial Products

Life cover product design

Q5: Life cover product design comments:

Chosen representative: *Use of this term makes it unclear in what capacity the proceeds are to be received – if as beneficiary, better to say so, if not, then what is the representative supposed to do with the money? Both routes have challenges, beneficiary being the simplest, but both are much preferable to the current default to legal personal representatives which leads to payment delays for the majority of cases without a trustee of the policy.*

Although I'm finding the terminology ambiguous, I trust and hope the reference to "chosen representative" reflects an intention to ensure policies can be paid out promptly to someone chosen under the terms of the contract ("nomination contract"), rather than by the (somewhat random in practice and generally unhelpful) application of the laws relating to trusts, succession, probate and inheritance tax.

The "nomination contract" concept is one I conjured up to avoid the need for (but not preventing) the use of trusts to ensure prompt pay-out of life cover. I raised the idea with Mick James of RGA and ILAG who has been hugely instrumental and diligent in taking it forward. My vision is to have available statistics also support the proposition "when you die, we pay" with 98% of claims paid out within a month of notification of death. Or even 90% would be a good improvement on where it has been.

Whilst insurers have been making changes to improve the situation, government help is needed to avoid the probate block. This means tackling the issue of inheritance tax, which is covered further below in the additional points section.

Additional features: *It makes sense to exclude the additional features you list. It is disappointing but expedient to have to exclude terminal illness benefit.*

This is something that might better be worked on separately through the ABI, to get right across the board wherever offered. But if such improvement was achieved and standardized it would be worthwhile to consider later as an included feature of the simple life product. Here's why:

Terminal illness cover is the feature which offers most real life benefit, when your physician has to break the news that you should prepare for having only a few months left to live. But unfortunately as currently presented, the terms of the cover compared to how medical professionals have to deal with patients can lead to false hope of payment in a number of cases. I say this from personal experience of being informed at the original diagnosis that the odds of one year survival looked worse than 50/50 and the dilemmas this presented for the potentially final life choices to make, most having financial impacts. It was only "insider" industry knowledge that made me aware that I needn't hope for my terminal illness cover to pay out. However, a recently televised similar case high-lighted the heart-ache for the woman and her family who reasonably thought it would.

As it turns out, we have both beaten the odds so far, but without the power of clairvoyance, that was of little help when the decisions had to be made. I'm lucky I didn't decide to spend my savings on getting my sister and brother-in-law back over from Australia and funding them suspending their jobs. I'm also lucky I didn't face a dying breath with that as a regret.

The ABI definition of terminal illness is:

A definite diagnosis by the attending Consultant of an illness that satisfies both of the following:
The illness either has no known cure or has progressed to the point where it cannot be cured; and

Independent response to Sergeant Review of Simple Financial Products

In the opinion of the attending Consultant, the illness is expected to lead to death within [the earlier of] 12 months [and the remaining term of the cover].

For someone who's told the prospects are more likely they won't last the year and there's either nothing more that can be done to improve that, or that those are the odds even with what remains to be done, it seems perfectly clear the cover is payable.

For an insurer, it's perfectly clear it's not (yet) payable until everything's been done, any further information becomes available, if there is any, and if so, with a revised prognosis, even though that may not happen until 9 weeks later as in my case, out of the possible 3 months I may have had of life. Further, the prognosis needs to be significantly worse than 60% likelihood of death, i.e. "more likely than not" is insufficient. To insurers "expected" in this context (though hard to pin anyone down to a specific percentage probability and even harder to get everyone to agree the same number) means "almost definitely". So more like 90%, usually.

So, over-simplistically, the **expectations gap** can be calculated to account for:

- **Disappointment** (as an insurer might say) or rather, devastating shock (as the claimant may actually feel), in up to **80%** of claimants who've been told they are more likely than not to die within the year
- **Delay** in payment through as much as the first **70%** of the time the person fears they may have left

There will be several reasons these figures won't show up as a major issue in insurer claim stats – not least because a surprising number of people don't even realise they've got this cover. But also this simple calculation doesn't take into account actual distribution of probability rates amongst the affected class, nor the way consultants will generally communicate with patients and various other factors.

The main point of the figures is just to make more tangible the actual scale of expectations mismatch when they do occur....not that often relatively, but if it's you affected that's a 100% hit rate! So much for peace of mind.

The options for improvement are:

Ideally: A more generous yardstick for pay out so that odds of worse than 50/50 do lead to a pay – out. This means higher premiums – but not as big an increase as incurred from any one of the gender equality changes or new internal fund taxation or the costs of regulation which currently have to be factored in to premiums.

