Unemployment, Past Present and Future

Presented to the Staple Inn Actuarial Society
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by Kathy Byrne, Simon Jeffery and Graham Bolton

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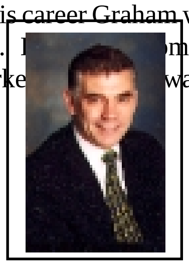

Graham Bolton is Group Marketing Director at Pinnacle Insurance. He has many years of experience in the Creditor Market. Early in his career Graham worked for Raleigh Industries Gradual Payments (RIGP) one of the early pioneers of creditor insurance in the UK. [illegible] completed the first of his two Master’s degrees. His thesis was on creditor insurance in the mortgage lending marke[illegible] was completed whilst Graham worked for Financial Insurance Group.

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We would like to thank Gary Fagg of CreditRe Corporation for the illustration of the Morris Plan Leaflet shown in Section 1 and Monica Dickman of RIGP for allowing us to use the RIGP Payment Card and Policy reproduced in Section 1. Thanks to our colleagues Sheena Walker, Joe McCormack and David Beard for their input on the state benefit system, sales aspects and claims management respectively. Thanks also go to our clients who have helped us in providing their views on the future of the creditor market and to our colleagues for reading and commenting on drafts, you know who you are! The views expressed in the paper are our own, and errors or omissions are ours alone.

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INTRODUCTION

Is unemployment an insurable risk? This might seem to be on odd question to ask in a paper about unemployment insurance! However, the first General Insurance Research Organisation (GIRO) conference I attended in 1994 asked this very question to a roomful of actuaries. Surprisingly the overwhelming response was ‘no’ even though unemployment had been underwritten in the UK for over thirty years. This might well be a reflection on the timing with which this was asked: in 1994 the UK was just coming out of recession and many Insurance Companies had lost a lot of money offering unemployment cover. If you ask the same question today, I expect the answer would be quite different. Today, unemployment is at an all time low and far from being uninsurable due to excessive anti-selection is perhaps uninsurable due to lack of need (demand)!

This paper explores the reasons why unemployment insurance is a different type of risk to many other personal lines covers and shows why the risk is real. It is aimed at actuaries working in Insurance, Product Development Actuaries in particular, and not just creditor specialists. It looks at all the risks that are covered under a creditor policy, not just the unemployment cover.

The paper is divided into three parts

I. UNEMPLOYMENT PAST
Section 1 provides a brief history of the creditor market in both the USA and the UK.

II. UNEMPLOYMENT PRESENT
Sections 2 to 6 describe, in general terms, the creditor product and the markets in which it is offered.

Sections 7 to 12 cover the actuarial aspects of product pricing and reserving for creditor insurance.

III. UNEMPLOYMENT FUTURE
This part of the paper is the one we hope will generate the most discussion at the meeting in Staple Inn. Sections 13 – 18 identify a number of potential opportunities and threats for unemployment insurance. In particular the impact of the next recession, the withdrawal of the State from welfare provision, future regulation and opportunities arising from Stakeholder Pensions.

Kathy Byrne

December 1999

I. UNEMPLOYMENT PAST

This part of the paper traces the history of creditor insurance from its beginnings in the USA to its arrival in the UK, highlighting major milestones in the product's development.

1. History of Creditor

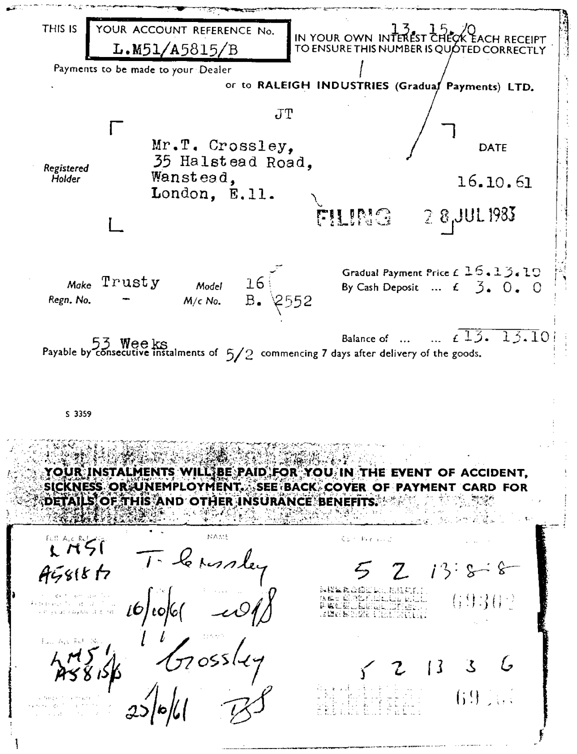
Personal lending started in the USA at the turn of the century. At this time banks would not lend money without security, which most people were unable to provide. Arthur J. Morris is credited with being the founder of both consumer lending and credit life insurance. He set up a bank in Atlanta in 1910 organised on the concept of lending money based on the character and earnings of the borrower. A number of Morris Plan Banks sprang up around the USA based on his principles. These banks have now evolved in to the banks and finance houses we know today.

A
MAN'S DEBTS
should not live
after him
THE
MORRIS PLAN
COMPANY
OF
RHODE ISLAND
25 CANAL STREET
PROVIDENCE, R. I.
THE MORRIS PLAN

Morris s a need for insurance on the loans, the loans could be recovered from the co-borrower on a
borrow pleasant task. Morris approached a number of Insurers to provide life insurance cover on these
loans; h ested, as there was no data on which to base pricing. So in 1917 Morris set up his own Insurance
compar ce Society, which had the motto "No man's debt should live after him".

In 1925 ngfield, Ohio formed the Credit Life Insurance Company. This company issued the first group
credito s the basis of modern creditor policies seen today. By 1931 there were only 4 companies offering
credito National Association set up its own creditor company, CUNA Mutual. Within two years CUNA
Mutual der of creditor insurance in the USA. Today the number of creditor insurance providers is
approxi

Credito know it today, appeared in the 1960s and 70s. The earliest example we have been able to find is
a policy wing illustration shows a Payment Card issued in 1961 by RIGP (Raleigh Industries Gradual Payments, a subsidiary of Lloyds TSB).



THIS IS YOUR ACCOUNT REFERENCE No. L.M51/A5815/B

13. 15. /0

IN YOUR OWN INTEREST CHECK EACH RECEIPT TO ENSURE THIS NUMBER IS QUOTED CORRECTLY

Payments to be made to your Dealer

or to RALEIGH INDUSTRIES (Gradual Payments) LTD.

JT

Registered Holder

Mr.T. Crossley,
35 Halstead Road,
Wanstead,
London, E.11.

DATE 16.10.61

FILING 28 JUL 1983

Make Trusty Model 16
Regn. No. – M/c No. B. 2552

Gradual Payment Price £ 16.13.10
By Cash Deposit ... £ 3. 0. 0
Balance of ... ... £ 13. 13.10

Payable by 53 Weeks consecutive instalments of 5/2 commencing 7 days after delivery of the goods.

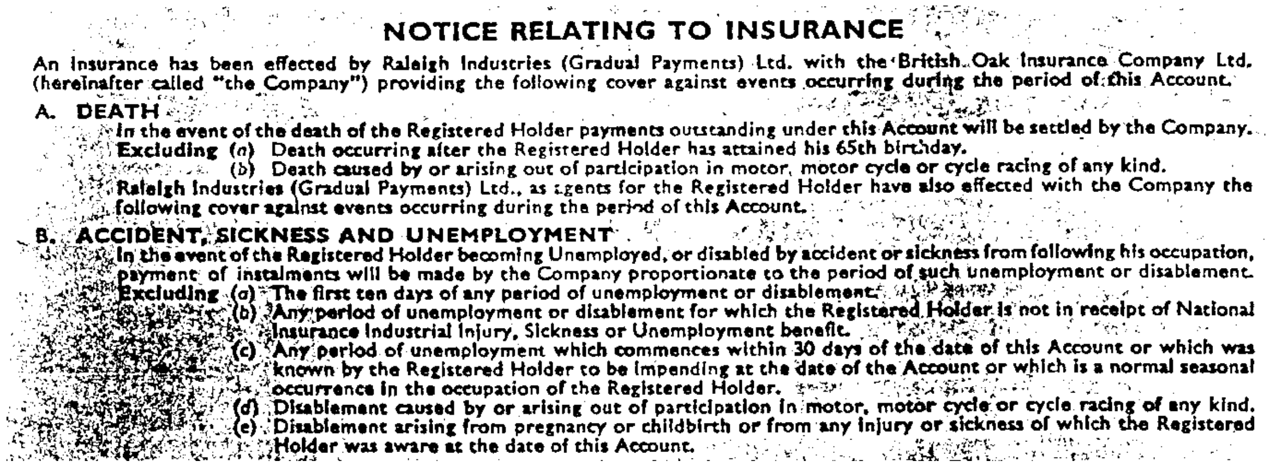
S 3359

YOUR INSTALMENTS WILL BE PAID FOR YOU IN THE EVENT OF ACCIDENT, SICKNESS OR UNEMPLOYMENT. SEE BACK COVER OF PAYMENT CARD FOR DETAILS OF THIS AND OTHER INSURANCE BENEFITS.

L M51 A5815/B T. Crossley 5 2 13 8 8
16/10/61 69302

L M51 A5815/B Crossley 5 2 13 3 6
25/10/61 69

The policy is printed on the reverse of the Payment Card and is shown below. This is the policy in its entirety; it is quite short compared with the Plain English policy booklets of today. This is one of the earliest 'modern' creditor policies and the cover includes life, disability and unemployment. The benefits and the exclusions are similar to those we see today.



NOTICE RELATING TO INSURANCE

An insurance has been effected by Raleigh Industries (Gradual Payments) Ltd. with the British Oak Insurance Company Ltd. (hereinafter called "the Company") providing the following cover against events occurring during the period of this Account.

A. DEATH

In the event of the death of the Registered Holder payments outstanding under this Account will be settled by the Company.
Excluding (a) Death occurring after the Registered Holder has attained his 65th birthday.
(b) Death caused by or arising out of participation in motor, motor cycle or cycle racing of any kind.

Raleigh Industries (Gradual Payments) Ltd., as agents for the Registered Holder have also effected with the Company the following cover against events occurring during the period of this Account.

B. ACCIDENT, SICKNESS AND UNEMPLOYMENT

In the event of the Registered Holder becoming Unemployed, or disabled by accident or sickness from following his occupation, payment of instalments will be made by the Company proportionate to the period of such unemployment or disablement.
Excluding (a) The first ten days of any period of unemployment or disablement.
(b) Any period of unemployment or disablement for which the Registered Holder is not in receipt of National Insurance Industrial Injury, Sickness or Unemployment benefit.
(c) Any period of unemployment which commences within 30 days of the date of this Account or which was known by the Registered Holder to be impending at the date of the Account or which is a normal seasonal occurrence in the occupation of the Registered Holder.
(d) Disablement caused by or arising out of participation in motor, motor cycle or cycle racing of any kind.
(e) Disablement arising from pregnancy or childbirth or from any injury or sickness of which the Registered Holder was aware at the date of this Account.

The consumer loan companies who were subsidiaries of the US loan companies and money shops began offering creditor insurance in the 1970s. It was also partly due to strict credit controls being imposed on finance houses forcing them to concentrate on their bottom line profit rather than turnover. Trustees Savings Bank introduced creditor cover on its personal loan business in the early 1970s but other banks did not follow their lead.

The 1980s in the UK saw the expansion of creditor in to the retail credit card market and the mortgage market. The Bank of Scotland was the first of the big high street banks to offer creditor cover in 1981 having seen how profitable it was to their Finance House subsidiary, North West Securities. They were soon followed by Barclays Bank and National Westminster Bank and later by the other major clearers.

The building societies had been slow to offer creditor insurance, they were strongly traditional and being mutual organisations they preferred to provide benefits for members on a non-profit making basis. The Furness Building Society was the first building society to offer a creditor scheme to its borrowers when it mailed an accident and sickness cover in 1982. The Cheshire, Birmingham Midshires and the Britannia followed them.

The positioning of creditor insurance by the insurer to the lenders was that profit could be gained, both from the commission earned and the fact that the premium would be charged to the loan account to cover the period of the loan. This meant that the lender also earned additional interest charges. Monthly premium products were not a major feature of this market until the late 1980s.

Lenders were hit hard by the recession of the late 1980s/early 1990s because only a small proportion of their borrowers had creditor cover. Since then they have promoted creditor heavily, initially to protect themselves against arrears. Now the income from creditor commission is a major income stream for lenders.

Today virtually every lender will offer some type of creditor scheme on its lending activities; it is very rare to find a loan book without creditor cover.

II. UNEMPLOYMENT PRESENT

This part of the paper provides a snapshot of where we are now, looking at the structure of the market and the products that are currently being offered. The actuarial aspects of pricing and reserving are covered, along with the social, legal and taxation aspects.

2 INSURANCE PROVIDERS

Here we look at what types of Insurance Company are underwriting creditor insurance at the present time. Creditor Insurance is written under a number of long term and short-term classes. The provider needs to be either a composite insurer with life and general licenses or to have separate life and general insurance companies within a group.

2.1 Specialist Providers

Companies that specialise in creditor will have expertise in managing creditor schemes in both good times and bad. They have to be experts as the success of their business depends on it. As well as expertise in product design and pricing, good administration systems are essential for efficient handling and management of claims. Most specialist companies have developed their own bespoke claims handling systems. The proprietary systems available in the market are generally unsuitable for creditor, having been designed with annually renewable motor or household policies in mind.

2.2 Large Composite Insurers

For these insurers, creditor is a relatively minor product line that often supports the distribution channels for other lines of business, such as household. Some composites have specialist creditor units that on a day-to-day basis operate like a specialist provider. However, even these companies may be influenced by the changing economic cycle and maybe not be fully committed to the creditor market over the long term.

2.3 Lloyds of London

During the 1980s there were a number of Lloyds syndicates that would provide rates for creditor insurance. The structure of Lloyds, and the need for brokers, meant that the lender had little direct access to the insurer. A feature of the Lloyds market is that the insurances they provide are very price driven. This meant that through the recession in the early 1990s many of the syndicates withdrew from the market.

There is only one Lloyds syndicate that has been consistent in providing creditor insurance and as such has developed in-depth knowledge of the market. It was one of the first to recognise the potential negative impact on claims experience of providing cover that did not exclude mental illness or backache.

2.4 Captives

A number of large lending organisations have their own captive insurance companies. Some of these are reinsurance companies whilst others are direct writers. During the 1980s a lot of banks and building societies set up life and general insurance subsidiaries. Lenders set up captives in order to share in underwriting profits and investment income. Today there is little benefit in these companies setting up a captive, as the largest lenders will benefit from profit sharing arrangements. The very large lenders might get a share of investment income as well. Some of these captive operations have been set up off shore in locations such as the Channel Islands, Isle of Man or Dublin. An offshore captive has lower solvency requirements and benefits from tax advantages. However, UK Tax legislation, notably controlled foreign company and transfer pricing legislation, has limited the tax benefits.

2.5 Reinsurers

Reinsurance in the creditor market is rare, other than reinsurance to captives and for large life risks. Stop Loss cover is available from time to time but is not generally used and may not always be available. As with the large composites, creditor is often a fairly minor line for reinsurers. In fact reinsurers sometimes act as introducers of business to the creditor specialists rather than the more conventional relationship!

