Striking the Balance – Underwriting Between Regulation and Digitisation

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The beauty of underwriting in the Life/Health insurance sector is that it never stays the same. The process of selecting and assessing risk is constantly evolving.

Having said that, the insurance industry in general is not considered particularly fast-changing or innovative. Thus, only a small fraction of the developments is being driven by the industry itself. Developments in other sectors, however, can have a significant impact. For example, this is true of advances in clinical medicine and transformations in healthcare systems and occupational trends, as well as political and legislative decisions.

Underwriting trends driven by the industry

In recent years, the insurance industry has been more proactive in implementing change, with a special focus on the application and underwriting process. This trend has been fuelled by the increasing digitisation of the industry and the need to adapt to new, "digital" generations of potential customers.

In the Life/Health sector, significant effort was put into simplifying the application process, i.e. making it easier and more comfortable for applicants to get a quote and eventually the insurance cover they apply for. This effort was made in response to constant criticism that medical underwriting questionnaires are cumbersome to fill out, asking overly intrusive questions, and that applicants need to wait too long for their underwriting decision.

The most important changes are:

- The number of application questions has been reduced to a minimum for pre-defined target groups. This was done by either relaxing risk selection, i.e. removing some of the questions, or rephrasing the questions so fewer questions suffice to collect the same amount of information.
- Accept/decline approaches have been implemented. This means applicants will be placed into two categories based on a few, easy-to-obtain criteria to allow an immediate decision.
- Non-medical limits have been increased to avoid delays in the application process, as fewer applicants need to provide medical evidence or undergo additional tests.

Content

- Data from external sources such as wearables, apps, or socioeconomic information has been incorporated into the process to replace or supplement some of the application questions.
- Underwriting software is increasingly being used, again speeding up the process by allowing immediate underwriting decisions at the point of sale for the vast majority of applicants.

These measures have been implemented by insurers across the globe in a very similar fashion. They have been well received as they have vastly improved the customer experience.

Underwriting trends driven by regulation

While the insurance industry has been busy improving processes as described, another trend could be observed that may at first glance seem surprising considering the industry's recent efforts.

For several years, regulatory authorities have focused on the application and underwriting process and put an increased emphasis on underwriting decisions. New pieces of regulation have been implemented globally at high frequency, regulating nearly every step of the process. These pieces of regulation all have their own nuances, but the underlying themes are strikingly similar across the globe.

Communication of underwriting decisions

Some of these changes have added to the workload of insurers – and more specifically underwriters – but will have limited impact on the actual risk selection. These are regulations that focus mainly on how the underwriting decision is being communicated to the applicant, e.g. when:

- Insurers are required to explain underwriting decisions to the applicant upon request; or
- Insurers are required to provide the evidence their decisions are based on to the regulator, or an authority appointed for this purpose. The evidence will then be scrutinised to see whether it is fit for purpose, up-to-date, and whether it supports the underwriting decision in that it is proportionate to the individual risk.

These regulations do not change insurers' work processes or their underwriting philosophy, but may in individual cases result in a modified, e.g. more favourable than intended, underwriting decision if the respective authority does not approve of the insurer's initial assessment.

Restriction of mitigation measures

On the next level, things get a bit more serious, as there are aspects of regulation that restrict the insurers' choice of risk-mitigating measures, e.g. when:

- Insurers are not allowed to decline any application but always have to offer terms, no matter how high the risk;
- Insurers are not allowed to exclude parts of a risk, i.e. use individual exclusion clauses, or incorporate general exclusions in their terms and conditions; or
- Insurers are not allowed to decline certain medical conditions per se but only after careful consideration of the individual application.

All these measures restrict insurers in the way they do the underwriting as they may not be able to compensate the risk they are taking in their preferred manner. Nevertheless, they may still apply terms they consider adequate for the risk to be insured.

Restriction of underwriting procedures

On yet another level, this is no longer the case. Some of the more drastic recent regulatory developments prohibit insurers from applying their standard underwriting procedures and leave them with no choice but to either accept risk without compensatory measures or not offer terms at all.

For example, in some regions and for a certain part of the business (usually, but not always limited to certain benefit types, sums insured and age groups):

- Insurers are no longer allowed to do any medical underwriting;
- Insurers are required to apply loadings that have been defined by the regulator; or
- Insurers are required to ignore certain medical conditions altogether.

The most intrusive recent regulation related to Life/Health underwriting is probably the Right to be Forgotten (RTBF) which is currently being implemented in the EU and has already started moving beyond it (see Underwriting Focus 2/2022). The RTBF is aimed at securing access to mortgages, loans and insurance and gives applicants the right to "forget" parts of their medical history.

