US Life Insurance 101

Life Insurance Defined

A protection against the loss of income that would result if the insured passed away. The named beneficiary (ies) receives the proceeds and is thereby safeguarded from the financial impact of the death of the insured.[2]

At the highest level, life insurance falls into one of two camps:

GROUP

Group insurance is just what it implies: insurance coverage provided to a group of individuals. It is priced based on the risk of the group, not the people in the group. The most common example of group is insurance provided by an employer. Group is not portable as new members join and current members leave. You only benefit from this coverage while you are in the group. This benefit is typically reviewed annually (both the level of benefit provided and the carrier selected).

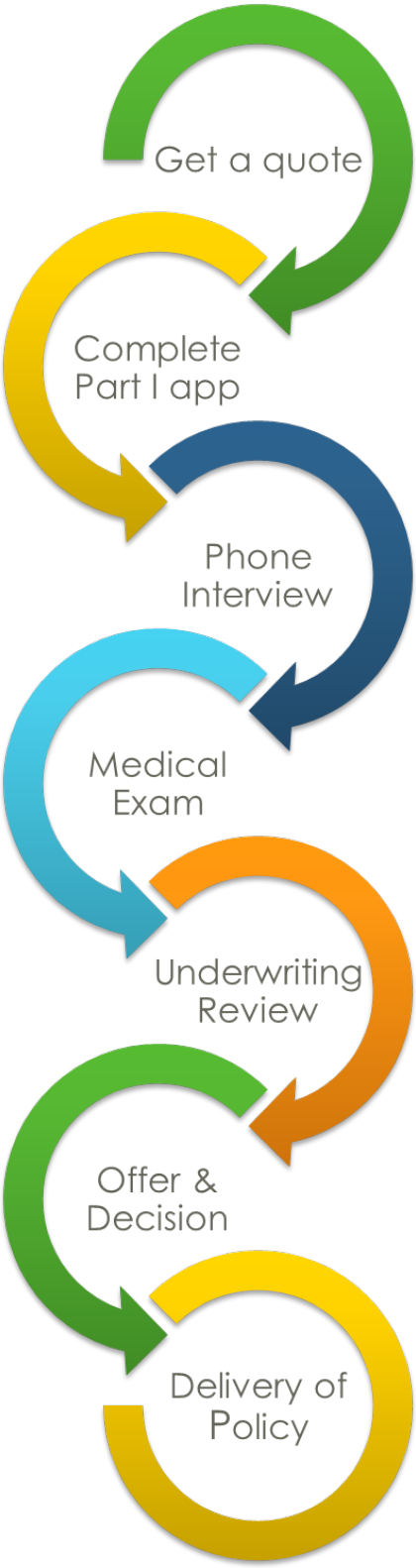
INDIVIDUAL

Individual insurance is coverage for one particular person. This type of policy is priced based on the health and risk of the individual. For this reason individual insurance is beneficial when the individual is in good health. An individual policy is potentially out of reach if the individual is in significantly poor health. Individual coverage is typically a longer term product which is a large advantage if the health of the insured changes dramatically. Once covered, the policy remains in effect provided the premium payments remain current.

Group vs. Individual Life Insurance Coverage[4]

	Group	Individual
Cost	▪ None, if part of employee benefits package ▪ Additional coverage at favorable group rate may be acquired without health assessment (generally though employer) ▪ Unisex rates	▪ May be similar to group, but based on individual underwriting results ▪ Rate can be locked in over a prespecified time ▪ Generally, the younger/healthier you are, the more favorable the pricing ▪ Generally, gender-specific rates
Coverage Limits	▪ Employer determines coverage limits and eligibility ▪ Less ability to customize ▪ For employer paid, coverage is generally minimal ▪ Possibly two or three times salary ▪ May not cover full life insurance need	▪ Coverage tailored to the individual based on needs and health issues ▪ Can add riders at added costs
Underwriting Requirements	▪ No individual health assessments for employer-provided coverage; may be required for optional coverage	▪ Individual health assessment helps determine the price for coverage, or whether insurance is offered
Portability	▪ Generally, none; when you leave your job, coverage typically ends or rates increase significantly	▪ Even if you change or lose your job, your coverage is not affected

The Application Process



Consumers can seek an insurance quote through a broker directly or through various tools that are digitally accessible. A quote begins to assess the consumer's needs in terms of what type(s) of policies may be suitable.

Based on the quote, consumers proceed with completing the Part I application. The type of data collected here include things like name, address, date of birth, driver's license number, beneficiaries, and some initial health questions such as smoking and drinking.

A phone interview may be scheduled with an agent to address any missing information and collection of additional information.

Depending on the type of insurance product the consumer is applying for, a medical exam and a donation of fluids (blood and urine) may be required. This will take place in either the consumer's home, a place of business, or a network lab.