3. MARKET SIZE AND COMPOSITION

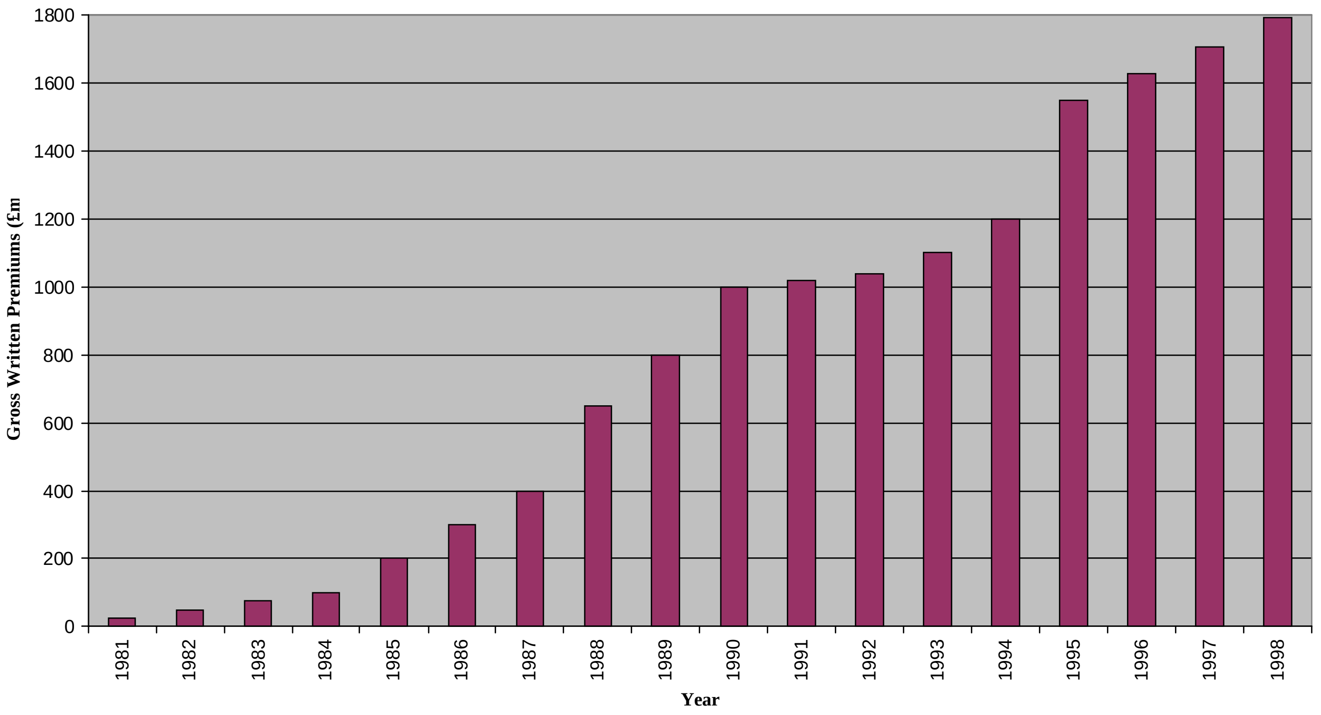
In this section we look at the size of the market in terms of gross written premiums and the composition of the market in terms of market share by type of lending and also by type of provider.

3.1 Market Size

The size of the creditor market is notoriously difficult to estimate. UK Institutions tend to be reluctant to reveal figures. The DTI returns can provide some information about what the insurers have written. However it is difficult to identify creditor separately as the large composites will have a number of different lines of business falling in to the same classes as creditor. Looking at it from the other direction via the lenders is also difficult, as lenders do not publish information about the volumes of creditor that they have written.

According to the 1999 Datamonitor report, the creditor market generated approximately £1.5bn of gross written premium in 1998. However, our own estimates of market size would be around the £2bn mark. Indeed Datamonitor's 1998 and 1999 reports give different market size figures for the same years. Therefore we have estimated market size using a combination of published data, combined with our own market knowledge.

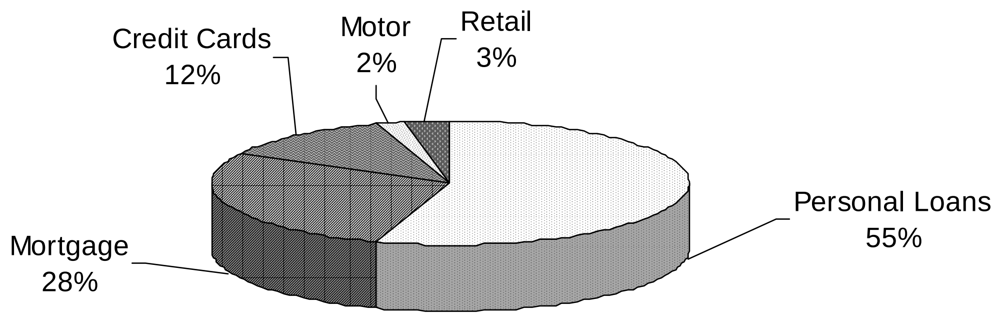
Creditor Market Size 1981 - 1998



The market has shown strong growth throughout the 1990s, even though unemployment has been falling since the middle of 1993. Lenders have promoted the cover strongly and customers who were affected by the last recession don't want to suffer financial problems again and so take out the cover.

3.2 Market Composition

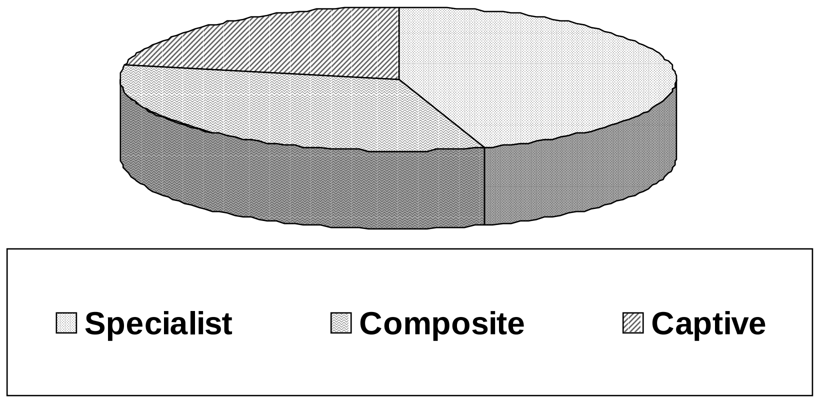
By market, the personal loan market generated the most premium, followed by the mortgage market, with credit cards, motor and retail making up the rest.



Source: Datamonitor 1999

The market is dominated by the specialist players who account for around half the market. However, captives have gained market share as a number of major lenders have moved to captive arrangements.

Specialists	GE Insurance, Pinnacle Insurance, Cassidy Davis, London General
Composites	CGU, NU/L&E, Cornhill, Royal Sun Alliance, Eagle Star, Guardian, Legal & General
Captives	Barclays, Lloyds TSB, Hamilton, St. Andrews & others



Source: Datamonitor 1999 and market estimates

4. PRODUCT TYPES

Here we look at the benefits that might be included in a policy and the definitions that might be used. Creditor Products combine a number of different benefits such as life, disability, unemployment, critical illness and total and permanent disability cover. The cover is in some ways similar to Permanent Health Insurance (or Income Replacement). However, it is not medically underwritten and is approached on a group rather than individual basis. Cover is usually for unemployment as well as disability. Benefits are provided on a short term basis.

Most benefit definitions are occupation based as benefits are triggered by inability to meet debt payments because the insured customer is no longer working.

The benefits for creditor insurance are important as there is usually much confusion as to what is actually being provided, especially in the mortgage related market. Creditor insurance is now referred to as Mortgage Payment Protection Insurance (MPPI), which of course is different to Mortgage Protection - a generic name used to describe Term Assurance. Neither should it be confused with Income Protection (IP) which although offering similar benefits to creditor is not required to be linked to a lending transaction. Permanent Health Insurance (PHI) is often provided to give the customer protection against long term illness. The benefits provided by PHI could complement the cover provided by creditor insurance, but often result in extending the confusion.

It can be argued that creditor insurance is a far more appropriate product for the majority of customers as the customer is more likely to suffer a reduction or loss of income as a result of a short term disability, or period of unemployment, than they are to benefit from a PHI policy because of long term illness.

4.1 Disability

The definition of disability used in the majority of policies is an ‘own occupation or any occupation to which suited by reason of education, training and experience’. Some policies may offer only accidental disability cover.

4.2 Unemployment

There are a number of different definitions used for unemployment claims, varying from redundancy to involuntary unemployment.

4.2.1 Redundancy

This is defined in employment legislation. A full time employee may be made redundant if the employer is no longer carrying on the business for which the employee was employed at the same location or in a suitable alternative site. Alternatively if the employer needs fewer employees to carry on particular work then it may also make people redundant.

4.2.2 Involuntary Unemployment

This is a less stringent definition of unemployment than redundancy. It requires an employee to have been made unemployed involuntarily, to be signing on for Jobseeker’s allowance and to be available for and actively seeking work.

4.2.3 Unemployment Cover for the Self Employed

Benefit is usually triggered when the business ceases to trade, which means that the company must have involuntarily ceased trading as a result of the business having insufficient assets to meet its debts and liabilities. This is usually confirmed by the company’s accountant and bank and by closing accounts being filed with the Inland Revenue.

4.3 Critical Illness

The critical illnesses covered by creditor policies are usually limited to the main six : cancer, heart attack, stroke, coronary artery bypass surgery, major organ transplant and renal failure. Industry standard critical illness definitions are used. Cover is provided either to pay off an outstanding debt or it can be linked to the monthly benefit, some policies will pay a higher number of monthly benefits per claim if the claim results from a critical illness.

4.4 Total and Permanent Disability

This benefit is not often included in modern UK creditor products but is a common benefit to be included in the South African market. Where this benefit is included it is usually based on an 'any occupation' definition of disability and the total and permanent disability is usually established over a six or twelve month period. A reason why this benefit is not often seen in the UK could be related to the Insurance Ombudsman's dislike of 'any occupation' based disability products.

4.5 Special considerations - Self Employed and Contract Workers

4.5.1 Self Employed

There have always been products offered to the self-employed, however, cover offered to the self-employed for unemployment varies. The self employed (and controlling directors) are in a position to influence their own unemployment which poses problems about the unforeseeable nature of the cover. There is also some moral hazard, if the business is in financial trouble it could be easier to claim under a creditor policy through being 'unemployed' rather than to persevere in a difficult business. The definition of unemployment described above will provide cover once it is certain that the business has no future. It will not help out if the business has temporary financial difficulties as to some extent these are foreseeable.

4.5.2 Contract Workers

Similarly unemployment cover has been available to contract workers for many years. Contract workers could always claim for unemployment resulting from early termination of a fixed term contract and could claim until the contract was due to expire. Employment patterns have been changing and some employers now offer only short contracts to their employees, which are regularly renewed. To all intents and purposes these employees are very like permanent employees. Over the last few years cover has been widened, recognising these patterns, and treating these types of contract workers as permanent employees if they have been working for the same employer for a number of years.

4.6 Payment of Benefits

In order to claim for unemployment or disability benefit an insured customer must be off work as a result of disability or unemployment for a minimum period of time. This period may be referred to as the '*deferred period*' or alternatively as the '*excess period*' or '*waiting period*'. We will refer to this period as the deferred period throughout this paper. The deferred period is usually measured in days and is typically 14, 30 or 60 days although longer and shorter periods are possible. At the end of this period the customer is eligible to start receiving benefit and there are a number of different ways this may be accrued:

Elimination Benefits (E) – These start accruing at the rate of one thirtieth of the monthly benefit for each subsequent day of disability or unemployment. No benefit is paid for the deferred period.

Monthly Benefits (M) – One monthly benefit is paid immediately on completion of the deferred period. Subsequent benefits are paid for each complete month that disability or unemployment continues.

Retroactive Benefits (R) - On completion of the deferred period an immediate benefit payment is made equal to one thirtieth of the monthly benefit for each day of the deferred period. Subsequent benefits accrue at the rate of one thirtieth of the monthly benefit for each subsequent day of disability or unemployment.

U Benefits (U) - One monthly benefit is paid immediately on completion of the deferred period. Subsequent benefits accrue at the rate of one thirtieth of the monthly benefit for each subsequent day of disability or unemployment.

There may also be a period at the beginning of the policy during which a customer cannot claim this is usually called the *initial exclusion period* but may also be referred to as the *qualifying period* or *waiting period*. This is typically 60 or 90 days for unemployment cover offered to new borrowers, 90 – 180 days for unemployment cover offered to existing borrowers and 0, 30 or 60 days for disability.

Benefits usually terminate on the first of the following events:

- The customer returns to work
- The maximum number of benefit payments is reached. The maximum number of benefits per claim and in aggregation varies widely, they can be anything from 3 months to 60 months. Typically benefits will be paid for 12 months per claim with an opportunity to requalify for further benefits after returning to work for a minimum period of time.
- The credit agreement is repaid

4.7 Exclusion Clauses

The eligibility criteria for creditor cover is very wide and is limited to age limits and employment criteria. Therefore there has to be some limitation on the extent of cover if it is to be provided at a low cost. Typical exclusions are listed below:

Life Exclusions
i) War riot and civil commotion
ii) Death within a number of days of the commencement date
iii) Suicide

Disability Exclusions
i) Pre existing conditions
ii) War riot and civil commotion
iii) AIDS
iv) Self inflicted injuries, alcohol and drugs
v) Normal pregnancy, miscarriage and abortion
vi) Mental and nervous conditions unless under the care of a Specialist
vii) Backache unless there is supporting medical evidence

Unemployment Exclusions
i) Prior knowledge of impending unemployment
ii) Unemployment occurring within a number of days after the commencement date of cover
iii) Seasonal, casual or temporary work or if unemployment is a regular feature
iv) Voluntary unemployment
v) Fraud, misconduct, dishonesty or criminal acts
vi) Payment in lieu of notice
vii) Arising from any of the disability exclusions

5. CLAIMS HANDLING AND MANAGEMENT

The product a customer is buying from an insurer is a promise to pay a claim if the insured event occurs. Thus the claims process is the end service that the consumer is buying. Claims handling needs to be efficient and clear to the customer.

A full description of a claims handling process is not within the scope of this paper. There are, however, some factors that are relevant to the development of creditor insurance.

5.1 Teleclaims

Most requests for claim forms are dealt with over the telephone. The teleclaims unit can take down the details of the claim over the phone and send out a pre-completed form, which can then be checked by the customer, the relevant signatures obtained (from the benefit office and former employer for an unemployment claim or from their doctor for a disability claim). Moreover, the initial telephone call can act as a screening process to identify those claims that are unlikely to be covered and to manage expectations.

5.2 Grey Claims

Creditor insurance companies, like other insurance companies, will pay all valid claims. Clearly fraudulent claims will never be paid out. In the recession of the 1990s it was estimated that approximately 20% of claims were fraudulent. There are approximately 15% of all claims that would fall into what could be called ‘grey claims’ where the decision to pay is not clear cut.

One of the key considerations for insurers and lenders when implementing creditor insurance programmes is the lenders attitude towards claims which fall into this grey area. Usually there will be a profit-share arrangement in place which means that the profit for any creditor programme would be adversely affected by a high claims experience.

5.3 Helplines

Many insurers offer helpline services to claimants, which can provide details of state benefits and entitlements and can provide help with CV writing and job searches.

5.4 Claims Management Initiatives

Most insurers will constantly be looking for ways to develop new initiatives and manage claims more effectively.

5.4.1 Proactive assistance to help customers return to work.

A “Back to Work” package to help customers who had lost their jobs return to active employment. Back to Work Assistance is a three-stage approach and is seen as an addition to anything the customers may do under their own imitative or through the Employment Service programmes.

The three stages of the package are as follows:-

- **Stage 1** - Sending a Back to Work booklet to the customer. The booklet details how to prepare for your job search, where to look, for example on the Internet or in specialist magazines, interview preparation and other general helpful pointers.

- **Stage 2.** Contacting the customer by phone to ask if they require any help with the job search and discussing how to assist them. Regular contact with the customer is established including reviewing and helping construct their CV, carrying out Internet searches on their behalf and researching any specialist publications.

- **Stage 3.** Offering the opportunity to attend a local workshop (subject to enough customers and interest in the same commutable location). The customer is offered the chance to attend a workshop with other claimants, they receive specialist advice from a Personnel Manager on the day and lunch and tea and coffee are included.

The use of this package offers the following benefits to the insurer:-

- Regular contact with the customer that identifies any potentially suspicious claims.
- A positive proactive approach to reduce the duration of the claim, which receives an excellent response from the customer and saves the amount of benefit paid.
- Is seen as a positive and customer friendly action by the lender
- The customer feels the insurer is trying to help, not just “not pay the claim”.

The package offers the following benefits to the customer:-

- The customer can accept the offer of assistance or not, once aware of the service they can take it up at a later stage if their own plans are unsuccessful.
- They can obtain one to one assistance or group help.
- There is the potential to widen their horizons to the type of work they can obtain.
- They return to work sooner than anticipated.

After reviewing the results it is clear this type of service is very well received, however, the return to work rate is much higher in some categories than others. In the unsuccessful cases the benefit is good customer relations rather than any cost saving.