It is usually limited to cancer which is to be forgotten some years after the end of active (= curative) treatment, but the RTBF has already been extended to other diseases, e.g. diabetes, HIV infection, and hepatitis C, and can be expected to disrupt the industry in the affected markets.

These requirements are in stark contrast to the way Life/Health insurers price and underwrite their business and the potential impact on insurers' risk selection is significant. While most of the previous examples can be considered manageable, this latest category of developments is worrying.

Why is this happening?

As an industry, we need to be asking ourselves why all of this is happening, especially when we have already turned the focus onto our customers and improving our service to them.

Despite all our best intentions, the regulatory activity suggests we are not (yet) doing (well) enough. The common themes of current regulation are treating customers fairly and avoiding discrimination, maximising access to insurance and other financial services for as many people as possible, and being transparent and communicating openly with customers. While these are objectives our industry should be buying into, the perception seems to be we are not.

When we look again at the changes implemented by the industry, one thing needs to be conceded: while the modifications have improved customer experience, not all applicants have benefited equally from them.

Accept/decline approaches, for example, have an inevitable drawback: to keep premiums low and appealing for low-risk applicants, the acceptance criteria need to be defined more strictly than with full underwriting, resulting in more applicants being rejected. In addition, a simplified process does not generate sufficiently detailed information for the assessment of high-risk applicants, e.g. applicants with a history of severe medical conditions.

To avoid unnecessarily rejecting such applicants who would otherwise be insurable, insurers can choose to follow up on initially declined cases or redirect them into a full underwriting process. However, this may not always happen, either because insurers choose not to do so, or applicants decide not to take a second chance after the initial disappointment.

Similar effects can be observed for simplified application forms, reduced non-medical limits and the integration of additional data sources. While these changes have been a major improvement for most low-risk applicants, those on the other end of the spectrum have not benefited to the same extent but would still be put through the traditional processes with all their perceived hurdles.

When it comes to underwriting guidelines, the biggest pressure – from salespersons and applicants alike – is usually on the standard to mildly elevated risk. From a sales perspective, these are the cases that have the highest chance of securing the insurance policy with minimal effort. From the applicants' perspective, these are people who – in contrast to those with severe disease – do not necessarily consider themselves at higher than ordinary risk.

As a result, insurers are constantly trying to create more subgroups of "normal" that can get better terms, or to move the mildly elevated risks to the standard pool.

Regulation, on the contrary, is not concerned as much with these risks but clearly focuses on the opposite end of the spectrum. The aim is to secure access to insurance for those applicants in the high-risk group who will be offered unfavourable terms such as significant risk loadings, exclusion clauses, or who will even be declined.

While all these underwriting decisions may be fair in that they are proportionate to the risk to be insured and thus justifiable and compliant with existing anti-discrimination regulation, they also prevent the respective applicants from obtaining much-needed insurance coverage and may ban them from other financial services, e.g. mortgages.

For us as an industry, the following questions arise: Have we exhausted all our options to give as many people as possible access to insurance cover? If so, have we made the limits of our options transparent enough? Is there anything we can do to prevent further, potentially disruptive regulatory developments such as the ones previously described?

What the industry needs to do

To ensure insurability for as many people as possible, three factors are of utmost importance: up-to-date underwriting guidelines; high levels of, and constantly enhanced, underwriting expertise; and the necessary resources.

Underwriting guidelines

Underwriting guidelines are constantly being reviewed to keep them up to date with current evidence and to modify assessments accordingly. This is a requirement of anti-discrimination legislation and thus a prerequisite of the insurers' right to underwrite.

Most frequently, updates in underwriting guidelines are being driven by advances in medicine. Recent years have seen an unprecedented pace of change in diagnostic procedures, development of new treatment options, and even preventive measures, resulting in improved outcomes in many medical fields. This progress is routinely shared with insurance applicants by adapting guidelines to offer improved terms.

In addition to the advances in clinical medicine customers will benefit from societal trends and trends that are partly driven by regulatory activity.

For instance, the "de-stigmatisation" of certain diseases goes along with a desire for more "inclusive" underwriting. Important examples would be an insurer's approach to mental health conditions, HIV infection or cancer. They no longer will result in immediate declinatures but will be carefully assessed and often covered.

Previously rare diagnoses are seen to a greater extent in day-to-day underwriting, suggesting that people affected by these conditions have an increased confidence that insurers will consider their applications despite their complex medical history. In fact, severe diagnoses are increasingly being considered for cover. And a more diversified product landscape helps further in offering more people the cover they need and apply for.

Underwriting expertise

Besides accurate and up-to-date underwriting guidelines, the best possible underwriting quality requires highly skilled and experienced underwriters. The underwriters' knowledge and expertise are required to keep up with the ongoing transformations.

