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COMMITTEE REPORT

INSURANCE

# Get the Best Offer

## Manage the underwriting process

Most people would say the hardest part about the life insurance business is getting people to pay for the insurance. I disagree. Once a person selects a life insurance product, the most difficult challenge is getting the best possible offer from the insurance companies. The estate-planning strategies agreed upon by a client and his advisor may hinge on the most fundamental aspect of the insurance product: How much does it cost? Particularly with larger insurance amounts and older clients, managing the underwriting process is critical for negotiating the best possible offer.

A good advisory team, quarterbacked by a lead insurance professional, should recognize that a well-planned underwriting design includes knowledge of the:

- total in-force coverage on the insured;
- total line to be placed on the insured;
- internal retention limits of carriers;
- auto-binding and jumbo capacity limits of carriers;
- insurance company's medical requirements (for example, treadmill, chest x-ray, etc.);
- staging of companies (that is to say, putting some coverage in force before applying for more, in order to maximize coverage without going "facultative");
- insured's foreign travel; and
- insured's health issues and ultimate offers from carriers.

So let's see how to achieve the best possible results for the insured, both in capacity and cost.

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work from the book. But skillful negotiation may win a better deal.

## MAKE A DIFFERENCE

Although underwriters work from the book, skillful negotiation can in many cases help achieve more favorable underwriting and pricing. How significant a difference can favorable underwriting numbers make? Here's an example: $1 million of death benefits for a lifetime guaranteed policy on a 75-year-old non-smoker female can range from $27,000 annually for "super-preferred" (rating for someone in excellent health) to $39,000 for "standard" (rating for someone in reasonable health) to $52,000 for a "Table 2" (rating for someone with a minor health issue). If applying for $10 million of insurance the difference in premiums between super-preferred and a Table 2 rating is $250,000. This cost differential will require the estate-planning team to come up with particularly clever ideas to avoid the payment of gift taxes.

Coordinating the underwriting process is especially warranted with jumbo-size cases because it's not just the named insurance company that will be carrying the liability. The "Direct Writing Company" (DWC) has a certain amount of retention or liability it keeps, which varies with each insurance company. The remainder, and usually the largest amount, is handed off to reinsurers. Some reinsurers actually hand off part of their liability to retrocessionaires.

Each insurance company has their own "retention" limit, that is to say the amount of insurance that it will underwrite without going to reinsurers. This can vary as much as $20 million from company to company. But once a company has reached its retention limit, the excess goes to reinsurance, where the reinsurers will share the risk.

Most companies have some amount of "automatic binding" which is determined by what the insurance industry calls a "treaty." A treaty is a reinsurance arrangement in which the DWC and "the Reinsurer" agree that all business of a certain description will be ceded to the Reinsurer. The ceding or DWC assumes full underwriting responsibility for all this reinsured business. The DWC has this arrangement with a pool of reinsurers. At the time of claim, the risk is shared among the pool.

Sometimes, the DWC will decide that a particular case needs to be examined more closely for its potential risk. The DWC then sends the actual file to the reinsurers, and the reinsurers make their underwriting decisions. This is known as "facultative" reinsurance. When someone has a serious health issue, for example, the description of that health issue may not conform to the automatic binding treaty between the DWC and its reinsurers. So facultative reinsurance may be the only way for that person to get a life insurance policy. Facultative reinsurance also may be required if the in-force and applied-for coverage exceed retention and automatic binding limits.

"Jumbo Limits" is the amount of in-force and applied-for coverage that an insurance company can write using its internal and auto-binding amounts. With most companies this is $65 million per insured. Above this limit, only internal retention and facultative may be used.

Your goal is to avoid facultative, because reinsurers may have different requirements and criteria for underwriting. A new set of hurdles obviously makes obtaining a policy more difficult to obtain, and drives up the cost, pushing the policy out of reach.

## SHRUNKEN MARKET

Significant changes in the reinsurance market made it trickier to get a good deal on a life insurance policy. From 1995 to the beginning of 2005, the reinsurance market shrank from 18 companies to eight. Total available capacity is therefore very limited—especially because there also have been mergers and acquisitions in the retrocessionaires market. The result is that today pitting one agent against another may actually undermine your negotiations and the best interests of the client, because the insurance companies might all be using the same reinsurers.