5.4.2 Disability Claims

A Medical Adviser (MA) reviews most new claims. This might include a home visit to customers making disability claims in order to obtain much more detailed information on the customer’s condition, treatment and attitude. Qualified Nurses carry out these visits and the customer is advised of the visit in advance. The Nurses will not offer specific advice or make any recommendations other than referring the customer back to their own GP if they feel necessary. Benefits are similar to those of the ‘Back to Work’ programme.

5.4.3 Fraud Detection

A shared database was established for the creditor market in 1999 using the HUNTER anti fraud system. Currently five insurers are contributing to this system, Pinnacle Insurance, Direct Line, St Andrews, Halifax, and Norwich Union. Royal & Sun Alliance have installed the system and are currently testing. The database holds in excess of 100,000 claims records and is growing at about 4,000 claims per month.

This system receives detailed claims information on a nightly basis. A sophisticated matching and rules system then checks all the data for discrepancies. Typical examples are:-

- Telephone dialling codes which do not match the area post code, usually when a customer reports a mobile number as their usual contact.
- Multiple claims with high monthly benefit.
- Checks a claimant does not have the same address or telephone number as their Employer, Doctor, Solicitor etc.
- Looks for two customers claiming from the same address.

This is only a small sample of the conditions that can be built into the system. In 1999 this has resulted in the detection of a number of serious fraud cases, in addition to providing leads on a number of other successful investigations.

6. MARKET SECTORS

The purpose of this section is to describe where creditor insurance is currently marketed and the features of product design relevant to each sector.

6.1 The Mortgage Market

Products will typically cover accident, sickness and unemployment. Life cover will usually be provided by a separate policy. There is typically a 30 day deferred period (sometimes 60 day), and monthly payments are protected for a maximum of 12 (or sometimes 24) months.

6.1.1 Sustainable Home Ownership – The CML Baseline Product

From 1st July 1999 the Council of Mortgage Lenders (CML) introduced a 'Baseline' Mortgage Payment Protection specification, which sets minimum standards for cover under mortgage payment protection cover. Details of the specification are outlined in Appendix 2. This was the culmination of a year of work between the CML, Association of British Insurers (ABI) and government in order to establish a suitable safety net for mortgage borrowers.

This project has established a target take-up rate of 55% to be achieved within five years. The Target of 55% was selected to be an achievable target taking in to account those without the need for payment protection. Lenders are more actively promoting the cover due to these targets and also due to the shrinking DSS safety net. Currently only about 25% of mortgage borrowers would qualify for any state help with mortgage payments.

6.1.2 Amount of Benefit

The amount of benefit can be selected by the customer and will usually be the monthly instalment under the mortgaged loan. In some cases the benefit can be increased in order to anticipate fluctuations in future mortgage interest rates, or simply to cover mortgage related outgoings, for example, endowment and buildings insurance premiums. The maximum uplift allowed is typically 25%. The borrower selects the monthly benefit at outset, but it is unusual for the borrower to review the amount of benefit as mortgage payments change. Policies allow flexibility to change amounts of benefit as circumstances change but these options are rarely exercised.

The insurer may pay benefits directly to the lender. However, some lenders prefer the benefit to be paid to the customer's bank account from which the mortgage direct debit is collected. This is simpler for the lender to administer, as direct debits do not have to be suspended during a claim.

6.1.3 Premiums

The premium is often expressed as a flat percentage (typically 5% - 6%) of the monthly benefit. However some products on the market are rated according to the personal details of the customer. Rates in these cases will depend on a combination of age, sex, geographical location and occupation, for example.

A table of current premium rates offered in the mortgage market by each lender is shown in Appendix 3.

Premiums may be collected by the lender as part of the monthly mortgage repayment, alternatively a separate direct debit may be collected by the insurer for the insurance cover.

6.1.4 Take Up Rates

The policy is normally sold at the 'point of sale', i.e. at the same time as the mortgage. The take up rate (penetration rate) can vary enormously depending on the lender involved. Most leading lenders will run a 'resolicitation program', offering the cover again after completion of the mortgage using a combination of direct mail and outbound telephone sales to enhance penetration. Typically a total penetration of 20% - 40% can be achieved from branch generated business. Introducers generally have not been successful in providing, or offering, MPPI. This reduces the total penetration.

6.1.5 Free Cover

Some lenders have offered free cover (perhaps with limited benefits) for a period of months, and then tried to convert customers to a wider 'paid for' product at mortgage commencement. At the end of the free period customers are offered cover on a commercial basis. Skipton Building Society pioneered a free unemployment cover for all its borrowers, the customer was offered the opportunity to purchase 'additional' disability and unemployment cover at the time of taking the mortgage.

6.1.6 Unemployment Only Cover

A number of 'unemployment only' products have appeared in the market over the last few years as unemployment rates have fallen. These are usually free cover offers or a step down offer for customers that already have disability cover. There are a number of problems with offering unemployment cover on its own, not least the long term viability and sustainability of cover and rates.

6.2 Personal Loans

The norm here is for full life, accident, sickness and unemployment cover. Some companies also offer critical illness cover too, but this tends to be rather expensive. The period of deferment will typically be 14 days, sometimes 30 days.

6.2.1 Life Cover

The life benefit covers the amount of loan outstanding at the date of death. This is normally reflects the Consumer Credit Act requirements and is therefore calculated using a method called the 'rule of 78'.

6.2.2 Disability and Unemployment Cover

The monthly benefit is the monthly repayment under the loan, including insurance. In this case however, the disability benefit will often not be limited to a fixed period of months, but will often extend to the expiry of the loan, which may be up to 5 years. Unemployment benefits are usually paid for a maximum of 12 months per claim.

6.2.3 Premiums

There are a number of different ways of calculating premiums for personal loans. The best method to use is to apply the premium rates to the Total Amount Repayable (TAR) under the loan. This reflects the monthly benefit inclusive of insurance, which will be paid in event of a claim. Other methods used are Loan plus Interest (=monthly instalment x term) and percentage of Loan, however, for both these methods rates vary according to the interest rate charged.

The lender usually collects a single premium which forms part of the loan. Premiums net of cancels, refunds and commission are remitted monthly to the insurer along with details for each customer.

A table of current Personal Loan premium rates is shown in Appendix 3.

6.2.4 Take up Rates

The insurance is normally promoted on the loan application form. Take up rates are around 60%. Where the cover is not taken initially, it is often promoted with the loan fulfilment pack, and sometimes even a telephone resolicitation programme.

6.3 Motor Finance

This is really a Personal Loan, but for a specific purpose. The same comments apply. However this market place is particularly competitive which accounts for some specific features of the finance package and the creditor insurance itself.

Firstly, the cover itself will often extend to include Critical Illness, at an increased price.

Secondly, the finance can be structured in a number of different ways, a normal Hire Purchase Agreement, a Personal Loan or a Personal Contract Purchase (PCP) arrangement. The PCP contract has a low monthly repayment together with a 'final repayment'. This final repayment will be linked to the residual value (often called a balloon) of the car at the end of the loan term. The insurance cover may or may not include cover for the 'final repayment' element of the loan. If cover is included it would typically be life cover on the final repayment.

6.4 Credit Cards

6.4.1 Cover

Full life, accident, sickness and disability cover is usually provided. The life cover pays off the credit card balance at the date of death. The monthly benefit for disability or unemployment is usually the Minimum Monthly Repayment on the card, which will typically be 10% or 5% of the outstanding balance. Benefits are paid for a maximum of 12 months (10% card) or 24 months (5% card). This benefit structure aims to repay the outstanding balance, plus interest, for those off work for the maximum benefit period.

6.4.2 Premiums

Premium rates are normally charged per £100 of outstanding balance per month. A table of current credit card rates is included in Appendix 3. Premiums are debited from the card account on a monthly basis and are shown on the monthly statement. The credit card company will normally pay the insurer a 'bulk premium' for all its customers.

6.4.3 Take Up Rates

Sales are generated via a simple question on the credit card application form. The insurance will sometimes be (re)promoted using an insert with the monthly statement. Typically take up rates of around 40% are achieved.

6.5 Retail Companies

Again this is really just a special case of the Personal Loan example, people often need credit when buying furnishings or electrical goods. There are some features of the underlying loan agreement that need special consideration when designing and pricing the creditor insurance product. There will often be a 'buy now, pay later' deal, interest free deals or interest free options. The disability and unemployment cover will not normally commence until the end of the initial 'free' period. Life cover normally applies from the start of the loan and is often offered on a 'free' basis to all customers.

6.6 Overdrafts

The cover provided will include Life, Accident, Sickness and Unemployment. Cover is normally provided for the account holder only, but in some circumstances can be extended to cover the spouse as well.

The life benefit can be the amount of overdraft at the date of death or it can be the credit limit. Alternatively the customer might be offered a 'units of cover' approach where the customer selects the life benefit based on their expected utilization, subject to the overdraft limit. The monthly benefits for disability and unemployment vary. Some are linked to the amount of life cover and typically pay 5% or 10% of the life benefit. Others will pay the amount of monthly interest charged pus any overdraft fee. The maximum benefit period is normally 12 or 24 months. Some products include an additional benefit, whereby the overdraft is repaid at a fixed time after the claim starts.

6.7 Utility Companies

Utility companies with 'high street' outlets offer personal loans through these networks. They may also offer cover for utility bills. Cover is typically Life, Accident, Sickness and Unemployment, with a monthly benefit equal to the monthly utility bill repayment and life cover of 12 times the monthly repayment. Premiums are usually charged on a flat rated basis, £3 per month would typically cover utility bills of up to £100 per month.

6.8 Premium Rate Comparison by Sector

Appendix 3, referred to above, includes a full market comparison of premium rates across all providers. It is helpful to summarise typical rates across market sectors. Rates have been converted to a percentage of monthly benefit for east of comparison.

Sector	Typical monthly premium as % of monthly benefit
Mortgage	5% - 6%
Personal Loan	10% - 13%
Motor Finance	15% - 20%
Credit Card	8% - 10%
Retail	10% - 13%
Utility and Overdraft	4% - 8%

It can be seen that the rates vary widely, the key drivers being:-

- **Claims Experience** - Generally, the higher the benefit level, the higher the claim frequency. The method by which the creditor product is promoted can also have a significant impact on claims.

- **Retail Mark Up** - The level of commission reflects the amount of effort required by the lender to promote the creditor product. In some sectors the commission element of the creditor product has become a major source of income to the lender.

7. RISK FACTORS AND RATING FACTORS

Here we discuss the risk factors for creditor insurance and look at how they are used in practice as rating factors.

7.1 Risk Factors for Creditor

7.1.1 Age of Customer

The older the customer, the higher the mortality and morbidity risk. Unemployment incidence follows a ‘U’ shaped curve with the highest incidence being at the youngest and oldest ages.

7.1.2 Employed/Self Employed

The self employed generally have a higher risk of unemployment through their business failing than an employed person being made redundant.

7.1.3 Occupation

Mortality, morbidity, and unemployment rates all vary according to occupational group. For unemployment risks it is difficult to predict where the next recession will hit. In the early 1990’s it was the white-collar workers that were hit hardest by unemployment. Previous recessions affected blue collar and manual occupations. This is an area where an insurer may find itself inadvertently over exposed to a particular sector.

7.1.4 Gender

Females tend to show better rates of mortality, morbidity and unemployment than their male counterparts.

7.1.5 Socio Economic Group

The effect of socio-economic factors on mortality and public health is well documented.

7.1.6 State of Health (Disability &Life)

The better the state of health of the customer base, the fewer life and disability claims. Some affinity group schemes, commonly via credit cards, will cover customers with specific medical conditions. These special circumstances need to be taken in to account in the policy wording and the premium rates modified accordingly.

7.1.7 Type of Credit

Claims experience can vary widely depending on the type of credit offered, even by the same lender. Different types of credit attract different types of customers, which can explain the variation in claims costs.

Claims performance, sales penetration and sales methods can all vary widely from lender to lender. These differences in relation to credit have long been understood by lenders, which is why different interest rates apply. These factors in turn all affect the creditor insurance programme.

7.1.8 New or Existing Borrower

A new borrower will have just been underwritten for credit and so the lender will have checked employment status, earnings and ability to repay the loan. Therefore a new borrower will be a lower risk for unemployment than an existing borrower.

7.1.9 Quality of Credit Underwriting

Prior to the last recession some lenders weakened their credit underwriting standards to increase lending volumes, particularly for the self-employed. This came back to haunt them in higher arrears, many of which subsequently became unemployment claims.

7.1.10 Penetration Rate

The higher the penetration rate the better the spread of risk being achieved and therefore the lower the anti selection. Conversely low penetration often leads to high volatility in claims experience.

7.1.11 Sales Method

The sales method will directly affect the penetration rate and hence the spread of risk.

7.1.12 Size of Benefit

As with many other classes of insurance, the propensity to claim increases with size of benefit. When the policy benefits are very low it may even be the case that the customer does not bother to claim.

7.1.13 Geographic Spread

A regional based lender is susceptible to local variations in risk for mortality, morbidity and unemployment. Larger lenders will have a spread of lending business across the country and will therefore not be affected by regional differences.

7.1.14 Claims Awareness

Some customers forget that they have the cover and so do not claim. Some lender’s arrears controls will include checking whether the customer has a creditor policy and will ensure that the customer makes a claim if they are eligible to do so. Other lenders are less proactive in encouraging customers to claim.

7.1.15 Premium Collection Method

For a monthly mortgage policy, premiums collected by the lender as part of the mortgage repayment are more difficult to cancel than a separate direct debit collected by the insurer. Thus both the persistency and claims experience will be better if the lender collects the premium as part of the repayment as the customer cannot selectively lapse the insurance cover.

7.2 Rating Factors

The list of risk factors in Section 7.1 above is long. In addition, few of them can be quantified as rating factors. Applying the same factor to a similar customer base can produce different results for different lending products. This means that each scheme needs individual assessment and rating.

As a result, very few of the risk factors that have been identified are actually used as rating factors. Rating is based purely on the amount of cover required (monthly benefit, loan amount, total amount repayable, outstanding balance). A few schemes might be individually rated; these will use rating factors such as age, occupation and postcode. However, most schemes will be flat rated, the rate chosen will depend on a qualitative consideration of the risk factors. Many large schemes will be rated according to their own claims experience.

8. PRICING

This section discusses how creditor products are priced, both at a gross premium level and also how the risk cost can be calculated.

The gross premium the customer pays for cover consists of the following elements:

Insurance Premium Tax
Commission
Retention
Expected claims costs
Claims margin/buffer

We now look at each element of the premium basis and how it is incorporated into the gross customer premium rate.

8.1 Insurance Premium Tax

This is levied by the Government on all general insurance premiums and is currently (since 1st July 1999) 5% of gross premiums. The insurer must collect this tax from the customer on behalf of the Government and pass it on to Customs and Excise. The insurer has no direct control over this element of the premium.

8.2 Commission

This is the remuneration paid to the lender by the insurer for introducing the business and retaining the business. The level of commission will largely be determined by the financial and business requirements of the lender.

8.3 Retention

This is the insurer's charge for doing business and it consists of a number of elements, namely expenses, return on capital and investment income.

Retention = Expenses + Cost of Capital – Investment Income.

8.3.1 Expenses

These are the insurer's costs of running the business and will include the costs of administration, sales & marketing, training, IT, literature costs, accounting, actuarial, management and overheads.

8.3.2 Cost of Capital

Shareholders require a return on their capital commensurate with the risks being taken. The insurer is required to put up unencumbered capital (solvency margin) to back the business, the amount of which is laid down by EC regulation. This is supervised by the Financial Services Authority who, for practical purposes, requires companies to hold higher than the statutory minimum amount.

8.3.3 Investment Income

This is the income that the insurer earns on reserves invested and as such can be viewed as an element to offset expenses. As creditor is a very short tailed business funds are not invested for very long before they have to be used to pay claims, so this element can be relatively small.