After the medical exam results are available, the carrier's underwriting team will review the consumer's data to determine whether the consumer is insurable or not. If they are insurable, what rates do they qualify for (standard, preferred, etc.)?

When the insurability of the consumer has been fully assessed, the insurer, or carrier, is in a position to present a policy offer back to the consumer. At this point it is up to the consumer to accept the policy offer or decline.

Regulation requires that a paper copy of the insurance policy be signed. An executed copy is then delivered to the consumer once it is accepted, fulfilled, and in-force.

Why should I buy Life Insurance?[5]

Many financial experts consider life insurance to be the cornerstone of sound financial planning. It can be an important tool in the following situations:

1. **Replace income for dependents:** If people depend on your income, life insurance can replace that income for them if you die. The most commonly recognized case of this is parents with young children. However, it can also apply to couples in which the survivor would be financially stricken by the income lost through the death of a partner, and to dependent adults, such as parents, siblings or adult children who continue to rely on you financially. Insurance to replace your income can be especially useful if the government- or employer-sponsored benefits of your surviving spouse or domestic partner will be reduced after your death.
2. **Pay final expenses:** Life insurance can pay your funeral and burial costs, probate and other estate administration costs, debts and medical expenses not covered by health insurance.
3. **Create an inheritance for your heirs:** Even if you have no other assets to pass to your heirs, you can create an inheritance by buying a life insurance policy and naming them as beneficiaries.
4. **Pay federal "death" taxes and state "death" taxes:** Life insurance benefits can pay estate taxes so that your heirs will not have to liquidate other assets or take a smaller inheritance. Changes in the federal "death" tax rules between now and January 1, 2011 will likely lessen the impact of this tax on some people, but some states are offsetting those federal decreases with increases in their state-level "death" taxes.
5. **Make significant charitable contributions:** By making a charity the beneficiary of your life insurance, you can make a much larger contribution than if you donated the cash equivalent of the policy's premiums.
6. **Create a source of savings:** Some types of life insurance create a cash value that, if not paid out as a death benefit, can be borrowed or withdrawn on the owner's request. Since most people make paying their life insurance policy premiums a high priority, buying a cash-value type policy can create a kind of "forced" savings plan. Furthermore, the interest credited is tax deferred (and tax exempt if the money is paid as a death claim).

Life Insurance Fraud

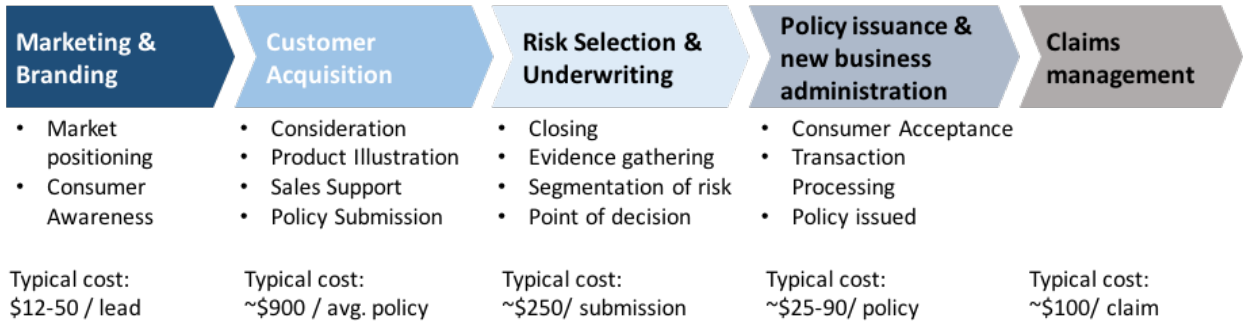
Below are the types of fraud impacting the life insurance industry.

SELLER FRAUD[2]			
Ghost Companies: In the ghost company scenario, policies are issued and premiums accepted from policyholders, but the company underwriting the policy isn't legitimate and often doesn't exist. These outright frauds are a team of high-pressure scam artists dial likely victims to sell them false policies. Unfortunately, the fraud isn't usually discovered until someone tries to file a claim on the policy their family member thought was in effect, in the event of his or her death.	**Premium Theft:** The premium theft scenario is when the insurance rep accepts premiums, but doesn't submit them to the company underwriting the policy, thus invalidating the policy. In this case, the agent essentially pockets the money. Premium theft has become less of an issue as more companies have moved towards direct deposit models, but it is still possible in some cases.	**Churning:** This situation is where the insurance rep advises the customer to cancel, renew and open new policies in a way that is beneficial to him or her, instead of beneficial to the client. This type of insurance fraud often targets seniors and is driven by the agent's desire for larger commissions. Churning keeps a portfolio constantly in flux, with the primary purpose of lining the advisor's pockets.	**Over or Under Coverage:** Similar to churning, under or over coverage occurs when an insurance rep convinces customers to buy coverage they don't need, or sells a lesser policy and represents it as a complete policy. In either case, the rep is trying to maximize commissions and ensure the sale, rather than focusing on meeting the client's needs.