How's that? Imagine a client wants $85 million in life insurance. Assume that he's a very healthy 62-year-old male with $10 million of insurance already in force. But he just sold a business that he built over the last 20 years and he now wants to do some serious financial planning.

You narrow the product choices to those offered by four companies. Your client wants to diversify by having at least two carriers. Say Carrier A has a retention of $5 million and an auto cap of $25 million. Carrier B retains $15 million and has an auto cap of $40 million.

At first glance, it seems that this arrangement will work. You send the case to Carrier A first because it doesn't require your client to take a treadmill test. Carrier A likes the case and offers a preferred rating for $30 million of coverage.

Next, you send the case to Carrier B, which does require a treadmill test and makes the same $30 million offer. Why, you ask Carrier B, can't you get more insurance? Carrier B's answer is straightforward: five of its reinsurers are already at their retention because Carrier A has tied them up.

What you need, but may not be able to get because there are so few reinsurers in the marketplace, is a third carrier that has different reinsurers and a product that is acceptable to your client.

Clearly, professionals must understand these market forces before attempting to package large amounts of death benefit.

To use the most capacity with each carrier, it may be necessary to "stage" companies. For example, if a client already has $30 million of insurance in force and wants to purchase another $60 million, we want to avoid going facultative. So, apply initially for only $35 million, which reaches the jumbo capacity of $65 million (total in-force and applied for coverage). Pay the insurance company and put the policy in force. Next find insurance companies with higher internal retention limits (no reinsurance involved) and proceed with the underwriting to place the next $25 million with them. Knowing the retention, auto binding, and jumbo limits with each carrier is critical. The insurance professional's underwriting advocacy team must be well coordinated, organized and systematic. Otherwise, the client could end up with either a lesser amount or more expensive insurance coverage because facultative underwriting occurred.

## HEALTH AND TRAVEL

More often than not, a client has some health issues. You may achieve capacity (that is to say the amount of coverage desired), but how do you get the best offer for that coverage? Given the threat of terrorism, insurers will scrutinize where a client travels. They've always looked at driving records, family history, financial documents, alcohol consumption, smoking habits, and purpose of the insurance, to determine price. But the retraction of the reinsurance market means insurers are far less flexible.

Equally critical to obtaining the best offer is the management of the paperwork process so that the Medical Information Bureau (MIB) is not notified unnecessarily. MIB is a membership association of life insurance companies in the United States and Canada that exchange confidential information pertaining to health and longevity of individuals requesting and owning life insurance policies. Information on your client in this system can impede an agent's ability to negotiate better offers. Whenever possible, particularly if there is a potential problem, it's therefore best to submit information about your client informally to the insurance company. This would mean including physician statements as well as financial information, along with a cover letter that explains what the client is looking to accomplish. The insurance company will come back with a tentative offer that will then help the insurance representative decide where best to place the case with a formal application.

How does the insurance professional manage all these issues to best effect? A good beginning is to understand the underwriters' perspective and why they are asking the questions they're asking. For example, regarding travel, whether a country is on the U.S. State Department's Travel Warning List *(http://travel.state.gov/)*, is not the deciding factor. Countries are categorized according to the risk that each represents; life expectancy of its citizens, medical/health hazards, economic stability, political stability, terrorist activity and crime. It's therefore important to obtain and share as much information up-front as possible. For example, a client was traveling to Bhutan, a Buddhist nation that is not on the warning list. Yet an insurance company became jittery because a few years ago there'd been some insurgent activity on the Indian side of Bhutan's border. The insurance professional did some homework on the Internet to find out about this country, got the client's tour itinerary, researched the tour company the client was using, and submitted this information along with the client's medical information. Without this research and an explicit cover letter, the insurance company would have held back an offer until the client's safe return.

The moral of this story: the more disclosure regarding travel, the better. Is the client a citizen of the country to which he is traveling? That is usually a positive, as it's expected that he'll know the culture and be better able to maneuver and integrate. How remote is the location to which he plans to travel? That could mean medical attention is not easily accessible. Although many companies ask for past travel to determine travel patterns, some states are proposing legislation that would prohibit insurance carriers from questioning and denying coverage based on past travel. Some insurance carriers will limit retention due to travel or offer to shop the case facultatively because of areas traveled. Generally speaking, term coverage may not be available as it could be conceived as "trip insurance" if purchased just before traveling.