8.4 Expected Claims Costs

In general terms this is what you will expect to pay out in claims and is the risk premium.
For a creditor premium the formula for expected claims costs is in essence very simple and can be summarised as follows:

Expected claims cost = incidence rate x monthly benefit x average duration of claim

The costs are summed over the term over the policy for each benefit that is offered. For example the risk cost for a single premium personal loan product providing life, disability and unemployment benefits is:

$$\sum_{t=1}^{n} SA(t)\, q_{x+t/12}/12 \;+\; MB\, i^{d}_{x:t}/12\, a^{d}_{x:n-t} + MB\, i^{u}_{x:t}/12\, a^{u}_{x:n-t}$$

where n = term of the loan in months

$SA(t)$ = the outstanding loan amount at duration t

$q_{x+t/12}$ = the annual mortality rate at age x and duration t

MB = the monthly benefit, i.e. the monthly loan instalment inclusive of insurance

$i^{d}_{x:t}$ = the annual disability incidence rate for age x and duration t

$a^{d}_{x:n-t}$ = the average duration of a disability claim at age x for outstanding duration n-t

$i^{u}_{x:t}$ = the annual unemployment incidence rate for age x and duration t

$a^{u}_{x:n-t}$ = the average duration of an unemployment claim at age x for outstanding duration n-t

The incidence rates and average duration of claim need to be assessed for each particular benefit. There are three main methods that can be used to calculate these:

8.4.1 Scheme Experience

This is the best method of determining the expected claims costs. Scheme experience should be measured over a number of years due to variations in claims experience according to economic cycles. Care is needed in interpreting experience where premium rates and cover have changed over the period of review.

For a new scheme, claims experience of similar schemes can be used for initial rating.

8.4.2 Published Statistics

In the absence of any scheme experience, published statistics can be used with appropriate modifications for insured experience. As business is written and scheme experience develops this can replace published statistics. In the UK there is a wealth of information published by the Office for National Statistics.

8.4.3 Estimation

Sometimes there will not be any insured experience or published statistics to use, for example in a market where there are no national statistics collected and no insured cover has been offered. This is the situation in South Africa for unemployment cover, which is starting to be offered now as part of credit life programmes. In these circumstances some educated guesswork is needed to get some initial rates that can then be modified as experience develops.

8.5 Claims Margin or Buffer

Once the expected cost of claims has been arrived at a margin needs to be added to allow for variability of claims. The cost of claims is necessarily a best estimate of what the claims will be and so in practice, even in a stable external environment, there will be differences in claim costs from year to year. Thus the claims margin acts as a buffer against adverse experience. If there is a profit share element to the pricing structure then a planned profit margin will need to be added as well.

8.6 Differential Pricing

In the UK creditor market most schemes are rated globally with the same rate applying to all customers whatever their risk factors. This is pooling of risk in its widest sense, so does not charge people with different risk profiles different rates. There are large cross subsidies from the good risks to the bad risks. Differential pricing attempts to distinguish between the different levels of risk and charge a premium appropriate to that level of risk.

Provided that suitable claims data and policy data is available, it is possible to construct rates that differentiate between different types of risk. The first step is to identify possible risk and rating factors and determine their importance in the propensity to claim. There are a number of statistical techniques that can be used. Care is needed as some factors are correlated.

The most important risk factors can then be developed in to rating factors and an appropriate pricing structure built up. There are a few schemes that are marketed on this basis but they are rare. Most lenders, having considered the pros and cons of rating for risk, have decided to opt for the simple approach of the same rates for all customers.

Differential pricing is unusual in the UK, but in Germany, for example, rates are usually banded by age and policy term.

8.7 Insurance Scoring

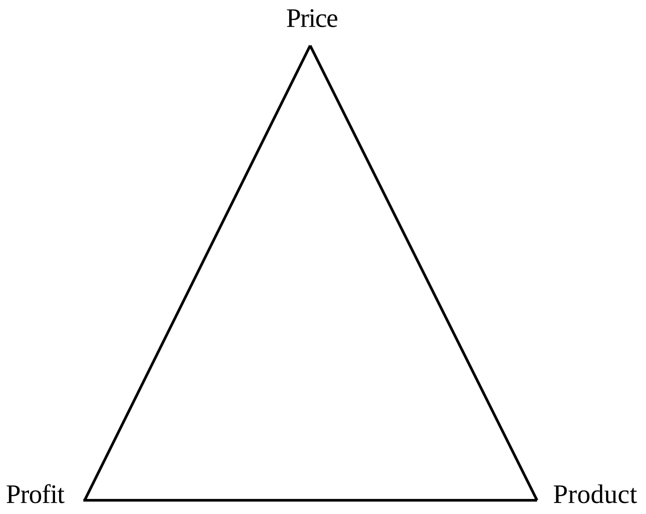
Lenders with captives can use a combined credit and insurance scoring package. As this is a captive arrangement, the selection of those customers that score well on both insurance and credit enhances the profitability of the group. Some factors, such as security of employment, impact insurance and credit risk in the same way. However, other factors, such as age, do not. The older customer is a good risk for credit but a bad risk for insurance.

What this means in practice is that some customers who would have been accepted for credit under a credit score would not be accepted under a combined credit and insurance score. Conversely there will also be some customers that are now acceptable but previously were not.

8.8 Commercial Considerations

Once a proposed rating structure has been arrived at it will need to be compared with other rates in the market. Commercial pressures might lead to a higher or lower rate being proposed, a lower rate might be offered based on current claims for a monthly scheme where the insurer can change the rates quickly should experience deteriorate. In a captive situation it might be better to charge a higher rate, which is sustainable over the longer term.

The lender will have their own ideas about the product to be offered, the price it is offered at and the profitability of it. There is a trade off between the product offered (cover), the price at which it is offered and the profitability. This can be summarised in the rating diagram below, an average product is terms of cover, pricing and profitability will be in the centre of the triangle, whereas the most competitively priced contracts will be at the top of the triangle. The positioning of the product will be a joint decision between the lender and the insurer.



8.9 Profitability

Creditor programmes should be regarded as a partnership arrangement between the insurer and the lender, to the mutual benefit of all, including the customer. Both the insurer and the lender have an interest in the profitability of the programme.

The profitability of a creditor scheme to the lender will depend on:

- Amount of Advance Commission
- Cost of distributing the product
- Amount of Insurers retention
- Amount of any profit share arrangement

The amount of advance commission that the lender receives to pay for the cost of distributing the product varies from market sector to market sector, and from lender to lender. The first requirement is that there must be sufficient funds to pay all valid claims. There should then be sufficient retention to allow the insurer to manage the programme effectively and efficiently in terms of new business, claims handling and administration processes. The retention will also include the cost of any sales and marketing support that is requested by the lender to ensure that the product is offered as widely as possible, and that the customer has sufficient opportunity to buy the product.

Profit share arrangements are a feature of the creditor market for the larger lenders. To call it profit share is probably misleading and is a legacy from the sales positioning of creditor insurance in the 1970s. The fund that is available after the payment of claims, allowing for reserving, any commission paid and the insurers retention is really a result of the way the programme has performed in relation to the premium rates that were set. A better description of the fund is that it is a rating experience refund (RER).

It is important that both the lender and the insurer retain a share of any RER. Clearly the insurer has to retain an interest in managing the claims process and the resulting claims experience. Additionally the lender should also retain an interest to ensure that all valid claims are paid. This method of sharing the RER ensures that a balanced view is maintained when the lender and insurer jointly review any grey claims.

The profitability of a creditor scheme to the insurer will depend on :

- The insurer’s expenses compared with the retention
- The investment income that is earned
- The actual level of claims compared with expected claims

One might expect claims experience to be the most important contributor to profitability for the insurer. However, the profit shares enjoyed by the major lenders mean that most underwriting profit is ultimately returned to the lender. The insurer benefits little, if at all, from good claims experience. On the other hand the insurer will suffer all the losses if claims exceed the claims allowance in the premium basis. Regular monitoring of claims experience is vital in order to anticipate future deterioration before a scheme moves into loss.

For the insurer the most important contributor to profitability is the level of expenses compared with the retention charged to each scheme. For large schemes, the competitive nature of the market means that these will almost certainly be costed on a marginal basis and so other schemes will have to cover the overheads.

Investment income is also a contributor to profit. However, in the current low interest rate environment investment income will only contribute a small amount to the total. In addition, many profit sharing schemes will receive credit for the investment income, thus reducing the insurer’s profit margins.

9. CLAIMS INCIDENCE RATES

Claims incidence rates are a central part of the technical basis for pricing, claims incidence rates are illustrated using published data.

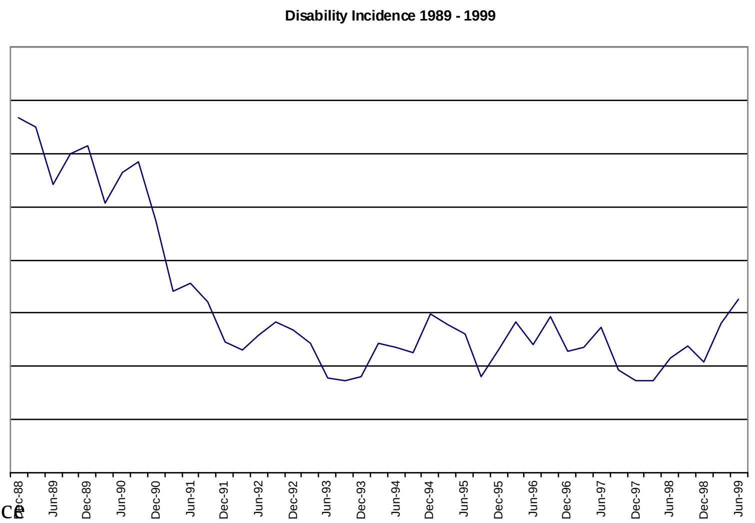
9.1 Mortality

Mortality tables are published in the UK for both assured lives and the population. Most creditor schemes will have mortality experience closer to population mortality than assured lives mortality due to the minimal initial underwriting that is done. If scheme experience is available then this can be compared with a standard table.

9.2 Morbidity

National disability statistics are available for those claiming state disability benefits. The benefit currently provided by the state is Incapacity Benefit, which is based on a stringent 'all work' test. Prior to this Invalidity Benefit only required the claimants' own GP to sign them off for them to receive benefit. Thus the disability incidence rate varies widely between these two types of similar benefits.

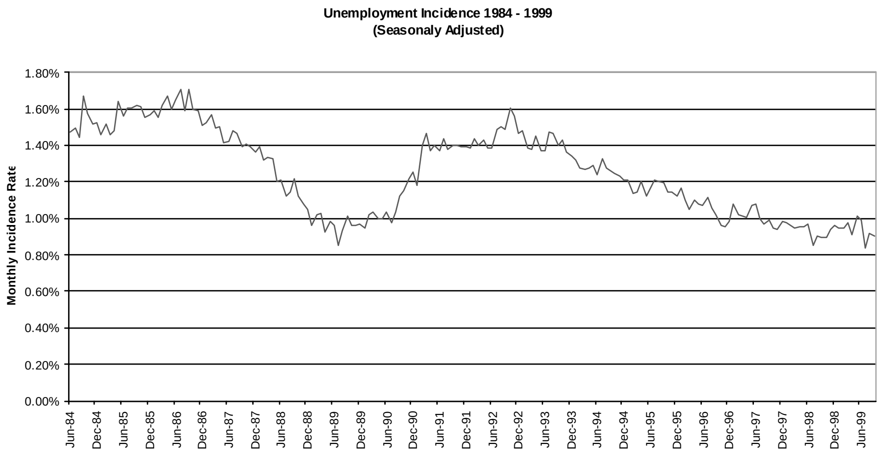
A specialist insurer will have plenty of claims data to build their own inception rates. Standard benchmarks exist for Permanent Health Insurance, which are detailed in the CMI reports. Disability incidence tends to be a bit more stable over the cycle but does show a cyclical trend over a period.



Source: Pinnacle Insurance

9.3 Unemployment

National unemployment statistics are published monthly and from these unemployment incidence rates can be calculated. Specialist insurers will have their own claims data for comparison. Both unemployment incidence rates and disability incidence rates vary according to the economic cycle. This is especially true of unemployment incidence and can be seen in the graph below.



Source: NOMIS

10. DURATION OF CLAIMS

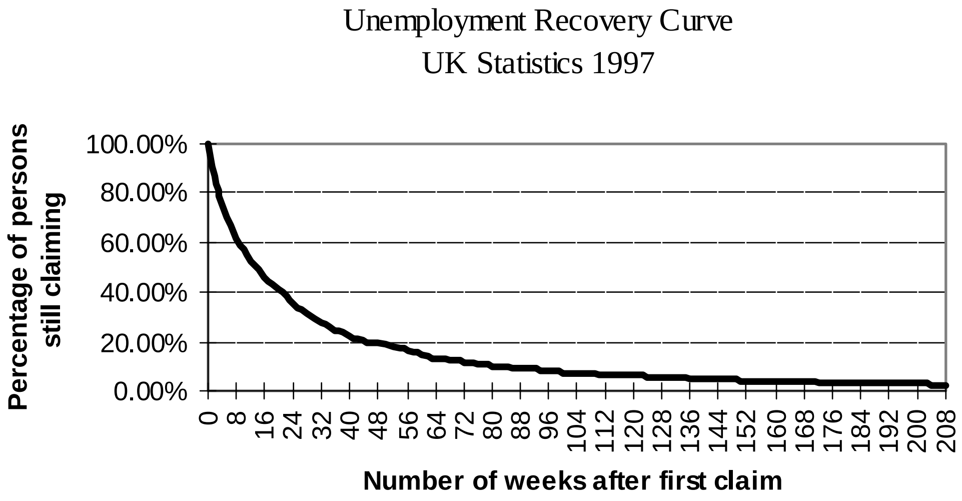
For unemployment and disability pricing the duration of a claim is needed to complete the pricing basis. These vary over time due to economic circumstances. In a recession claims last longer as it is more difficult to find a new job. This phenomenon is seen in disability claims as well as in unemployment claims.

10.1 Duration of Disability Claims

National statistics are available giving durations of disability at a high level. These are not detailed enough to be useful for pricing. Scheme experience can be used to develop annuity factors for various different benefit options, these are usually derived from a recovery curve which shows the number of days of expected disability at various claims durations.

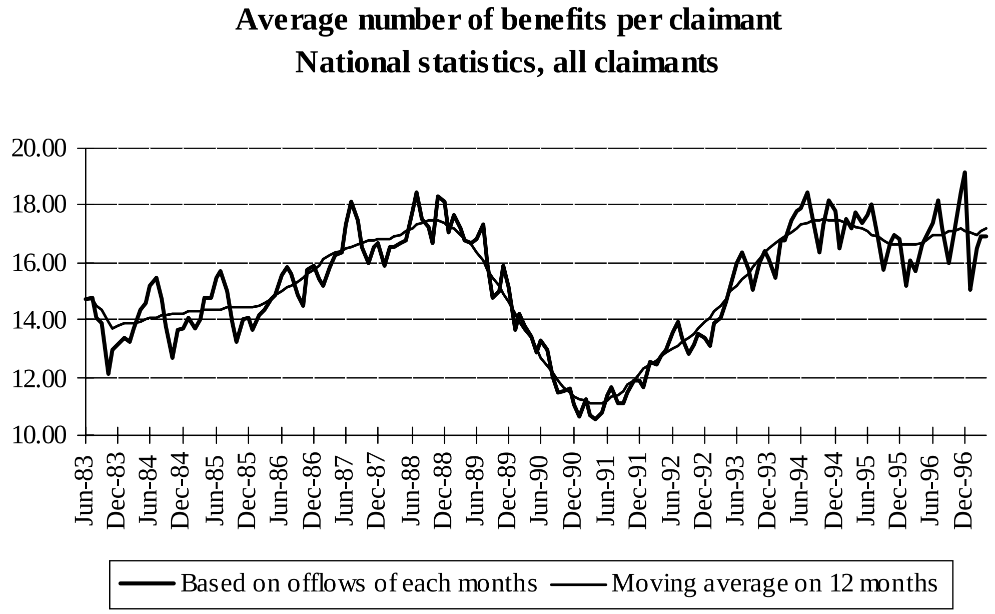
10.2 Duration of Unemployment Claims

The offlow statistics can be used to derive recovery curve and annuity factors for unemployment claims. However, there is a big problem with unemployment offlow statistics as these are prone to adjustment by the Government of the day. The Recovery Curve graph shows that 80% of claimants have returned to work within 12 months.



Source: ONS

The graph below shows that the duration of unemployment follows a cyclical trend.



Source: ONS

11. RESERVING

The principles of reserving are the same as for any class of insurance. The reserves held for creditor business must satisfy the requirements of the Insurance Companies Regulations.

For short-term business the regulation is limited to the requirement that the amount of reserves shall be determined in accordance with generally accepted accounting concepts, bases and policies or other generally accepted methods appropriate for insurance companies.