BUYER FRAUD[2]			
Post-Dated Life Insurance: Post-dated life insurance refers to a policy that has been arranged after the death of the person being insured, but appears to have been issued before death. This type of fraud is usually carried out with the help of an insurance agent. It is also one of the easier types of fraud for insurance companies to detect, because record keeping has become more stringent.	**False Medical History:** Falsifying medical history is one of the most common types of insurance fraud. By omitting details such as a smoking habit or a pre-existing condition, the buyer hopes to get the insurance policy for cheaper than he or she would have otherwise been able.	**Murder for Proceeds:** There are two versions. In the first, the insured doesn't know they are insured and are understandably surprised to be murdered. In the second, the policy is legitimate and was taken out in better times, however, financial hardships lead the perpetrator to decide that killing his or her spouse/family member/business partner, for the money, is the best way out of the problem.	**Lack of Insurable Interest:** Insuring people you shouldn't be insuring, in hopes that they will die, constitutes fraud. Insurance is founded on the idea of protecting people from financial loss, so using it to gamble on lives for a financial gain is a perversion of the system. This includes viatical settlements, which combine non-insurable interest with falsified policies taken out on the terminally ill.
Suicidal Accidents: Financial hardship can lead otherwise rational people towards murder. The same factors can lead people to commit suicide in a way so it looks accidental. This constitutes fraud. It is an intentional act for the purpose of collecting benefits, and would not have occurred if those benefits did not exist. This can be a very difficult one to detect, as the medical examiner has final say in accidental death. Even if it is clearly a suicide, the claim centers on the state of mind, rational or not, at the time of suicide.		**Faking Death or Disability:** Many life insurance policies have riders for disability, creating the temptation to fake one to get the payout. However, some people take it a step further and fake their own deaths. In both cases, the fraudster has to deal with the possibility of being discovered through an investigation.	

