

# Underwriting for Today

*Why are we still using 20th century tactics when we have 21st century technology at our disposal?*

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I was sitting in a hotel room in Dallas recently trying to arrange a trip for the upcoming month. I accessed the LIMRA database remotely to find the email address of the president of a company I wanted to visit and sent him an email. Five minutes later, he responded and we arranged a meeting. After putting together the rest of the trip, I went online to find airline tickets, make hotel reservations, and set up a rental car.

Consider how this might have been transacted twenty years ago. I would have dictated a letter to the people I wanted to meet and followed up with phone calls a few days later. Once the trip was set up, I would have contacted a travel agent to figure out the best flights and hotels so that they could book them. The whole process would have taken much more time and involved many more people.

Whenever I feel anxious about the current economy, I find consolation in how technology has drastically transformed and improved the way business is conducted. In addition to the obvious enhancements that the Internet has brought about, the mobile access to information via cell phones and PDAs has made us all more accessible and arguably improved or ruined the quality of our lives depending upon your perspective. And for those of us who travel frequently, the soothing voice of our GPS has become our new trusted travel companion.

By comparison, consider how the typical life insurance application is processed. An agent completes an application and mails it to his/her carrier. A paramedical exam is ordered along with laboratory tests, and a telephone interview is conducted. An underwriter accesses a number of electronic databases and, if necessary, orders attending physician statements. Weeks later a decision is made and, if approved, a policy is mailed out. This entire process is eerily similar to the way we used to set up our business trips 20 years ago, requiring a lot of time and the involvement of a lot of different people.

Why are we still using 20<sup>th</sup> century tactics when we have 21<sup>st</sup> century technology at our disposal?

Before I address this question, I'd like to point out that it took us a while to figure out the proper applications for the Internet. In the late nineties everyone was scrambling to apply the Internet to their businesses and at that time there was even an expectation that this signaled the end of traditional distribution channels such as brick and mortar stores, financial institutions and service companies, and insurance agents and car salesmen. Although there are some notable exceptions—Amazon, eBay and iTunes come to mind—what ultimately transpired was that Internet technology enhanced rather than replaced traditional processes. The same people who now buy books from Amazon also enjoy spending a quiet afternoon browsing at their local Barnes & Noble. People research their cars online but usually head to a dealership to make a purchase. And people utilize the Internet to better understand their insurance and financial needs but usually require the motivation of an agent to do anything about it.

In a similar manner, we now have the technology in place to automate a large part of the underwriting process. Websites have been created to facilitate online applications. Algorithms have been developed to automatically interpret the data residing in a variety of consumer databases. Rules engines have been programmed to make business decisions based upon the logical interpretation of a variety of variables. In some cases, we can program a computer to synthesize and interpret complex data better than a human. As a result, it's now possible to effectively evaluate and execute a new life insurance application without any interaction with an agent or home office employee.

Does this signal the end of the human underwriter as we know it? I doubt it. Just as Amazon and eBay can only serve a certain constituency, automated underwriting is only perfectly suited for specific products and markets.

And just as the Internet enhanced rather than replaced existing processes, so can new underwriting technology complement and support the effectiveness of the risk selection process.

A good example can be found in the simplified issue marketplace. According to the recent LIMRA report *Simplified Issue Marketplace: An Individual Life Insurance Product Study*, out of 29 companies offering one or more simplified issue life products, 40 percent use automated underwriting as part of their process. Of those companies using automated underwriting, 85 percent make the initial underwriting decision on an automated basis and 65 percent make the final underwriting decision on an automated basis. Clearly there is an application for automation with simplified issue contracts.

## Human Touch

In addition, simplified issue underwriting is an integral part of the small face life business that comprises the core of the LIC membership. Although processes can vary greatly by company, the typical small face life sale is centered on a precisely designed application with knock-out questions to separate risks, and verification via telephone interviews and MIB reports with APSs used only when absolutely necessary. One might conclude that small face life products are ideal candidates for automated underwriting but I would suggest that the need for aggressive anti-selection protection provides an ample argument in favor of more human intervention, especially since it can be done without slowing up the process or significantly increasing the cost.

For example, let's consider the telephone interview. The genesis for this process was to keep the agent honest by verbally verifying the validity of the application directly with the insured. This is a common practice with most companies. In fact, according to a 2007 survey of 135 insurers conducted by Hank George, Inc., three out of four insurers use some form of teleinterview on their new business and 75 percent of teleinterviews are outsourced to specialty firms. These specialty firms can offer a variety of services ranging from call center reps reading from a simple script to full-fledged underwriters following a company's specific guidelines. And as the popularity of this practice indicates, most specialty firms can provide this service better and cheaper than the insurance carriers.

Teleinterviews form the foundation for most small face life companies' risk assessment and it's doubtful that this part of the process will be automated. Given the high number of elderly applicants, the telephone interview provides an important safeguard to verify that the application questions were understood and answered accurately. In addition, given the high rate of agent turnover and the single interview nature of these sales, the telephone interview creates a valuable sentinel influence over agent behavior. However, technological enhancements have been developed that enable even the most elementary interviewer to probe with pointed questions via increasingly sophisticated drill-down questions that guide the interviewer through a carefully crafted decision tree. In this way, the intuition of Sherlock Holmes is available to every Dr. Watson.