For long-term business the regulations are more prescriptive. There is a statutory minimum valuation basis specified by regulation, which is a net premium basis. Any reserves held, must exceed the statutory minimum requirement.

The long-term business is generally a small part of a creditor portfolio and therefore the reserving methods follow General Insurance principles but with a check that the long term reserves meet the statutory minimum basis. Normally any life Unearned Premium Reserve is well in excess of the required net premium reserve.

There are some methods of reserving that are particularly suited to creditor insurance and these are discussed below.

11.1 Premium Reserves

11.1.1 Unearned Premium Reserves (UPR)

For single premium business an Unearned Premium Reserve needs to be held in respect of cover for future periods of insurance, for which a premium has been received already. For monthly premium business some insurers will hold half a months premium as a reserve, others do not hold UPRs for monthly business.

Premiums are normally earned on a straight-line basis for profit share purposes, i.e. according to the rule of 12 (or rule of 365).

For management accounts or statutory reporting, premiums may be earned more quickly. Life cover premiums are normally earned according to the Rule of 78 because the amount of risk reduces over time. Disability and Unemployment premiums may be earned according to Rule of 45 – this is an average of the rule of 12 and rule of 78 earnings methods. (The rule is so named because (12+78)/2 =45).

11.1.2 Unexpired Risk Reserves

If the premiums charged are thought to be inadequate then an additional unexpired risk reserve may be set up. This might be required during a recession when premium rates were charged based on prior claims experience which was lower than that being experienced.

11.2 Claims Reserves

11.2.1 Claims In Course Of Payment (ICOP)

These are reserves for claims that have already been accepted and payments have commenced. There are a number of different methods that can be used for these reserves:

Inception Annuity Method

For each claim in course of payment a reserve is set up for the expected number of payments still to be made given the number of payments that have already been made. This would normally be done on the basis of a company's own data, using recovery curves to calculate annuity factors. Some companies, however, use a fixed factor irrespective of the duration of the claim. During a recession the duration of claims tends to increase, so the annuity factor must be able to take account of expected trends (i.e. worsening factors).

Triangulation Methods

These are the methods actuaries typically look to use for all types of general insurance reserves. However, a number of assumptions underlying these methods are inappropriate for creditor business:

- Triangulation methods assume a stable pattern of claims over time – this may be true during a prolonged period of stable unemployment, but during a recession numbers and durations of claims increase dramatically making the stable pattern assumption invalid.

- These methods assume no changes in claims handling, reporting and settlement patterns. When volumes of claims increase substantially over a short time period, this puts extra strain on a claims department and backlogs can build up. In addition the 'acceptance rate' – the proportion of notified claims that are accepted – can vary widely over a period of time. Typically mortgage lenders will insist that every claim is paid whereas finance houses concentrate more on the bottom line and are happy for 'grey area' claims to be rejected. If the mix of business of a creditor book changes then the claims payment patterns will also change.

- The advantage of a triangulation method is that it can be used for ICOP and IBNR reserves without making specific assumptions about the business. However, you do not know explicitly what assumptions have been made.

11.2.2 Incurred But Not Reported (IBNR)

These reserves are held for claims that have occurred before the reserving date but have not yet been reported to the insurer. There are two main methods of reserving for IBNR claims.

Delay Tables

A delay table is drawn up based on historic data, this might show, for example, that 50% of claims are reported in the month of occurrence, 25% a month late, 10% two months late and the remaining 5% are reported three months late. This table can then be used to gross up the number of claims actually reported to date in order to calculate the number of IBNR claims.

Another delay table method is to calculate the average reporting delay in days for each scheme. The number of claims reported in a particular month can be multiplied by the average delay and divided by the number of calendar days to get an estimate of the total number of claims that have occurred. The number of IBNR claims is equal to the total number of claims estimated to have occurred less those already reported.

Once the number of IBNR claims has been established, the IBNR reserve can be calculated by multiplying by the acceptance rate, average monthly benefit and average claim duration (annuity factor at time zero). This is normally done at a scheme and benefit level.

Triangulation Methods

If a triangulation method is used for reserving then IBNR can be included within these calculations.

11.2.3 Notified But Not Admitted (NBNA)

These are claim forms that have been received but a decision to accept or reject has not been made because some information is missing or some additional information had been requested, such as a doctor's report, but had not yet been returned. As the number of claims falling in to this category are known they are dealt with in a similar way to IBNR reserve using acceptance rates, the amount of monthly benefit being claimed and annuity factors for the benefit type.

This reserve can be important for proper reserving during a recession when the volume of claims increase dramatically over a short time period.

11.2.4 Claims Equalisation Reserves

These are not required by the Financial Services Authority and so are not allowable for tax purposes.

12 TAX

12.1 Policyholder Tax

12.1.1 Disability and Unemployment Cover

Insurance Premium Tax (IPT) was introduced on 1st October 1994, initially at a rate of 2.5%, on all general insurance premiums. It was increased to 4% on 1st April 1997 and was increased again to 5% on 1st July 1999. The insurer must collect this tax from the customer on behalf of the Government and pass it on to Customs and Excise.

The original draft regulations issued in 1993 had been drafted with annual premium household and motor policies in mind, with the result that there was a retrospective nature of the tax for single premium creditor policies. In April 1997 a penal rate of IPT at 17.5% was introduced on certain types of business, although the penal rate does not apply to creditor, the draft regulations did capture some creditor business. Creditor business is different from other mainstream general insurance covers and so any changes in IPT regulation need careful scrutiny, and sometimes lobbying, to ensure that creditor does not attract unfavourable treatment.

The disability and unemployment benefits of a creditor policy are tax free in the hands of the recipient.

12.1.2 Life and other long term covers

Any life or critical illness benefit is subject to the taxation rules for non-qualifying life assurance policies. Death or disability constitutes a chargeable event for tax purposes. However, for practical purposes, no tax will be due as the taxable gain is based on the excess of the surrender value over the premiums paid. As the surrender value never exceeds the premiums paid there will never be a chargeable gain.

12.2 Company Tax

General insurance business is taxed on profits.

Any long-term business falls under the life assurance company taxation rules. Creditor policies generate excess E, which can be utilised to offset Investment Income. Thus creditor insurers are often active in the single premium bond market since they can offer better returns to investors than a fully net office.

III. UNEMPLOYMENT FUTURE

13. MARKET ENVIRONMENT

The current Government is escalating the pace of State disengagement from the provision of welfare, health care and pensions. The need for this process has been recognised for some time by all the main political parties. The reasons are well documented; the changing demographics; the increased longevity of life; the improvement in medical treatment. Governments of both the major parties have presided over periods in office during which the commitment to provide support was met out of the current years income. Funds that were collected under the guise of National Insurance were diverted away from what many members of the public feel was their right. That is the right to claim benefit if they were unemployed; the right to have disabilities treated quickly and without consideration of the cost; and the surety that the State would provide in old age. This diverting of funds by the State is diametrically opposed to the current proponents of hypothecation.

The State disengagement has provided the opportunity for insurers to develop products that fill the gap left by the State, however many of these, including creditor insurance, have yet to be considered by customers as a critical purchase.

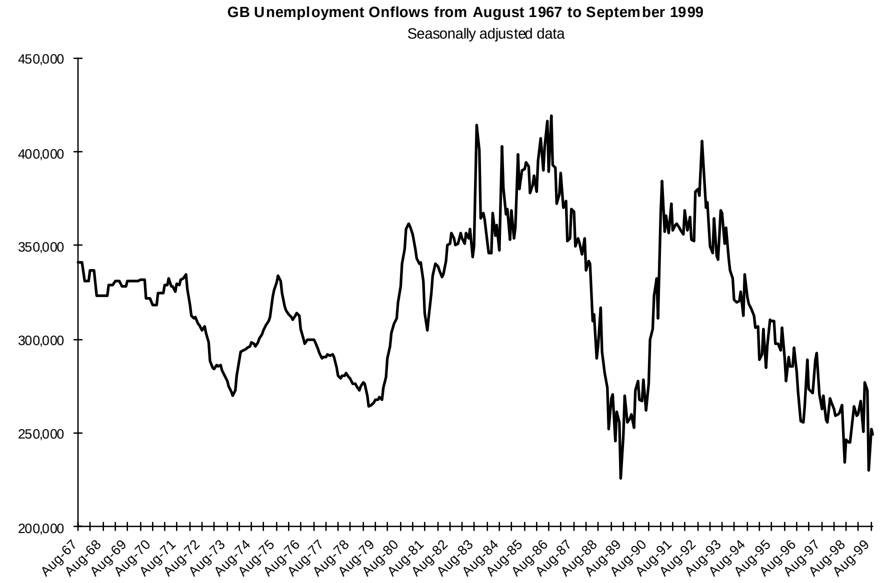
13.1 The Next Recession

Since 1994 unemployment numbers, onflows and claims have shown a falling trend. What are the prospects for unemployment in the next Millennium? Are we going to see increasing unemployment and perhaps another recession or will the future pattern be stable with continued low levels of unemployment? This section tracks some economic indicators over a number of years and compares these with unemployment over the same period.

13.2 Unemployment Onflows

National unemployment statistics are published monthly, these include the total claimant count, onflows and offlows. The total claimant count is the unemployment number that is widely reported, but this is not that relevant for insurance. Of more interest are the ‘Onflows’, which are new people registering as unemployed with the benefit office. Ultimately if these people stay out of work they will become claimants under a creditor policy.

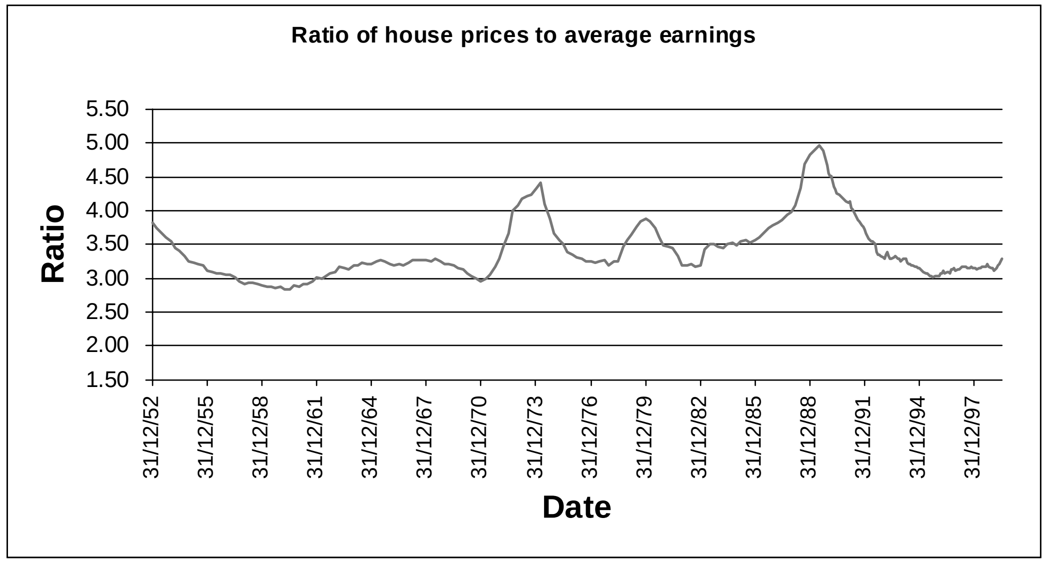
The graph below shows the Unemployment Onflows for Great Britain (seasonally adjusted) from 1967 to 1999.



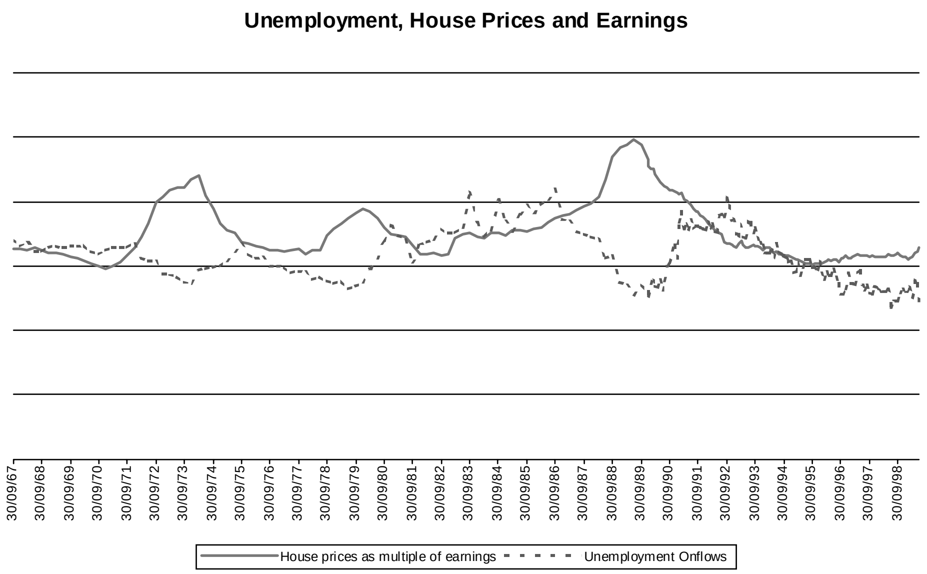
Source: NOMIS

13.3 House Prices

The graph below shows house prices divided by national average earnings, which gives an indication of the affordability of houses. At the moment the ratio is relatively low with house prices being approximately three times national average earnings.



The next graph superimposes unemployment onflows on top and shows that high multiples of earnings are associated with low unemployment and vice versa.



13.4 Mortgage Possessions and Arrears

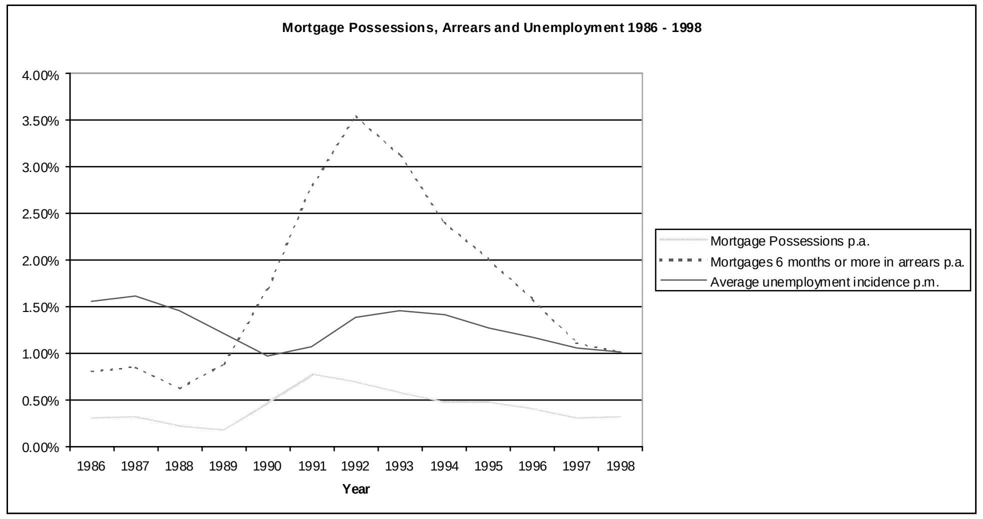
Unemployment is one of the causes of arrears and possessions and so one might expect these to be correlated with unemployment. However, job loss only accounts for about a quarter of the arrears and possessions cases. The reasons for arrears and possessions are shown in the table below.