As a compromise: A change to partial pay-out eg 20% to allow for a more generous yard-stick without increase to premium rates – but this adds complexity of understanding, systems and admin

As a minimum: A much more explicit explanation of the likelihood and timing of pay-out – whether or not the above get done. And especially to make clear how "expected" is measured – not just a balance of probabilities.

Suicide exclusion: *Yes, reasonable within 12 months, but is it even necessary, as it is in a small way counter to the aims of simplicity? Unless it is necessary to industry acceptance of the product.*

Many policies no longer include this for a number of reasons. To have it there at the choice of individual providers is counter to the appearance of comparing like for like (though in reality it makes little difference). To have it there as standard across all simple policies seems like the addition of a perceived less beneficial feature and slight element of complexity.

Independent response to Sergeant Review of Simple Financial Products

Reasons for no longer including this standard exclusion are:

- It is of little practical value as proving suicide is notoriously difficult for insurers
- In the rare cases of blatant provable abuse of effecting cover with the intent and successful execution (!) of suicide, recourse to general law is available to insurers protecting them from insured's purposely bringing about the very event insured against (oh, and fraud)
- It's a very penal exclusion to punish the bereaved family with. It's already bad enough that not only they've lost their loved one, but they have the additional pain of knowing it was through suicide (or hurt and anger at the belief some bureaucrats are wrongly asserting that to be the case to prevent pay out). So to make sure they're pretty much destitute into the bargain is not the sort of tack to make all concerned feel proud. Nor even the threat of it by including the exclusion in the first place.
- It's not possible to establish the extent to which presence of the exclusion acts as a deterrent to effecting cover in anticipation of and carrying out suicide

Having said all that, it's worth keeping it if industry acceptance can't be gained without it!

Non-standard exclusions: *It is unclear whether these are to be permitted.*

As individual underwriting approaches will be permitted to be applied, it would be helpful to clarify whether non-standard exclusions may also be applied (individual to the life covered). Or is suicide the only exclusion contemplated, whether standard or non-standard?

Calls caveats: *The threefold repetition in the draft policy of "We may record and monitor calls. Call charges will vary." imparts an unfortunate and avoidable flavour to what is intended as a trust-generating product.*

Possible reading between the lines by the non-trusting public:

- "We do this (record calls) and keep telling you about it because otherwise we expect you to lie"
- "We are going to sting you for as much as we can get away with if you bother us by calling and you won't know how much you're spending. Something to ponder while you're on hold in our queues listening to Vivaldi. Ha!"
- "We plaster these caveats everywhere because we care more about covering our own back and making it harder for you to spot the info you're looking for than telling you something useful."

Options for improvement are:

- Instead say "We may record and monitor calls to improve our standards." So people are still warned what they say can go on record, but with less opportunity to infer an accusatory implication. This covers the whole gamut of reasons it's good to record calls – including being able to refer back to what was actually said if there is any dispute and ensure payment is not made for false claims.
- Say it just once under a separate section after How to..., headed "Calling us". To be in right place, this needs to come before the FSCS section, which would benefit anyway from being promoted to a full final section of its own, not a "how to". It's more of a point of information about the external-to-policy-terms protection available in an unlikely event the insurer can't do its bit.
- Don't charge for service calls, then there's no need to say call charges may vary. (Charges related different telecommunications services are nothing to do with the policy.) And then there's another levelling of the playing field, as policy pricing can't be artificially reduced by shifting service charges to premium rate call lines. Charging for service calls (or threatening to, as this caveat does) is seen as a discouragement to call and an opportunity to extract money from customers at a rate they have no control over – stop it and you've made another advance in regaining trust.

Independent response to Sergeant Review of Simple Financial Products

Minor draft policy points

Premium collection: As there's usually a practical and rules-related delay for starting collection by direct debit, either cover start has to be delayed (regrettable) or some amendment seems needed to "We'll collect from start date". Complaints occur when customers don't realise the likelihood of first payment being caught up with the second.

Cancel this policy: This section doesn't actually say "how to..." yet.

Claim requirements positive spin opportunity:

- "We will require the death certificate of the person covered and the policy schedule and any other documents we may reasonable (sic) request" ...
- **reads less bureaucratically** ("we are all about rules, will make them up as we go along and will require you to obey them now we have power over you")
- **if tweaked to** "We will need the death certificate of the person covered, the policy schedule and possibly other documents to be able to settle your claim."
- in other words ("we'll only be asking you for things that are important to sort it all out")

The "Don't send it and we won't necessarily pay" sentence that follows ensures the teeth are still there to insist on what's needed. And it doesn't sound so bad, having prefaced it with what's needed so nicely.