But why turn Watsons into Holmes when we can turn Holmes into Einsteins? In other words, why not use real underwriters rather than interviewers and let skilled experts exploit the technological enhancements to their fullest extent?

Effective risk selection is difficult enough even with access to complete medical records and recent lab results. By comparison, simplified issue underwriting relies on interpretive rather than evaluative data and could benefit from any advantage possible. Telephone interviews provide insurance companies with the opportunity to have a personal conversation with each and every prospective new insured. How much would your company's mortality improve if an experienced underwriter were the one having this conversation? This advantage is even more attractive considering that some teleinterviewing firms will import their own technology into their customers' home offices. In this way carriers can use their own underwriters for a majority of the applicants, while still utilizing the interface of the teleinterview company's technology and their support for after-hours or high volume calls.

Surprisingly, the principal objection to this sort of thinking comes from underwriters themselves, many of whom have told me that the costs involved in using underwriters rather than teleinterviewers is too prohibitive to be practical. While conceding the point, I'll also add that with final expense policies, the impact on profitability from a 25 percent improvement in mortality is five times that of a 25 percent reduction in expenses. At the very least, it

would be worthwhile—as well as telling—to test whether companies would be better off evaluating their risks with either an Einstein or a Holmes!

In addition to pre-programmed logic trees and analytical algorithms, there are some other technological enhancements that significantly improve the efficiency of the underwriting process and lend themselves nicely to teleunderwriting. For example, the MIB now offers a Code Table option that allows carriers to translate common MIB codes into English. This “fluency on the fly” feature enables a qualified interviewer to readily interpret MIB records while simultaneously carrying on a telephone interview. They also offer a Custom Filter option so that only the most meaningful codes make their way to the interviewer’s screen. This is ideally suited to simplified issue policies where the application is only concerned with very specific health conditions.

Another useful technology for simplified issue underwriting is the Prescription Drug Database. These systems provide the interviewer with “real time” information about an applicants’ prescription drug history. The effectiveness of this tool was recently documented in “An Analysis of Prescription Histories and Mortality,” an article in *On the Risk* magazine by Timothy L. Rozar and Scott A. Rushing of RGA Reinsurance Company. In this study, RGA worked with Milliman IntelliScript in order to evaluate the mortality experience from a large block of insurance applicants for whom prescription drug histories were obtained at the time of application. This comprehensive study included 1.1 million applicants, 21 million distinct RX fills, and 2,530 deaths, and evaluated the mortality differentials by drug severity classification and fill frequency. Milliman IntelliScript uses color-code mapping to classify drug significance as green, yellow, and red with green being the least important to insurability.

The study found that in instances where there was no RX information available, mortality was slightly worse than average. In instances where an RX history was available but no prescriptions had been filled, mortality was about average. In instances where an RX history was available but only green and yellow drugs had been filled, mortality was markedly better than average. And in instances where an RX history was available and red drugs had been filled, mortality was found to be significantly worse than average.

The effectiveness of the RX database has been further enhanced through the use of rules-based underwriting engines which automatically access combinations of drugs and fill histories in order to instantaneously interpret the data in a manner and speed that isn’t humanly possible. Of course, as we’ve recently seen in the economy, a computer model is only as good as the assumptions feeding into it and if something unforeseen occurs the effectiveness of the model can be very different from what was expected.

One final outcome of the teleinterview process that hasn’t been embraced by very many companies is the application process itself. A teleinterview already involves collecting specific identifying information about the agent, applicant, and insured, as well as all of the pertinent medical information. This pretty much completes the process for small face life applications. By adding just a few additional questions regarding beneficiaries, replacements, payment methods and an agent’s statement, in most cases the application would be complete. How much money would a company save if all of the expense involved in processing paper applications disappeared? How much more effective could an agent operate if they didn’t have to complete and submit an application? How much more efficient would a company’s new business department function if every application were complete, accurate, and without amendments?

A number of companies have cited the compliance uncertainty associated with using voice rather than wet signatures as a reason for clinging to paper. Although that sounds like a good topic for a future article, I will only reference here the fact that voice signatures have become fairly routine on the property/casualty side of our business. In addition, Baltimore Life has offered a successful paperless final expense application process for a number of years.

The future of simplified issue new business processing has arrived, yet few companies have fully embraced the total potential benefits that current technology brings to the table. Is there a cost for waiting? Perhaps. According to *The Case of the Disappearing Customers*, a recent joint study conducted by LIMRA and the Life Insurance Direct Marketing Association, nearly half of consumers surveyed expected to have a policy issued and in their

hands within two weeks of applying. Unfortunately, this expectation was met in only 28 percent of the cases issued. In addition, the No. 1 reason identified in the report for consumers abandoning their life insurance pursuit was cost. Teleinterviews, paperless processing, automated underwriting, and improved access to a variety of consumer databases allow carriers to underwrite and issue small face life policies before the agent has even left the house. And best of all, these enhancements to speed come at a reduced cost and an improvement in risk selection, representing a rare opportunity to address the primary reasons consumers fail to complete the application process while potentially improving profits at the same time.

Although the jury is still out as to whether Albert Einstein or Sherlock Holmes would make a better underwriter, thankfully current improvements in technology provide simplified issue companies with the opportunity to find out for themselves.