Main Reasons for Arrears and Possessions

	Main Reason For Arrears	Main Reason For Possessions
Job Loss	23%	24%
Illness/Disability/ accident	8%	2%
Loss of Earnings	23%	20%
Failed Self Employment	12%	18%
Relationship Breakdown	10%	14%
Giving up work to have a baby	3%	5%
Unexpected Bills	2%	3%
Credit Commitments too high	4%	0%
High Interest Rates	3%	11%
Other Reasons	14%	2%

Source: Mortgage, Arrears and Possessions: Perspectives from Borrowers, Lenders and the Courts HMSO

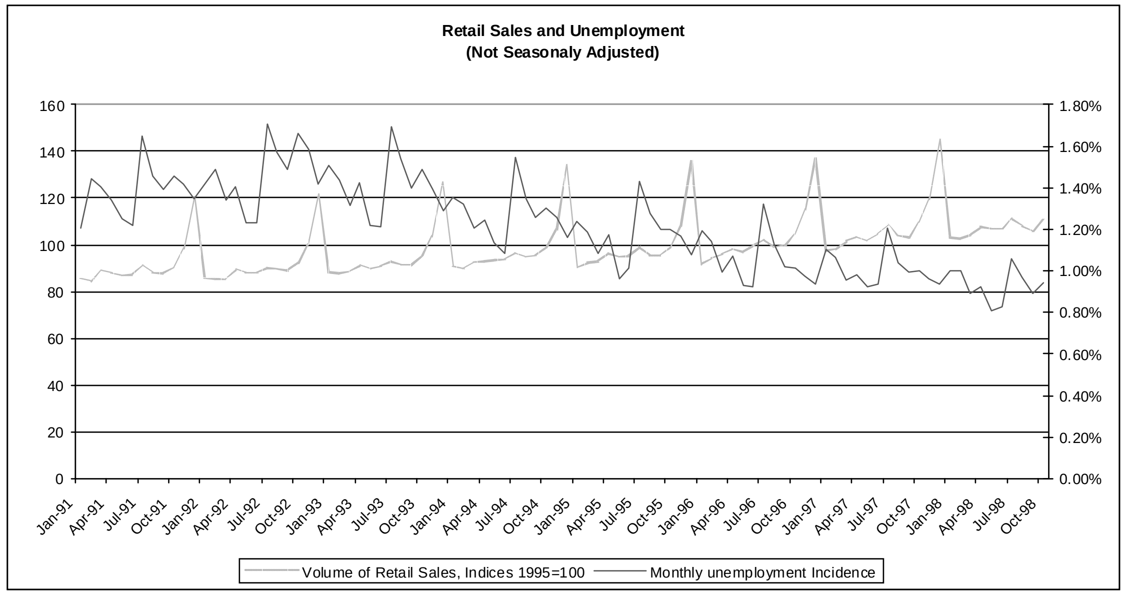
The graph below shows the percentage of mortgage possessions and arrears each year as a percentage of mortgages in force at the end of the year. Average monthly unemployment incidence rates have been superimposed on this. The unemployment incidence graph is the same shape as the possessions graph but with a twelve-month lag.



13.5 Volume of Retail Sales

The volume of retail sales reflects the trends in overall consumer's expenditure and the level of consumer confidence at any time. The volume of retail sales increased by a fifth between January 1991 and January 1998. Retail sales follow a strong seasonal pattern, peaking in December each year. For example, the weekly average in December 1997 was just over a third higher than the average for the year as a whole. This is followed by the slowest period of sales for the year; the average for the first three months of 1998 was over 29 per cent lower than the average for December 1997.

Unemployment incidence also shows strong seasonal patterns with a peak in July each year. As might be expected unemployment and retail sales show opposing trends.



13.6 Future Environment

The move towards acceptance by consumers for the need to provide for one's own welfare is probably going to be generational. There is evidence that many twenty and thirty year olds have seen the lack of provision made by grandparents and the subsequent financial drain on their own parents. As a result, many are now consciously setting aside sufficient funds in order to provide for themselves.

Traditionally, creditor insurance has only been available through lenders at the time a lending agreement is completed. There have been a number of lending companies who implement resolicitation programmes in the month immediately following the commencement of the new financial commitment. Periodically lenders, especially mortgage lenders, will offer customers the opportunity to buy the product. Until now the distribution channel and the timing of the offer has largely been at the discretion of the lender. However the use of new technology is slowly changing this. In the mid 1990s General Accident launched a creditor insurance product aimed at existing mortgage holders. This was a product not linked to a particular lender's mortgage but enabled the customer to select a level of cover at a premium that varied dependent on the post code, age and sex of the customer. The premium that the customer paid was often lower than that provided by lenders. The early attempts at matrix rating of a creditor product was made possible by the improvement of data held and speed of computers, coupled to an effective telephone call centre.

New technology and the speed of the spread of the internet will provide the opportunity for customers to seek out products that suit their needs, and importantly their pockets, from a wider variety of sources. Currently it appears that only two creditor insurance suppliers have made a product available by the internet via this route.

14. UNEMPLOYMENT COVER FOR PENSIONS

Unemployment cover can normally be offered on any regular commitment. It has been offered on life assurance premiums and on motor and household premiums. However, it has not been offered on pension contributions, arguably a more important regular commitment, due to regulatory constraints.

14.1 Why Can't Unemployment Cover be Offered Now?

The Income & Corporation Taxes Act 1988 allows that a personal pension scheme making provision for insurance against 'a risk relating to non-payment of contributions' shall not be prevented from approval. However, current Inland Revenue Practice is to restrict the benefits that may be provided under this section to waiver of contributions during incapacity only. Thus the current legislation already allows for unemployment cover to be provided under personal pensions, it is only prevented by Inland Revenue practice.

14.2 Stakeholder Pensions

Consultation Brief 6, Stakeholder Pensions - The Tax Regime, was issued in October 1999 and contained several important proposals that have opened the door to providing unemployment cover on pension contributions.

The first was the proposed removal of the link between contributions and earnings for contributions up to £3,600 per annum. This means that a person can now pay contributions to a pension scheme even if unemployed, which currently is not the case.

The second was the proposal to remove the carry forward/ carry back provisions and replace them by allowing contributions to be made for up to five years after termination of employment.

This consultation brief also sought views on life and other rider benefits, whether the rules relating to rider benefits should be changed and how limits for rider benefits should be set.

As the link between contributions and earnings has been broken, the only question seems to be whether an unemployment rider benefit would be inside or outside of the tax wrapper.

14.3 Benefits to the Customer

For people who have recently been made unemployed their resources will be most stretched following unexpected unemployment. At this time their main aim will often be to reduce or pay off debts if they have received any redundancy money. It is unlikely that their pension contribution will have a high priority, as it is discretionary expenditure.

Whilst pension contribution holidays may be taken, the long term consequences of missing pension contributions for a number of months are significant but not often appreciated by the person at this time of financial stress. Even a relatively short suspension of contributions early in life has a disproportionate effect on ultimate entitlement, particularly in a low interest rate environment. For example a person contributing say £100 per month who experiences two periods of unemployment of 9 months between the ages of 20 and 30 would lose on average three times more pension at retirement than a similar individual in the same situation aged between 40 and 50, this equates to approximately 9% of the pension fund.

14.4 Benefits to the Pension Provider

For the pension provider there are a number of significant benefits in providing unemployment cover in conjunction with a pension:

- Security of income stream as pension contributions can be maintained by policyholders during periods of unemployment.
- Improved policy persistency and therefore faster recovery of initial set up costs and reduction in administrative costs.
- Opportunity to make a margin on unemployment risk rates.

14.5 Benefits to the State

If individuals take on responsibility for providing their own pensions then this reduces their dependence on the State. Unemployment cover can ensure maintenance of contributions during unemployment and thus reduce the burden on the State even further.

14.6 Unemployment Cover on Pensions - The Future

Assuming that the proposals for stakeholder pensions go forward and the link between contributions and earnings is removed, then it will be possible to offer unemployment cover on Stakeholder Pensions from their inception in 2001. Moreover, the proposals also suggest that Personal Pensions will be brought under the same regime. The only thing preventing companies offering unemployment cover on personal pensions now is Inland Revenue practice. Given that this will be allowed from 2001, it may be possible to introduce this earlier by lobbying Government.

15. OTHER PRODUCT OPPORTUNITIES

15.1 Premium Protection

The case for including creditor insurance on pension contributions is well made, but there are many other insurance products that lend themselves to either including creditor insurance as a premium protection, or to developing a variant of an existing product.

Simply stated premium protection is the addition of an extra nominal amount, no more than one pound a month in some cases, on the main insurance premium e.g. car or motorcycle insurance. The benefit pays the customer's monthly premium should they suffer disability or unemployment. The premium protection product, although not uncommon on car and motorcycle insurance, has yet to be sold with other general insurance, such as contents.

Other variants of the creditor insurance would be a 'super waiver' on life insurance products. Market sources estimate that less than 12% of customers with life and endowment policies will take out waiver of premium. The reason for this low rate is that there is a reluctance of the seller to 'complicate' what may be a relatively simple sale. Super waiver is simply a short term disability and unemployment product that requires no medical underwriting; instant acceptance is guaranteed. Cover is immediate and the first month a customer cannot meet the premium for the life or endowment product, then the super waiver starts to pay, usually for a period of twelve months. Clearly the twelve month benefit period is different to the extended benefit provided by a traditional waiver of premium, but a combination of the products is possible, with the longer term disability element being provided by the life assurer in the normal way.

A combined creditor insurance and PHI product would provide benefits that would appeal to customers, at a realistic premium. The customers that have the propensity to buy a PHI product will often also buy creditor insurance. It therefore makes sense to offer a joint product. The short term nature of the creditor product (a 30 day waiting period for both disability and unemployment with a twelve month benefit) means that the customer has a wider more immediate cover. This also allows the PHI element of the cover to have a twelve month deferment period which greatly reduces the premium for this long term benefit.

15.2 Other Financial Commitments

Although the original market for creditor insurance was the lending market, it has now developed so that any regular financial commitment can be covered. There are products on the market that provide cover against disability and unemployment that are not linked to any formal finance agreement. The customer is free to make the choice of which of their regular commitments to protect; council tax; telephone bills; sports club membership; internet bill. In fact any regular financial commitment is able to be protected.

16. CAN PRIVATE INSURANCE REPLACE STATE BENEFITS?

Currently unemployment benefits, in the form of job seekers allowance, are paid from public funds and administration is provided by the public sector. In addition, Income Support for Mortgage Interest is paid to some unemployed borrowers. In 1996/97 £2,803 million was paid in unemployment benefit and job seekers allowance in Great Britain (source Government Statistical Service website 4/10/99). Mortgage payment protection schemes cover about 20% of mortgage borrowers and we estimate that benefits received are about £250 million per annum.

Here we look at some alternative ways of administering and funding unemployment benefits. If unemployment benefit were to be privatised, then this is likely to be a two-stage process with the private sector first taking on the administration of benefits and then privatised funding could follow.

16.1 Public Funding, Private Administration

Benefits continue to be paid from public funds but administration is provided by outside agencies, such as insurance companies, who have experience of administering similar schemes.

If administration is carried out privately it could be decentralised to a number of Regional Administration Companies, who could be chosen by tender. These administrators need to be a minimum viable size so that work is conducted efficiently. Branches could be at existing benefit office locations with some smaller units being replaced by mobile offices.

Some claimants would need to claim by post due to distance from their nearest office. Arrangements would need to be made to visit these claimants to process their initial claim and to check progress with job seeking. Other mobile staff would also be needed to check and investigate cases of fraud.

A centralised computer system networked between offices would be needed to aid administration and check up on fraud. Modern technology, such as computers, telephones, ISDN and the internet, can be used to improve efficiency but would require considerable capital investment

16.2 Private Funding, Private Administration

A new scheme underwritten by the private sector could be introduced to replace or complement existing benefits. This could either be a compulsory or optional scheme.

16.2.1 Compulsory Scheme

Advantages of a compulsory scheme over an optional scheme are:

- Reduction in cost to the State as individuals bear the cost
- Enables cross subsidies between different risk groups, reducing costs for higher risk groups
- Allows cover for all including high risk groups
- No anti selection risk

Disadvantages

- No right of rejection for bad risks
- Good risks are cross subsidising bad risks

Specific Contribution Scheme

This scheme would be operated in a similar way to the existing contributory job seekers allowance, but with specifically allocated contributions. Benefits are provided for claimants from a pool of contributions received. There would be an automatic right of entry to the scheme for all eligible employees. This means that there will be cross subsidies between different groups of employees, as premiums are not related to the risk of becoming unemployed.

Conventional Insured Scheme

This scheme would be operated more in line with conventional insurance principles with a link between contributions and benefits and could take in to account specific risk factors. Risk factors might include the following:

- ***Industry or Occupation*** **–** the risk of unemployment varies by occupation, the unskilled worker is more likely to be made unemployed than a professional person, for example. Thus the contribution rate as a percentage of the benefit would vary by industry or occupation to reflect the level of risk. A maximum and minimum rate could be applied to ensure that the scheme would be affordable to all. Thus there is still an element of cross subsidy from good risks to bad risks.

- ***Employer*** **–** In a similar way that occupation can be used as a factor for rating, another approach might be to rate according to type of employer. This could take in to account the employer's approach to employment policy, for example, if a "hire and fire" approach was used a higher rate would be charged. The employer could be charged for the cost of the insurance or the cost could be collected by the employer on behalf of employees. Thus an employer might think more closely about making staff redundant if it would increase premiums charged.

- ***Income Related Benefit*** **–** Once a relationship between benefits and premiums has been established, it is then possible to link benefits and premiums to income. For example, premiums could be charged for earnings below a certain level to provide a basic flat amount of benefit. An additional premium could be charged for earnings above a minimum level to provide a benefit related to a percentage of earnings. There would need to be a maximum amount of benefit to ensure that the scheme met genuine needs but still provided an incentive to return to work.

- ***Individually Underwritten Scheme*** **–** This type of scheme would take into account a range of rating factors about the individual employee and would be similar to other types of conventional insurance in its rating. The rating factors might include age, sex, amount of benefit, address, occupation and employment history.

16.2.2 Optional Scheme

This is an insured scheme with a range of benefits devised to match contributions. If such a scheme is implemented then there will be insured and non-insured people in the population and so a state provided safety net will be required. The way such a scheme would operate would be similar to the insured compulsory scheme described above. However, there are some important differences and issues that will arise and these are discussed below.

Freedom of choice

An optional scheme allows freedom of choice, an individual can chose whether or not to have cover, who the provider will be and how much cover to have. The individual can chose the scheme best suited to their own circumstances and can feel that the premium charged will reflect their risk so that they are not subsidising bad risks.

Individual Responsibility

Individuals are encouraged to take responsibility for their own welfare and such a scheme encourages self-help. On the other hand, an individual may have no incentive to take out suitable insurance cover.

Opt In problems

With an optional scheme there will need to be provisions for people to be able to opt in or out. In addition there will need to be a safety net for those that do not take the insurance and suffer financial hardship on becoming unemployed.

Anti Selection

As the insurance is optional, there is an anti selection risk in that those that think they have a high risk of becoming unemployed are more likely to take out cover than those that do not have such a risk. Underwriting to filter out bad risks or to charge more for the bad risks can reduce this risk.

Fraud

There is a moral hazard with this type of income replacement insurance and cases of fraud need to be identified and weeded out.

Insurability

Not everyone will be able to obtain insurance at all and for some high risk individuals the costs could be too great to take out cover. Thus some form a safety net or cross subsidy will be needed to ensure that no one falls through the net.

17. COMMISSION

17.1 Commission Disclosure

Currently a major issue in the creditor insurance market (and other general insurance markets) is that of commission disclosure. The merits of this debate are considered in this section.

The payment of commission sometimes generates an implication that the person receiving the commission is gaining some unfair reward. Commission payments are a method of ensuring the seller has sufficient margin to cover the costs of promoting the product and to receive payment for the time and effort spent in obtaining the sale. Commission is the ultimate payment by results system, and all sales efforts are ultimately rewarded by payment by results.

In all products, not just financial services, there is always an element of commission, often called a retailers mark up. The lending companies who make the creditor insurance product available to their customers should be considered financial retailers, selling a range of products. Why then should these financial retailers have to disclose the level of their mark up when retailers in other market sectors (e.g. clothing, food, electrical goods, cars, restaurants, mortgage, personal loans) do not have to?

One of the concerns often quoted is that there should be a level playing field for all financial services, which means that general insurance should be treated the same as life insurance and investment products - and so commission should be disclosed. Alternatively a level playing field of no commission disclosure could extend to all market sectors, including financial services.

Would commission disclosure benefit the consumer? Does the consumer really care, especially with regard to general insurance products? General insurance products offer stated benefits for a stated price, the commission is included in that price. If the commission was reduced it would not necessarily mean that the customer would gain in either benefits, or a reduction in premium, as there would still be distribution costs to meet.

Commission disclosure on general insurance products is not as relevant as on the majority of life or investment products. The purchase of general insurances is a transparent transaction, customers receive stated cover for a stated price. The purchase of some life and investment products however is not as straight forward. The investment nature of these products means that any amount of money diverted away from the premium the customer pays results in less being invested for the customer’s benefit.