Income protection

Q7: Product design comments

Early intervention PMI pot

It's more valuable to individuals and society to enable people to carry on earning than to replace earnings...and cheaper.

Incapacity persisting beyond 6 months has a much lower chance of being adequately recovered from. Yet NHS resources are not placed to assist. For the most common causes of claim under protection, the waiting lists to see the specialists who will remediate the problems are typically well over 6 or even 12 months. Physio, pain management, stress management, etc are all overly called on for non-life threatening but potentially disabling and certainly distressing conditions.

And the irony is that a well-designed low tech intervention package can make a huge improvement when applied early in the process and often at relatively small cost compared to many treatments. Also a catch 22 for claimants if it means they can't even get a diagnosis which will satisfy the requirements of their insurer.

5 year benefit period

Still provides meaningful maximum pay-out duration even for longer deferred period cases. Facilitates more accurate price modelling as 5 year is universally used as patient outcomes benchmark in medical studies.

Allows sensible and humane time for claimants to re-design their lives

Distinguishes the cover from PPI

A shorter time is not really that helpful when deferred periods, medical waiting lists, claims to and fro, time to work on improving health, the decision process and opportunity to downsize the family home, time to identify and train for and secure an alternative means of earning are all added to the time-line.

Less than 5 years could leave many more people exposed than is appropriate to the aims of getting them covered in the first place.

Independent response to Sergeant Review of Simple Financial Products

Lump sum end of claim benefit

For permanent severer cases where it seems unlikely the insured will be able to return to earning near the benefit level a lump sum benefit of say 5 times the benefit level seems a more humane and palatable way to terminate income replacement.

Musculo-skeletal /mental illness and stress-related or non-specific chronic pain syndromes could be excluded to improve affordability as their personal risk would be more importantly mitigated by availability an early intervention PMI pot.

It would be important to establish non-eligibility or potential eligibility for the lump sum early in the claims process.

Do what it says on the tin:

Own job: Own occupation needs to mean **own job** and under the circumstances the current, not a mythical, employer is actually prepared to apply, regardless of what the claims team imagine they ought to apply. This turned out to be an issue in my own claim, much to the amazement of those who know me and my doctors, even though having had the discussion with claims experts in the context of product design, I had been assured the own occupation would never be used against claimants in that way.

Even if there are other jobs being advertised which the claimant might physically be capable of, the chances of being successful in taken on for such a new role are minimal (ignoring the competition for jobs issue) but just due to the fact that the claimant is currently not at the current job because....err, they are too ill to do that job.

(And of course it's old news to point out people need to be aware of the real-life implications of obtaining only the lesser definitions of incapacity preventing performance of "own or suited occupations" or "any occupation" – the latter being an unfortunately ambiguous definition which can be taken either way.)

Benefit of the doubt claims stance:

It's just inappropriate to expect trust where the claims process goes beyond a balance of reasonable probabilities and opinion of the medical professionals involved, to place the onus of proof on claimant as if in a court case, but where the insurer is prosecutor, judge and jury. Not so much an issue where there are physical medical tests which can give a more incontrovertible indication of the root of the illness or incapacity. Hard luck though if you don't fall into that category – as do a large proportion of claimants due to the nature of the more common causes of impairment.

Again, my own case served as an eye-opener to me. But not to any of the medical professionals involved with me. More than one said "We see this time and time again."

Specifically, the opinions of these professionals and their bases of the decisions for treatment all of which indicated a valid claim, was dismissed as not being to be relied in evidence to support the claim as these people "are the advocate of the patient". This seemed to justify the CMO in dreaming up his own diagnosis and appropriate treatment without even meeting me. A clairvoyant and all-round genius with his wide-ranging knowledge superior to the specialists involved. (After months of wrangling and stalemate, a prompt about-face and pay-out followed receipt of a copy of my submission to the Ombudsman.)

To be fair to the insurer involved (not my ex-employer I'm pleased to make clear!), this isn't the whole story and I mention it not to "have a go", but simply to demonstrate first-hand experience

Independent response to Sergeant Review of Simple Financial Products

of weaknesses in the product and process, which apply to everyone. These are general weaknesses which have been identified by the Income Protection Working Party, but many of us close to it in the industry, these have either become widely accepted as normal and appropriate (by claims and actuarial managers) or not appreciated to exist (by marketing – who design and describe the product...oops, and compliance managers, who police descriptions of the product).