- What was previously known, will change. This means that underwriters need to put in significant effort to keep up with the developments and the resulting faster update cycles of underwriting manuals.

- As conditions become insurable that were previously uninsurable, new unknowns will come up. Underwriters therefore need the dedication, the time and the opportunity to expand their knowledge to these new types of risks.

Constant learning and reconsideration are therefore required for underwriters to do the best possible job in offering as much insurance cover as possible.

Underwriting resources

Beyond the need to constantly acquire new knowledge and experience in assessing new types of risk, there is another challenge underwriters are faced with: assessing (highly) substandard risks requires significant efforts from underwriters. More information needs to be digested, there may be additional evidence, e.g. lab values and medical reports, that are to be retrieved and analysed, and a referral to a medical officer or reinsurer may be warranted.

Adding to these complications is the shortage of experienced underwriters currently observed in many insurance markets, and the time pressure applied from salespersons and applicants alike. The increased transparency of competing offers through, e.g. comparison websites, further adds to the strain on the underwriter to decide quickly in complex cases. Finally, the increasing need to explain decisions to salespersons and applicants and convince them of their adequacy poses an additional challenge to underwriters. This is again especially true for complex cases with unfavourable underwriting decisions such as significant loadings, exclusion clauses applied or even more so declinatures.

To achieve best possible underwriting outcomes, i.e. the highest possible number of cases accepted after careful consideration and with risk-adequate conditions, sufficient resources need to be available, so underwriters have the necessary time on their hands to do the job.

How digitisation can help

Up-to-date underwriting guidelines and sufficient resources of highly skilled and experienced underwriters pave the way to offering insurance to most applicants. And with the advances in medicine expected to continue, further improvements can be predicted in the years to come to include more and more substandard applicants in insurers' portfolios.

The question remains whether digitisation has the potential to improve the application and underwriting process for these applicants, as otherwise this may continue to represent a hurdle for them in obtaining insurance cover. The answer to this question is clearly positive.

On one hand, digitisation is improving underwriting outcomes already as it helps users to consult existing resources in a wiser and more targeted way. With the increasing use of underwriting platforms, not every underwriting application needs to be seen by a human underwriter.

Underwriting platforms will pre-select simple from complex cases and assess standard to low-risk cases by applying immediate and consistent decisions. This will free up resources for human underwriters who in turn can focus on substandard cases or more generally assess complex and unusual cases with extensive information or those new and emerging risks that are not (yet) sufficiently covered by standard underwriting rules. In this example, technology is not immediately used to assess substandard cases, but their outcomes may nevertheless be improved.

There is also the potential to use digital solutions to underwrite substandard risk directly. In recent years healthcare systems across the globe have been undergoing the process of digitisation, as have other sectors. With digitisation, more and more health data are being stored digitally. In the healthcare sector itself, this data is being used for several purposes, e.g. to facilitate information exchange within different departments of hospitals, but also for data analysis, e.g. to gain new insights into medical conditions.

Some countries are introducing central repositories allowing access to all available health data from one entry point. Such solutions have a wide range of potential benefits for patients and healthcare providers such as:

- Increasing transparency of the healthcare system by giving patients insight into their medical history;
- Improving the quality and reducing the cost of medical care by enabling data exchange between physicians (also across borders), thereby avoiding double examinations and treatment;
- Facilitating emergency management;
- Reducing risk of harmful drug interaction;
- Reminding the patient of routine check-ups and vaccinations; and
- Allowing patients to "carry their data around" easily.

Typically, an electronic health record would contain information such as doctors appointments, diagnoses received, prescribed medication, hospital stays, time off work for medical reasons – information very similar to that required for underwriting in the Life/Health space.

With the further roll-out and development of electronic health records solutions, future options for the application processes will include retrieving those data to use them for underwriting purposes. If they could do that, insurers will avoid putting applicants with a complex medical history through a lengthy underwriting process

but be able to assess them in an automated way just as quickly and seamlessly as other applicants.

What can be achieved

There is reason to believe that insurers in the Life/Health sector will be able to further improve their service offering to their potential customers. On one hand, medical advances bring about the potential to extend insurability and making insurance more affordable for a wider range of potential applicants. On the other hand, digitisation offers new opportunities to redesign processes to make insurance more accessible for the full range of applicants.

It is crucial to find the right balance between standard and substandard risks. While a majority of standard-to-mildly-elevated risks is needed for the stability of any insured portfolio, the much smaller group of substandard risks also deserves insurers' best efforts. By embracing the changes and proactively using their full potential to the benefit of all customers, insurers will be able to serve their customers better and consequently also meet the demands of regulation, reducing the need for further regulatory interventions in the future.

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