17.2 Commission Level

The level of commission that is paid is one criticism that is sometimes singled out for attention on some creditor insurance products. There are isolated cases where the level of commission, on some creditor insurance schemes, may be considered by some to be excessive. These levels of commission, however, are usually in the market sectors where there is an extended distribution chain, from insurer to eventual customer. Once again the argument is that commission payments are simply a margin for retailers to promote and sell the product at each stage of the distribution chain.

Typically the amount of advance commission taken by the lender is relative to the particular market sector and the distribution channel employed. Ultimately this is reflected in the price the customer pays. We have detailed earlier in this paper the take up rates in particular market sectors, increasingly customers are purchasing creditor insurance, not only as a single purchase but also as a repeat purchase and indeed multi purchase on a number of financial of their commitments; mortgages; loans and credit cards. This presumes the customer is generally happy with the benefits they are receiving in relation to the amount they are paying and that they do not consider that creditor insurers and other financial retailers to be part of the current ‘rip off Britain’ culture adopted by some other retail sectors.

18. THE GENERAL INSURANCE STANDARDS COUNCIL (GISC)

At the time of writing the GISC is due to take over the role, currently carried out by the Association of British Insurers (ABI), in the regulation of the selling of general insurance business. Two consultation documents have been issued so far. The second consultation document issued in October 1999 presented the mechanisms the GISC intends to use to regulate the General Insurance Industry from February 2000.

The consultation document describes the scope of the GISC as the regulation of:

- General Insurance
- the sales practices and advisory aspects of both insurers and intermediaries in the selling of General Insurance
- the financial requirements of intermediaries;
- the competence and training of the sales staff of its members;
- procedures for the handling of complaints from consumers and the availability of redress.

The document also states that in future the GISC will consider regulating other aspects of general insurance.

The issues arising from the document that are of particular relevance to creditor insurers and lenders are discussed below.

18.1 Membership

It is the intention of the GISC that all insurers selling general insurance direct to the public and all intermediaries selling General Insurance will become members of the GISC. The board regards an intermediary as any entity other than an insurer, selling or advising on General Insurance in circumstances where either

- it regards itself as fully responsible for services to its customers; or
- it has agency agreements with more than one insurer for any particular line of business.

Under the existing ABI code, lenders could deal with up to six insurers without having to be independent intermediaries. Some lenders used just one insurer for all their general insurance products, others used different insurers for each product line, and in particular the creditor insurer was often a specialist. These new proposals mean that virtually all lenders will now have to become members of the GISC.

A potential problem area is that companies that become members of the GISC will be banned from trading with companies that are not members. Presently the GISC is being threatened with legal action on the grounds that this is a restrictive trade practice, as a company will have to be a member of the GISC if it wants other members to deal with it

The GISC has set itself the ambitious target of February 2000 for the first members to be admitted. As it is problematic to admit 30,000 members in one go a phased timetable finishing in October 2001 will be used for a staged entry of members. It is questionable whether this timetable is achievable as comments can still be made on the second consultation document until 31st December 1999. This leaves only a month for the GISC to review and act on comments received as part of the consultation process before they intend to start admitting members.

18.2 Financial Requirements

The financial requirements include a proposal for the segregation of insurance money. Intermediaries will not be allowed to mix insurance money with their own money and will be required to maintain designated bank accounts for insurance premiums not accessible to their general creditors in the event of their insolvency. There are practical problems with this requirement because insurance money is often collected by a lender using a single direct debit for both the insurance premium and the loan repayment.

18.3 Competence and Training

Training standards will be applied to the General Insurance sales and advisory process. A qualification similar to NVQ is envisaged. However, this will be very difficult to apply in a retail environment where insurance is not the main product. It is recognised that it is not practical to expect all staff at point of sale to have insurance qualifications, and the level of training will have to take account of the different levels of accountability and the complexities of different products in the general insurance industry.

18.4 Complaints Handling

Members of the GISC will be required to have internal procedure to deal with complaints and may also be required to join the new Financial Services Ombudsman scheme. However as the Financial Services Ombudsman will not be prepared to admit new members before the middle of 2002 and there are presently doubts about the funding of the scheme, an interim Ombudsman scheme may need to be created.

19. CONCLUSION

In June 1980 the National Consumer Council issued a report entitled Consumers & Credit. In the report they considered 'Payment Protection Insurance' in which they quoted research undertaken by the Birmingham Money Advice Centre which asked the question:

"Do you consider the benefits provided (by Payment Protection Insurance) worth paying extra ..." To which over 60% of the respondents thought that it (Payment Protection Insurance) was a good idea.

In June 1998 MINTEL published research in creditor insurance which identified again that well in excess of 60% of the people interviewed thought that the benefits provided were a good idea. This was wide ranging research across sexes, age boundaries and geographical areas.

In the two surveys quoted, however, creditor insurance was criticised because of the cost in relation to the perceived benefits. Additionally in many later articles creditor insurance has often been criticised for many of the exclusions, terms and conditions that are part of the policy. Undoubtedly when the industry was in its infancy the customer literature, point of sale training and information needed improving. All too often there was a low awareness amongst the lenders own field staff of the exact nature of the cover. Due to training programmes, undertaken by the creditor insurer, and increased sophistication of the provision of literature, there is now a higher level of product awareness and product knowledge amongst staff and customers.

Creditor insurance is a mass market insurance product, sold to the majority of people at a reasonable price. Without doubt the terms, conditions and exclusions can be relaxed but at a cost. The increased cost would need to be passed on to all customers taking the cover, which would mean the majority of customers being financially disadvantaged for the benefit of the few. Whilst it can be argued that this is the basis of insurance, it is generally thought that it is everyone's best interest that the majority benefit from the cover at an affordable price.

Surveys continue to demonstrate that the customer wants the benefits offered by this type of product. Sales of the product increase year on year as more customers buy the product. Once customers have had the security of the product they tend to re-purchase. Cancellation rates for the product average 10% per annum. This is not a true cancellation rate because customers are unhappy with the product, most of the cancellations are because mortgages and loans are redeemed.

Historically many of the early American pioneers of the product in the UK thought that the 'S' curve for creditor insurance was ten to fifteen years. Whilst the product life cycle for the early forms of creditor insurance may be ten to fifteen years, with each product and distribution enhancement an extension of the product life cycle is assured. Clearly there is a Government wish that individuals take more responsibility for all aspects of their own welfare, there is a danger is that insurers become myopic in their initiatives to product design and distribution efficiencies. The customer is becoming increasingly willing to buy creditor insurance.

What are the key drivers for success in the creditor industry? As always in a market driven economy it is the organisations that innovate and lead the way that typically reap the benefits of first to market. Those that develop systems; claims and administrative processes as well as enhancing the product and experimenting with distribution will succeed. In any service industry it is the organisations who invest in the people they employ, both in the back office and front of house, and ensure that these people remain motivated, committed and eager to please, that succeed. It is in short the organisations who are customer and client focused that will reap the benefits of this unique and special product offering.

GLOSSARY

Ceased Trading means where you have involuntarily ceased trading as a result of your business having insufficient assets to meet its debts and liabilities and ;

a. your accountant confirms that accounts to cessate the business have been prepared and submitted to the Inland Revenue; and

b. your bank confirms that your trading account has been frozen and no further funds will be advanced in respect of your business.

Contract Workers - In order to claim for unemployment contract workers must satisfy special conditions. If you were made unemployed from a fixed term contract, you will only be entitled to unemployment benefits if:

a. you were on a yearly contract which had been renewed at least once immediately prior to you being made unemployed; or

b. you were under contract with the same employer for a period of at least 24 consecutive months immediately prior to you being made unemployed.

If you were with the same employer for at least 6 months and your contract had been renewed at least twice the you will only be entitled to benefit for unemployment if your contract if your contract terminated early. Unemployment benefit will cease at the end of the contract term.

Deferred period - In order to claim for unemployment or disability benefit an insured customer must be off work as a result of disability or unemployment for a minimum period of time. This period may be referred to as the '*deferred period'* or alternatively as the *'excess period'* or *'waiting period'* (see also *initial exclusion period*).

Disabled means being unable to work at your normal occupation (or at any job which you are reasonably able to do, given your experience, education or training) because of an accident or sickness. If you are self-employed, you cannot be receiving any form of payment or be helping; managing or carrying on any part of the running of the business while you are disabled.

Elimination Benefits – These start accruing at the rate of one thirtieth of the monthly benefit for each subsequent day of disability or unemployment after completion of the *deferred period.* No benefit is paid for the *deferred period*.

Excess Period – see *deferred period* (see also *initial exclusion period*)

Initial Exclusion Period – This is the period at the beginning of the policy during which a customer cannot claim. This may also be referred to as the *qualifying period* (see also *deferred period*)

Involuntary Unemployment means

i) being entirely without gainful employment (which includes the assisting, managing and/or carrying on of any part of the day to day running of a business); and

ii) being available for and actively seeking work and being able to provide evidence of this; and

iii) having signed a Jobseeker's Agreement or any such agreement in succession and provided us with a copy of the same (unless exempt).

Monthly Benefits – One monthly benefit is paid immediately on completion of the *deferred period*. Subsequent benefits are paid for each complete month that disability or unemployment continues.

Qualifying Period – see *initial exclusion period* (see also *deferred period*)

Redundancy means the ending of your full-time employment because:

i) your employer is no longer carrying on the business for which you were employed in the place where you were employed, or in a suitable alternative site; or
ii) your employer needs less employees to carry on work of a particular kind in the place where you were employed, or in a suitable alternative site

Resolicitation - Customers who have not taken a creditor policy at the time the loan is arranged are contacted after the sale has been completed, usually within one month, and are offered the opportunity to purchase creditor cover. The product offered may be the same as the point of sale product or it might be a cheaper product with limited benefits.

Retention – This is the insurer's charge for doing business and it comprises an expense charge and a charge for cost of capital.

Retroactive Benefits - On completion of the *deferred period* an immediate benefit payment is made equal to one thirtieth of the monthly benefit for each day of the *deferred period*. Subsequent benefits accrue at the rate of one thirtieth of the monthly benefit for each subsequent day of disability or unemployment.

Rule of 78 – This is the basis on which interest is rebated on early termination of a finance agreement. Some finance companies may use rule of 78 +1 or rule of 78 + 2. The formula for a refund on the Rule of 78 is:

$$\frac{(n-t)(n-t+1)}{n(n+1)}$$

where n = original term in months
t = expired duration in months

The rule of 78+1 uses t+1 rather than t and the rule of 78 + 2 uses t+2 rather than t. This formula might also be used for calculating unearned premiums for life risks.

U Benefits - One monthly benefit is paid immediately on completion of the *deferred period*. Subsequent benefits accrue at the rate of one thirtieth of the monthly benefit for each subsequent day of disability or unemployment.

Waiting Period – see *deferred period* (see also *initial exclusion period*)

APPENDIX 1

THE STATE BENEFIT SYSTEM

Many people rely on the state for protection but few realise how limited state benefits are. Qualifying for state benefits is not so simple as it used to be, for example, if you have a partner that works or have £8,000 in savings you will not get any help with mortgage costs. The interaction of creditor benefits with the state benefits system is described below, along with the levels of various state benefits and the rules for qualifying for these benefits.

Interaction of creditor benefits and state benefits

Mortgage Payment Protection

Any payments under a mortgage creditor policy which are received and used to pay housing costs not being met by the Benefits Agency will be ignored. If the amount received exceeds the total of :

- The interest paid on a qualifying loan which is not met by the Benefits Agency;
- Capital repayments on a qualifying loan; and
- Any premiums paid on the policy in question and any buildings insurance policy;

Then the excess amount will be counted as income and could reduce the amount of benefit.

Other Payment Protection Policies

Payments under insurance policies taken out to insure against the risk of being unable to maintain hire purchase or similar payments or other loan payments, for example, for credit card debts, will be ignored. However, anything received above the amount used to make the payments and the premium of the policy will be counted as income and could reduce the amount of benefit.

Job Seekers Allowance (JSA)

Job seekers allowance was introduced on 7th October 1996 as a replacement for unemployment benefit and income support (for those required to look for work). It is a benefit for all people who are unemployed and who are looking for full-time work. There are two forms of JSA – *contribution-based* JSA, which depends primarily on the NI contribution history of the claimant and *income-based* JSA, which is means tested. A claimant can receive both at the same time but contribution-based JSA will only be paid for the first 26 weeks of any jobseeking period.

To qualify for JSA, a claimant must :

- Be unemployed or working for less than 16 hours a week. A partner must either be unemployed or working for less than 24 hours a week; and
- Be capable of work; and
- Satisfy the 'labour market conditions', which are :
  - Be available for work; and
  - Be actively seeking work; and
  - Have a current jobseeker's agreement with the Employment Service; and
- Be below pensionable age; and
- Not be younger than 19 and still at school or college on a non-advanced course; and
- Be in Great Britain.

In addition, to qualify for contributions-based JSA, a claimant must :

- Satisfy the contribution conditions. These look at the amount of NI contributions in the two complete tax years preceding the claim (the relevant contribution years). The first condition requires the claimant to have paid Class 1 NI contributions of at least 25 times the weekly lower earnings limit in at least one of the relevant contribution years. The second condition requires that in each of the relevant contribution years, the claimant has either paid or been credited with at least 50 times the weekly lower earnings limit.

- Not have earnings above a prescribed amount. The prescribed amount depends on the age-related amount of contribution-based JSA (A) and the earnings disregard (B) (this is the amount a person is allowed to earn without having his/her benefits reduced. For most people, it is £5 per week). The prescribed amount is equal to A plus B less £0.01. For this test, the earnings of partners are ignored. If a claimant earns more than £5 a week but less than the prescribed amount, his/her benefits will be reduced pound for pound for all earnings above the earnings disregard.

- Not be entitled to income support.

Income-based JSA is means-tested. The key difference for income-based JSA is that the earnings of partners and savings are taken into account when assessing eligibility.

State Disability Benefits/ Statutory Sick Pay

Incapacity Benefit (IB)

Incapacity benefit is not means-tested, and depends on the claimant meeting the following criteria :

- They are assessed or treated as being incapable of work. This is determined by way of the own occupation test (for the first 28 weeks of a claim) or the "all work" test (after 28 weeks).
- Are not entitled to Statutory Sick Pay (SSP); and either
- Has been paid or credited with enough NI contributions; or
- Qualify as a widow or widower.

IB is paid at three rates and depends on the length of time a claimant has been entitled to IB:-

- The lower rate of short-term IB is paid for the first 28 weeks of entitlement;
- The higher rate of short-term IB is paid after 28 weeks of entitlement.
- Long-term IB is paid after 52 weeks of entitlement.

For short-term IB, a person must not be more than 5 years above pension age, but for long-term IB, they must not be over pension age.

Waiting Days
A person will not be entitled to IB for the first three days in any period of incapacity. The waiting days are waived if the period of incapacity can be linked to a previous one; or the person was previously receiving Statutory Sick Pay (SSP) and the period of incapacity falls within 57 days after the entitlement to SSP ended.

Statutory Sick Pay (SSP)

SSP is paid to employees for up to 28 weeks of incapacity. SSP is administered and paid for by employers. To qualify, an employee must be aged between 16 and 65 and have normal earnings equal to or above the lower earnings limit. The incapacity must last for a period of 4 or more consecutive days. Two periods of incapacity will be linked of they are separated by 8 weeks or less.

Contract workers are also entitled to SSP, provided the contractor is employed for three months or more. SSP is only payable for the term of the contract, if this is less than the 28 week entitlement. However, if a contractor has been employed continuously for three months or more, then he/she is entitled to SSP even if the contract was originally a short-term one. To stop employers avoiding SSP by employing people on a series of short-term contracts, the rules say that if a person has been employed by the same employer on two or more short-term contracts separated by 8 weeks or less and the total period specified in those contracts when combined exceeds 13 weeks, then the person is entitled to SSP. As for IB, the SSP is not paid for the first 3 days in a period of entitlement. Again, these waiting days will be waivered for a linked claim.

Other benefits

Severe Disablement Allowance is paid to people incapable of work and who become so on or before their 20th birthday and who are considered to be 80% disabled or who were previously entitled to non-contributory invalidity pension. Entitlement is not affected by NI contributions, nor does the claimant need to have been employed. Therefore someone may qualify even if they don't qualify for SSP or IB. Any income or savings does not affect entitlement.