A product with catch-22 problems built in deserves not to be trusted by the public. (But then admittedly it's difficult to design a no catches product that can be afforded by the public...another catch 22.)

Q7: Can S.I.R. be made sufficiently straight-forward to “qualify”?

Yes, it has to be.

As the Swiss Re Health Watch numbers show, the gap is even greater than for life cover and that's worsened over the last 10 years. Yet the social importance measured by impact on individuals and dependence on welfare is much greater than for the life cover gap. Especially as the welfare safety net has become less and less safe.

There are plenty of grounds for arguing “no”, which is why this most socially important insurance has failed to reach the coverage it should and why the Income Protection Task Force is still needed after more than 5 years concerted effort. Even if you receive a lot of “no”s, that should not be permitted to prevent the attempt to at least make progress.

So please don't let this become an academic “yes” or “no” debate or nothing will happen and for this product it really must. What matters here is to do as much as is possible to simplify this crucial product sufficiently to improve outcomes for the people who need it.

Exclusion of this key product from scope would mean this initiative will have only achieved the simplification of 3 products which are already pretty simple and whose take up needs less help than income protection, both in scope of shortfall and in social and economic benefit to be gained.

Income protection resources

When it comes to more detailed work on simple income protection, if not already considered, the input of the Income Protection Task Force and of the Centre for Risk and Insurance Studies at Nottingham University Business School would be valuable. But I guess most of you already know that.

Additional points

Some cover is better than no cover

Making sure people get covered and that something actually pays out when expected and needed is more important than whether:

- they paid the cheapest possible price for it (though affordability is important so the January 2013 changes in life fund internal taxation won't help, and gender equalization is a lamentable step away from fairest price for the risk presented)
- they read a pile of disclosures regulation imposed by regulation - the more there is, the less likely even the important bits will be read
- a slim opportunity for a small amount of IHT to be collected might be missed so most bereaved families are without a pay-out whilst the months of the probate process tick by

Independent response to Sergeant Review of Simple Financial Products

- an income protection claimant might be able to do a theoretical job which isn't in fact available to them – better a lesser benefit amount and more generous claims criteria

Please remember small businesses

Whilst protection of all shades is vastly undersold, it is especially so where most needed – amongst small business owners (and their employees). Whilst their needs are covered as well as the general public's needs in most of what is proposed there are two contexts worth bearing them particularly in mind:

- for income protection, the extra difficulty for the self-employed of getting adequate cover – both in amount and definition
- the business protection gap as a percentage shortfall of cases needing to be covered is much greater than for personal/family cover and with even greater social and economic ramifications, so my plea is that after income protection, a simplified business protection solution be considered for micro-businesses...I have suggestions (which I have spared you here!).

Although business owners are often perceived to be well off, though less so currently, the actual make-up and importance of the small business population is quite different to how it is generally viewed. Few people appreciate that:

- Of the 4.5m private businesses in the UK, 99.9% are "SME"s (small or medium enterprises) with large companies accounting only for just under 6,000.
- 95% of government support goes to the larger small (<50 employees) and medium enterprises (50-250 employees), i.e. to less than 5% of SMEs.
- 96% of SMEs are in fact micro-businesses (0-9) employees, with about 75% having no employees - other than the owners
- About 1 in 7 (about 4million) of the adult workforce are running a micro-business and micro-businesses at the start of 2011 had 27% (3.7m) of the employees in the SME sector.
- So over a quarter of the UK work-force of 29m works in a micro-business, both contributing to the economy and taxes, and keeping off benefits.

Business protection itself is also often misunderstood. Apart from the confusion with general business insurance (covering liabilities, property and risks of loss of profits etc of the business) or group insurances to give medical, life or illness cover to employees of the business, the types of life, critical illness and income protection arrangements needed on the owners lives are over-looked, over-simplified or mishandled.

Sometimes this cover can be thought of just as the life cover needed to back a loan for the business. Or more sophisticatedly, "keyman" cover might get mentioned – compensating the business for the losses and expenses of dealing with loss of a key performers input. But least attended to and least well handled is the need to ensure the very survival of the business and financial security of the bereaved family if one of the owners dies. Or just as importantly, when an owner survives a critical illness but can no longer work, to ensure the business survives too, along with the finances of all the owners and their families and employees.