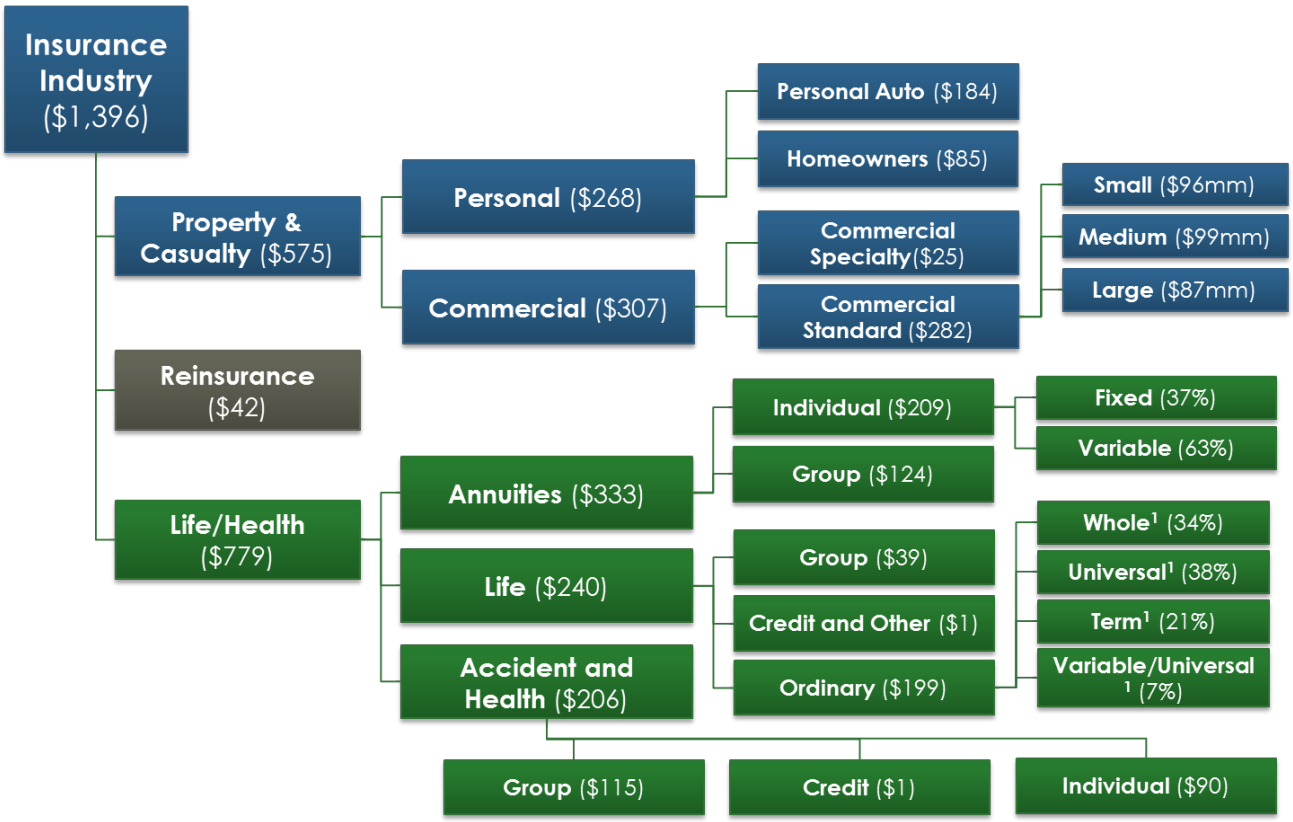
Insurance Agent Based Value Chain

Today's value chain utilizes the same laborious application workflow that has been used for decades. However, consumers are not all that interested in stacks of paper and lengthy, opaque processes. The application process as we know it is a thing of the past, and at this point, re-scripting the full customer experience is table stakes. Thus, the value chain is becoming a disaggregated value chain with niche competitors specializing in pieces of the value chain.



U.S. Insurance Industry Structure (2013)

Gross premium by major product line ($ bn)



Industry Facts

Insurance Information Institute

The Life/Health Insurance Industry[5]

- Whether measured by premium income or by assets, traditional life insurance is no longer the primary business of many companies in the life/health insurance industry. Today, the emphasis has shifted to the underwriting of annuities. Annuities are contracts that accumulate funds and/or pay out a fixed or variable income stream. An income stream can be for a set period of time or over the lifetimes of the contract holder or his or her beneficiaries.
- Nevertheless, traditional life insurance products such as universal life and term life for individuals as well as group life remain an important part of the business, as do disability income and health insurance.
- Life insurers invest primarily in corporate bonds but also significantly in corporate equities. Besides annuities and life insurance products, life insurers may offer other types of financial services such as asset management.

Life Insurance Ownership[5]

- Fifty-seven percent of all people in the United States were covered by some type of life insurance in 2014, according to LIMRA's 2015 *Insurance Barometer Study*. Nearly one-third of Americans said they need more life insurance in 2015, as reported in the LIMRA study. Other findings from the 2015 report include:
  - Fifty-four percent of Americans say they are unlikely to purchase a life insurance policy within the next year. Sixty-five percent said that they have not purchased more life insurance because they think it is too expensive, yet 80 percent of consumers misjudge the price of term life insurance.
  - Millennials overestimate the cost by 213 percent and Gen Xers overestimate the cost by 119 percent.
  - The most common financial worry among consumers over 25 years old is being able to afford a comfortable retirement. Consumers 25 and under are more concerned with paying monthly bills.
  - Only 13 percent of Americans own long-term care insurance; 26 percent own disability insurance.

Distribution Channels[5]

Life insurance was once sold primarily by career **life agents**, captive agents that represent a single insurance company, and by independent agents, who represent several insurers. Now, life insurance is also **sold directly** to the public by **mail**, **telephone** and through the **Internet**.

Miscellaneous Insurance Facts

The middle market study according to LIMRA[6]:

- This study defined the middle market as adults in U.S households ages 25-64 with household incomes of $25,000 to $99,999.
- 50 million households make up the middle market. Of that population, they estimate that **35 million are underinsured**. It is estimated that there is a **$10 trillion coverage opportunity** in the life space to reach this market.
- There are four key reasons why this opportunity exists:
    - Industry has failed to establish coverage as a priority,
    - There has been no cost-effective mechanism to solicit this market,
    - Eliciting a consumer at the time they are shopping is not well understood, and
    - The value proposition of life insurance has not been well communicated.

Why don't people buy life insurance? *(see Appendix: The Periodic Table of Emotions)*

- Financial: It costs too much.
- Education: Don't understand product or needs.
- Procrastination: Not an urgent need.
- Sales Aversion: High-pressure tactics.
- Privacy: reluctance to share medical information.
- Lack of Need: Other sources of financial protection.
- Short Sighted: Focused on immediate needs.

Most American still buy life insurance in person – 67% in person, 22% direct, 11% combination of in person and direct (Source: LIMRA *Trends in U.S. Life Insurance Ownership*)

$29.50 per month buys enough life insurance to pay off the average U.S. mortgage (Source: RGA Term Market Update Q1 2014)

The middle market has not been effectively reached by the life insurance industry (Source: McKinsey *Winning in U.S. Life Market*)

Notes