## CALMING THE WATERS

How can you make the process go as smoothly as possible? First, it's essential to educate clients on the process and what's involved; this will help manage their expectations and assuage concerns about privacy and confidentiality. It's also key that insurance professionals question clients closely so they can best represent them to underwriters. Many clients think that if they are willing to pay the premium, that should be enough for the insurance company. They are often surprised and sometimes find it intrusive when asked for details about travel plans, financial documents, and drinking habits, etc. But the more cooperative you can persuade a client to be, the greater the chance of getting a better offer for him. For example, a 65-year-old client with a rare blood disease who visits his hematologist monthly got a letter from his doctor explaining the impact of the blood disease on his mortality. The result of that letter: the offer went from a decline to a standard rating.

Always submit an explicit cover letter addressing all important and relevant information. From the underwriters' point of view, sketchy information forces them to draw their own conclusions. In the cover letter, state:

- the purpose of the insurance;
- how the requested coverage amount was determined;
- the potential policy owner's relationship to the insured and why that potential owner was chosen;
- how much coverage is currently in force;
- what the purpose of the current coverage is and whether it will be replaced with the new coverage; and
- if there is a family history of longevity or early death, include specific details regarding individuals' causes of death.

Be sure to detail your own client's weight, smoking habits, regular exercise program, pertinent facts regarding medical issues and how the client deals with the condition. Obviously, it's better if the client visits the doctor regularly and takes any prescribed medication religiously. With an older client, be sure to mention his activities. Does the client drive and have a clean driving record? Walk the 18 holes of golf instead of ride in the cart? Have a job? Work for charities? Coach his grandchildren's little league teams?

The amount of coverage most underwriters will consider depends on age, net worth and income. The rule of thumb is 50 percent of net worth is reasonable for clients aged 70 and greater. For clients in their 50s or younger, most insurers will consider 100 percent to 110 percent of net worth. These financials should not be underestimated. Be sure that with jumbo cases, the net worth supports the coverage. In one scenario, a 65-year-old client had a net worth of about $30 million. She was concerned about how estate taxes would reduce the amount her children would inherit. The coverage being purchased was $40 million in already-established generation-skipping trusts, which had assets to support the premium. The insurance company offered $10 million more than her net worth because the accountant provided financial statements and her investment returns, demonstrating that $40 million in coverage was reasonable given her projected life expectancy and investment growth.

The insurance professional also needs to be clear with the underwriter about clients who are important. Sometimes underwriters can be convinced to be more flexible. What could tip the scale is understanding that a particular client could impact future business that the insurance representative might bring to the company. For example, is the client a well-connected professional who refers considerable insurance business to the insurance professional? Is this a person whose brother is the insurance professional's most loyal and largest client?

## GO TEAM!

The right team advocating for the client to the insurer has medical expertise, negotiating skills, good relationships with insurance companies, a strong understanding of the reinsurance market and a willingness to provide necessary support throughout the process. How long the process will take is impossible to determine, as each case has its complexities. How long until the client's physicians respond to the requests for the records? Did the client get the flu in the meantime and go back to the doctor? Was another doctor mentioned in the report that the client hadn't mentioned? It could take up to a month to get the records at a hospital. Did the underwriter read melanoma (could be fatal) instead of melasma (benign skin disorder) on the dermatologist's report? Does the underwriter want a letter from the client's doctor clarifying a condition? Going back and forth, negotiating among insurance companies could take six weeks to six months.

Although the design of an insurance product has specific parameters, the underwriting to obtain these products is subjective and often negotiable. The purchase price of the insurance policy is ultimately the most important aspect of the life insurance process. Every advisor representing high-net-worth clients can benefit by being aware of the tremendous difference artful underwriting can have on the premium clients pay. Understanding and communicating to the client the attributes and strategies with each life insurance product is important, but the cost is what will dictate the ultimate effectiveness of the insurance program. ■

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