According to the 2010 survey by Scottish Widows:

- About 5% of businesses have keyman cover on death or critical illness although 60% of businesses wouldn't survive their loss and 77% have at least one key person whose loss would

Independent response to Sergeant Review of Simple Financial Products

seriously impact the profitability of the business. So the gap represents 93% of businesses who need the cover. (In the personal market, the gap is probably on 80% of relevant lives, assuming the 19.8m targeted by the review have no group life cover with their employer either.)

- As for exit planning for death or serious illness, the best prepared are partnerships, 52% having a plan (how robust?), compared to 40% of companies and 32% of sole traders (how are they or their families to pay the bills?). But even 43% of partnerships surveyed still didn't even have a partnership agreement in place, in the absence of which under English law the default is that the business dissolves on a partner's death and the assets are to be carved up between their estate and the surviving partner(s).

So wouldn't it be great to do something about it?

Products should do what it says on the tin – key to trust

Currently what it says on the tin is not achieved for protection:

What it says	Reality
It pays out when you die	It pays out eventually after you die - usually several months or even over a year later
It pays out if you are unable to work due to ill-health	It pays out if you are unable to work due to ill-health – maybe . That's if we are prepared to believe you haven't fooled your doctors and we can't think of a pretend non-existent job you could in theory do instead

We are promoting the uptake of protection on the basis of peace of mind that financial difficulties arising when the medical worst happens will be solved or at least softened by the insurance. People need reason to trust that what they expect to be paid will be paid and when they expect it.

What happens at claim is therefore the most important consideration if this premise is to be consistently borne out by reality. **Currently it is not.**

So this end of the process needs as much thought as the purchasing end for the insurances, whereas the interim report looks a bit thin on addressing the pay-out side – which for life cover is down not just to insurers but also the government/Treasury as regards probate and tax complications.

Inheritance tax on pure protection is an unwarranted and damaging distraction

Not only does the possibility of inheritance tax add an irritating complication (including the need for trusts) to what should be a simple product type, much worse it is a major **stumbling block** to opening the way to significantly **improving the average pay-out time** for life policies.

For the vast majority of the 19.8m target audience, IHT is an irrelevance. However, because of its theoretical relevance to a minority, in disclosures about the product far too much air space is given to the subject, with knock-on reference to the (almost) universally mis-understood area of trusts. Plus, the primary idea behind targeting the 19.8m is that the cover is needed to protect families, not to boost tax take.

But much more importantly, the area of damage is in the delays of months (and even years) bereaved families unexpectedly find they have to endure before their financial distress is eased. The key remaining reason for this delay is down to the (low) possibility there may be an inheritance tax charge (low-ish in the greater scheme of things) to be gleaned.

Independent response to Sergeant Review of Simple Financial Products

Reducing (or removing ideally!) the need to touch the topic for both personal and business protection would be a significant ingredient in simplifying life cover and making it do what it says on the tin: “when you die, we pay”. Treasury concerns about this may be balanced, I hope, by the counter-balancing benefits to be gained.

What is suggested here is to exclude the insurance element of life policies from the inheritance tax rule which currently brings those amounts into consideration for inheritance tax by looking at the value of assets just after death instead of just before death.

It is already in the power of the wealthy to do just this by ensuring they place their policy under trust. So it's really not a flood-gates opening suggestion. For those worried about allowing the use of life policies purely for “wealth creation”, well this is how the stable door is already open. It is of no help to make it a matter of theoretical relevance to the masses to whom it's usually not going to apply, but we end up having to try and explain it to them anyway and try to cajole them (ineffectively) to put trusts and trustees in place.

The greatest social and economic good at stake is not to seize every possible chance to find an inheritance tax charge, but to ensure that bereaved families have access to appropriate financial provision at the time they need it – which for peace of mind usually is pretty much immediately.

Whilst moves have been made to improve the time it takes for life policies to pay out since Mick James of RGA and I raised the issue in 2009, there remain 2 legal barriers to ensuring speedy pay-out in the desired 98% of cases.

One is the need for insurers to have someone legally capable of accepting the proceeds without going through probate. This can be achieved by the nomination contract solution put forward via ILAG and which I very much hope is what is envisaged for the simple life cover product, as suggested by reference to paying “your chosen representative”. (For those who still believe “just put it under trust” is the easy solution, this time-tested solution has demonstrably failed in astonishing proportions, not least because even when the trust gets done, appointment and updating of appropriate trustees doesn't. Or someone in the process just makes a mess of it – pretty common too.)

The other barrier is the IHT rule which makes it a slim and socially unhelpful possibility that the policy may attract IHT, meaning the Treasury/HMRC would not be happy for insurers to pay-out without awaiting probate.... unless the insurers wanted to step up to pay any missed tax. Can you imagine risk, compliance, claims, actuarial, legal and finance managers queuing up to sign that one off? (And yet jointly owned policies can be paid out immediately, despite a possible tax charge relating to half the value of the proceeds in the case of unmarried couples. Not that I'm suggesting that should be stopped!)

Here are some numbers to put the matter in perspective:

- No married women and only 5% of married men liable for IHT in 2009/10 had any taxable life insurance. So no insurance or insurance in trust. (Only 6% of all life policies are under trust.)
- Total pay-outs per deceased with cover averaged 10% of gross assets, ranging from £75k to £103k, in each age group of the sexes, except under 45s.
- For under 45s, males averages were £171k and females £191k (these groups were small: 41 and 21 cases). For this younger age group, policy proceeds accounted for 14% (men) and 23%

Independent response to Sergeant Review of Simple Financial Products

(women) of their gross assets. It seems appropriate to see higher sums assured at these ages, implying suitable provision for dependants, not “wealth creation”.

- Among the wealthy whose families are otherwise catered for, the main reason for effecting life cover is to be able to pay inheritance tax without liquidating other assets of the estate. What’s wrong with that?
- Overall, the benefit to the Treasury of applying IHT to life policy pay-outs accounted for 3.3% ie £79m of the total £2,391m, IHT paid in 2009/2010. Total tax-take for that fiscal year was £477.8bn. So IHT on life policies contributed 0.017% to the public finances. What can’t be deduced from the reported tax figures is what portion of the policy proceeds came from policies with no surrender value. ie valueless until death. So all we can say is that £79m is an overstatement of the amount at stake under the proposal to exclude the insurance element.
- If the Simple Products initiative was to be successful in closing the estimated life cover gap of £2.4 tn, for 19.8m people to the extent of 5% up to the moment of death within the term, there would be an extra £120bn released into the hands of families/dependents who need to spend it. And when spent it nearly always gets taxed. Say conservatively the resulting tax take is at a combined rate of 33%, there’s an additional £40bn over time (40 years?) towards the public finances (plus hopefully a number of cases saved from drawing on benefits thanks to the payouts.) It would take 506 years of IHT on life policies collected at the current rate to reach that £40bn.

So would it be such a big deal to exclude the actual insurance element of life policies from the IHT net?

But as a perceived (though hardly ever relevant) additional encouragement to take out the life cover needed, to simply say “proceeds are tax free” (whether the simple or non-simple version) and say little about trusts, wouldn’t that be simply lovely?

Parting shot

If you have found any inspiration or even enjoyment out of reading this, then I have not wasted my time.

Thank you for reading this far.

Independent response to Sergeant Review of Simple Financial Products

Appendix of handy stats

I nearly deleted this, so don't bother looking if you're not interested.

These are just some statistics I found helpful to set my own thinking about life cover in context, so I thought it might be helpful to a few of you too. Apologies for any inadvertent errors...I'm not the ONS after all.

- Av house prices: Greater London 2012 £458k, SE £280k to £150k poorer areas of UK
- £325k nil rate band 2012/13,
- 2011: 71% of households, 18.6m, include > 1 person. 773k households with >1 person aren't families (couple or parent child relationships). All married = 12m, married + kids 4.5m (down .3m since 2001) All co-habiting opposite sex 2.9m, inc. unmarried w kids 1.1m (up .3m), lone parents 2m (up .2m), 3.7m households have adult children (4.7m) living with parent(s)
- 2009/10: 66% own home, 14.5m (31% own outright, 34% own w. mtg)
- 6% of policies under trust
- 2010/11, IHT raised £2.7bn on 16k estates
- 2007/8, 3,600 estates >£1m raised £1.8bn tax, being 58% of all IHT
- Given about 1.5m life policies are taken out each year (ignoring £3.5k guaranteed acceptance WL for funeral costs cases) and average term policy duration is about 5 years, and average number policies per life might be say 1.5, crudely, it can be estimated 5m UK adults are covered by a personal life policy (up to 17% of working population if all lives covered were workers, which they aren't). Compared to the 19.8m adults estimated to need the cover which don't have it. So, the life cover gap comprises 80% of individuals who are expected to need it.
- But for businesses the shortfall (on a small survey of 500 businesses), the gap looks like 94%.