Industrial injuries benefit is paid if a person is disabled as a result of an accident at work or a disease caused by their job. The main benefit is disablement benefit and entitlement is not dependent on NI contribution history.

Income Support is a benefit for people on low income. However, is not paid to unemployed people available and actively seeking work as they are expected to claim JSA instead. Income support is means-tested and does not depend NI contributions. Sick and disabled persons will be eligible to receive it if they are incapable of work because of illness or disability and:

- Are receiving SSP; or
- Satisfy the own occupation or all work test for IB; or
- Are treated as incapable of work by an adjudication officer; or
- Are treated as capable of work because they are disqualified from receiving IB due to misconduct or failure to accept treatment.

Income support is claimed for a family and therefore, a person will not be eligible if their partner is receiving income-based JSA.

Mortgage Payment Scheme

If a person is eligible for income support or income-based JSA, they will also be eligible for help with their mortgage payments. The benefit is designed to cover mortgage interest payments only and so a claimant will still need to meet any capital repayment or associated insurance premiums.

Benefits do not start immediately an income support or income-based JSA claim starts. There is a waiting period, which depends on when the loan was taken out :

If the loan was taken out before 2 October 1995 then a claimant gets:

- Nothing for the first 8 weeks of the claim.
- 50% of the eligible mortgage interest for the next 18 weeks.
- 100% of the eligible mortgage interest after 26 weeks.

For loans taken out after 1 October 1995 :

- Nothing for the first 39 weeks of the claim.
- Full housing costs after 39 weeks.

Interest Rate

If the interest rate paid by the claimant is above 5%, then the standard rate of interest, as set by the DSS, will be used in calculating the amount, not the actual rate paid by the claimant. If the actual rate is greater than this standard rate, the claimants will have to meet the shortfall themselves. Where the actual rate of interest is below 5%, this will be used instead.

Loan Amount

The loan amount on which the benefit is based will not necessarily be the full amount of the mortgage, because there is a upper limit of £100,000. For mortgages above this amount, interest will be calculated on £100,000 only. If living costs are thought to be excessive, for example, because the home is too big for the family or the area is more expensive than other areas where there is suitable accommodation for the person's needs, then the amount may be restricted.

MPPI - BASELINE COVER SPECIFICATION

- Cover Purchased by Borrowers -

The Baseline Cover is the minimum cover that should be offered to borrowers to purchase. It is expected that lenders will offer products that are superior to the minimum but for each element (accident/sickness and unemployment) the dimensions set out below are the absolute minimum.

Element	Dimensions	Explanatory Notes (not for borrowers but to clarify issues with Government, PIA etc)
1. Risks that are covered option, provided	The benefit is paid if the person insured is unable to work due to: • accident or	All lenders will offer, at least, the standard cover insuring against accident, sickness and unemployment. Some lenders may choose to offer, as an unemployment cover on its own or accident/sickness cover on its own,
2. Eligibility to upper apply Man will or	• sickness or • unemployment (which is involuntary) The applicant must: a) be aged between 18 and 64 (unless otherwise stated); b) live in the United Kingdom, the Channel Islands or the Isle of Man; c) be working in the United Kingdom, the Channel Islands or the Isle of Man; d) either be applying for a residential mortgage or have a residential mortgage that is not in arrears;	the borrower states that the option selected meets their particular needs. If a lender offers a product with a longer benefit period than 12 months, the age qualification can be reduced accordingly. When a borrower commences working in the UK, Channel Islands or Isle of and subsequently the job location moves outside these territories, the cover remain valid provided: • if claim validation is carried out: - by a doctor resident in the UK, Channel Islands or Isle of Man for an accident and sickness claim - by an appropriate employment office situated in the UK, Channel Islands Isle of Man for an unemployment claim; or
company	e) be in paid full time employment (including self employment and contract work) and f) have been continuously employed for at least the previous six months at the date of application.	• the insured person is working for the British Armed Forces or as a civil servant in a British embassy or consulate; or • the insured person is working for an employer that is a UK registered who assigns the insured person to work within the European Union. Continuous employment can be with more than one employer. Full time employment is officially defined as 16 hours per week.
3. Initial qualifying period (for people unemployment only)	• 60 days from the date of completion on a residential property (for cover arranged at the same time as the mortgage) • 120 days from the date of application for	This is the period of time at the start of the policy during which a claim for unemployment will be declined. It is included to eliminate claims from who are aware of impending unemployment. Throughout this period cover against accident and sickness remains. It is expected that some lenders will be
4. Excess period any (for each claim)	cover (for cover arranged after the mortgage) 60 days	able to commence the initial qualifying period from the date of exchange of contracts. The excess period is the number of days at the beginning of a claim before benefit will be paid. As in the excess on a motor insurance policy it is the
part of helps borrowers		the claim amount that is the responsibility of the claimant. Its inclusion reduce the cost of cover. When a claim is received during this period, will be requested to send in a claim form once the excess period has expired.
5. Benefit payment period. basis will	Daily benefit, payable monthly in arrears	The benefit will be paid at the end of each month, following the excess For part months (which can occur at the beginning or end of a claim), benefit be calculated as 1/30th of the monthly benefit for each day of the claim.
The		combination of the 60 day excess period and the daily benefit paid in arrears means that the first full monthly benefit will be paid on day 91 of the claim.

6. Benefit period for months benefit 7. Insured person specific	12 months for any one claim, subject to the length of individual claims Any named mortgage applicant or existing borrower	This is the maximum benefit that a claimant can receive for any one claim, following the excess period. Not all claims will actually last for 12 months, example a borrower who has had an accident might return to work after 6 because he/she has recovered. It will be open to lenders to offer a longer period than 12 months if they wish The insured person will normally be the first named applicant or main earner. However, benefit can be shared between joint borrowers to reflect their
the 8. Linked claims 9. Requalification period following receipt of the of the maximum benefit	Insurers will follow the linked claim rules set out in the ABI guidelines (as summarised in the explanatory notes). Monthly benefit ceases once 12 months' benefit has been paid. For unemployment claims and disability claims where the same disability has recurred: once the maximum benefit has been paid, the borrower will	requirements. Lenders will be able to offer increased cover (up to 100% of mortgage payment) for each joint borrower, provided each borrower pays the appropriate premium. Two claim periods separated by three months or less will be treated as one continuous claim. Where a claim changes from, say, a sickness claim to an unemployment claim, a second excess period will not be applied. The requalification condition is necessary to prevent claims continuing for longer than the maximum benefit period. In effect, it restates the 6 month continuous employment condition at commencement of cover.
10. Monthly payment benefit ensure often levels.	qualify for subsequent claims following a period of 6 months' active employment. For disability claims where a different disability occurs: once the maximum benefit has been paid, the borrower will qualify for subsequent claims following a period of one month's active employment. Not less than the full monthly commitment to the lender at the start of the mortgage	The monthly benefit will be adequate to cover the monthly mortgage at the start of the mortgage. While it is the borrower's responsibility to that the monthly benefit is adequate for their needs, as mortgages are arranged on fixed, capped or discounted interest rates, insurers and lenders will take all reasonable steps to remind borrowers to ensure adequacy of cover
mally during 11. Minimum periods of a notice for the changes to to	The minimum period between consecutive changes is 180 days. Notice given to borrowers for:	The insurance is designed to cover primarily the mortgage payment (nor- interest only or capital and interest). It can also cover: • the mortgage repayment vehicle (endowment, PEP etc., but not pension) • buildings/contents insurance at the borrower's option. The monthly benefit will cover the MPPI premium (if not already waived the claim period). The purpose of minimum notice periods is to protect the borrower against detrimental changes with little warning. However the insurer's right to charge premium that reflects the true risk, which can sometimes change rapidly as economy changes, must be preserved. The periods of notice are those given
the insurance not contract or close to when the change actually	Cover changes: 30 days Premium rate changes: 30 days IPT changes: Defined by law Withdrawal/cancellation:	borrowers and any associated contracts between the insurer and lender must compromise them. Single premium contracts can normally not be amended cancelled. It was also felt that the notification date should be reasonably 90 days (if no the effective date so that it is still relevant to borrowers
	substitute scheme is offered) 30 days (if Substitute scheme is offered)	occurs.

	Individual cancellation (e.g. due to fraud): Immediate	
12.Claims secure eligibility **contract workers:** a) regularly same renewable: ended	Covered if: • on a yearly contract which has been renewed at least once, or • under contract with the same employer for a period of at least 24 months.	The purpose of this condition is to demonstrate an applicant's ability to employment. In effect, once a contract worker has been continuously employed with the employer for two years, he/she becomes entitled to equal standing as open-contract employees.
b) individually negotiated:	Covered if at least 6 months with the same employer and the contract has been renewed at lease twice. • unemployment benefit paid only if contract terminated early • unemployment benefit ceases at the end of the contract term	
13.Claims qualify eligibility **self employed:**	The self employed will be covered if: • they have involuntarily ceased trading and declared this to the Inland Revenue and • they have registered for Job Seekers allowance at the appropriate office in the United Kingdom (or equivalent in Channel Islands or Isle of Man)	The self employed can register for Job Seekers allowance. They may not for benefit but they will receive a National Insurance credit.
14.Temporary policy earnings during a claim period not	Will be allowed, in effect suspending claim payment for the period of temporary work.	This approach has been offered by most insurers. It will be included in the wording, rather than allowing it to be discretionary. Temporary work taken immediately after unemployment, but before a claim has commenced, will adversely affect the claim.
15.Exclusions normal	For accident, sickness and unemployment: • any pre-existing medical conditions for which treatment had been given or diagnosis had been made or investigations had commenced during the 12 month period before cover commences • pre-existing chronic or continuing disease • self-inflicted injuries • alcohol abuse • drug abuse • war, invasion etc. • radioactive contamination • pregnancy For unemployment: • casual or temporary work • when unemployment is a seasonal occurrence • known or impending unemployment • voluntary unemployment • unemployment caused by misconduct • a period of unemployment for which pay in lieu of notice has been received	For claims relating to certain conditions, including: • aids • pregnancy complications • backache • stress and mental disorders additional specialist medical evidence will be sought to validate the claim. Pregnancy complications does not include conditions that are considered in pregnancy such as morning sickness and post natal depression. Cessation of temporary employment which commences during a claim (as described under section 15) is not excluded.
16.Medical evidence	Normally the doctor's report is sufficient. The borrower pays for this at the commencement of the claim. If further specialist medical evidence is required by the insurer, the cost is met by the insurer in line with the standard fee structure as set out by the BMA	Borrowers are required to complete continuation claim forms if the duration exceeds several months. The borrower pays for further medical evidence if charged by the doctor. Some insurers will take copies of Form MED3 as evidence.

APPENDIX 3

CREDIT CARD INSURANCE

COMPETITOR ANALYSIS

Note:

Information collated purely on standard cards

Cost is based on Oustanding Balance

L	=	Life
AS	=	Accident and Sickness
U	=	Unemployment
H	=	Hospitalisation
CI	=	Critical Illness
ADB	=	Accidental Death Benefit

November 1999

CARD PROVIDER (ISSUER WHERE APPROPRIATE)	PPI INSURER	COVER	QUALIFYING PERIOD	COST	BENEFIT	PURCHASE PROTECTION	TRAVEL ACCIDENT	CARD PROTECTION
Abbey National	CGU	L U AS	- 15R 15R	71p per £100	O/Balance 10% of O/B - Max 12 months 10% of O/B - Max 12 months	Cover within 90 days of purchase £50 franchise Max £3,500 Agg	Not Provided	£10 - 1 year single £16 - 1 year joint £25 - 3 years single £39 - 3 years joint
Alliance & Leicester	Sterling	L U AS	- 30M 30M	74p per £100 69p per £100 if taken within 8 weeks of opening account	O/S Balance 3% of O/B - Max 12 months 3% of O/B - Max 12 months	Cover within 100 days of purchase £50 franchise	Provided up to £100,000	£12 - 1 year single £18 - 1 year joint £29 - 3 years single £44 - 3 years joint
American Express	London & Edinburgh	L U AS	- 30M 30M	66p per £100	O/Balance (Doubled if death result of accident) 5% of O/B - Max 24 months 5% of O/B - Max 24 months	Cover within 90 days of purchase Max £20,000	Not Provided	-
Barclaycard	Captive	L U AS	- 30M 30M	70p per £100	O/Balance 10% of O/B - Max 12 months 10% of O/B 0 Max 12 months	Cover within 100 days of purchase £50 franchise Max £1500 per claim and £5000 in 12 months	Provided Up to £50,000	£10 - 1 year single
Bradford & Bingley (MBNA)	London & Edinburgh	L U AS	- 30M 30M	68p per £100	O/Balance 3% of O/B - Max 12 months 3% of O/B - Max 12 months	Provided £1000 per purchase	Provided Up to £100,000	-

CARD PROVIDER (ISSUER WHERE APPROPRIATE)	PPI INSURER	COVER	QUALIFYING PERIOD	COST	BENEFIT	PURCHASE PROTECTION	TRAVEL ACCIDENT	CARD PROTECTION
Capital One	London General Holdings	L U AS	- 30M 30M	69p per £100	O/Balance 10% of O/B - Max 12 months 10% of O/B - Max 12 months	Not Provided	Not Provided	-
EGG	Guardian	L U AS	- 30E 30E	59p per £100	O/Balance 10% of O/B - Max 12 months 10% of O/B - Max 12 months	Cover within 30 days of purchase £25 excess Max £1000	-	£10 per year
Goldfish	Hamilton	L U AS	30M 30M	74p per £100	O/Balance 10% of O/B - Max 12 months 10% of O/B - Max 12 months	Not provided	Not provided	
Halifax	GEFI	L U AS CI	-	76p per £100	O/Balance 10% of O/B - Max 12 months 10% of O/B - Max 12 months O/Balance	Cover within 100 days of purchase £50 franchise Max £15,000	Provided Up to £50,000	£12 - 1 year £30 - 3 year
HSBC	CGU (Life by Captive)	L U AS	- 15M 15M	73p per £100	O/Balance 10% of /B - Max 12 months 10% of /B - Max 12 months	Not provided	Provided up to £50,000	£10 - 1 year single £16 - 1 year joint

CARD PROVIDER (ISSUER WHERE APPROPRIATE)	PPI INSURER	COVER	QUALIFYING PERIOD	COST	BENEFIT	PURCHASE PROTECTION	TRAVEL ACCIDENT	CARD PROTECTION
Lloyds TSB	London & Edinburgh	L U AS	- 15M 15M	75p per £100	O/Balance 5% of O/B 5% of O/B	Not provided	Not provided	£10 per year
Marbles (HFC)	Hamilton	L U AS	- 30M 30M	74p per £100	O/Balance 10% of O/B - Max 12 months 10% of O/B - Max 12 months	Not provided	Not provided	£12 - 1 year £30 - 3 years
MBNA	London & Edinburgh	L U AS	- 30R 30R	68p per £100	O/Balance 10% of O/B 10% of O/B	Provided	Provided up to £10,000	-
Morgan Stanley Dean Witter	Norwich Union	L U AS	- 30R 30R	68p per £100	O/Balance 3% of O/B - Max 12 months 3% of O/B - Max 12 months	Not provided	Provided up to £100,000	£10 - 1 year single £16 - 1 year joint £25 - 3 years single £39 - 3 years joint
Nationwide	Pinnacle	L U AS	14M 14M	60p per £100	O/Balance 10% of O/B - Max 12 months 10% of O/B - Max 12 months	Provided Cover within 100 days of purchase £50 franchise	Provided up to £50,000	£10 - 1 year single £16 - 1 year joint £25 - 3 years single £39 - 3 years joint

CARD PROVIDER (ISSUER WHERE APPROPRIATE)	PPI INSURER	COVER	QUALIFYING PERIOD	COST	BENEFIT	PURCHASE PROTECTION	TRAVEL ACCIDENT	CARD PROTECTION
NatWest	RSA	L U AS	- 30M 14M	76p per £100	O/Balance 10% of O/B - Max 12 months 10% of O/B - Max 12 months	Cover within 90 days of purchase £50 excess Max £3000 per claim Max £15,000 per year	Provided	£10 - 1 year single £16 - 1 year joint £25 - 3 years single £39 - 3 years joint
Peoples Bank	Cornhill	L U AS	- 30M 30M	69p per £100	£5000 10% of O/B - Max 12 months 10% of O/B - Max 12 months	Cover within 90 days of purchase	Provided up to £100,000	£10 - 1 year single £16 - 1 year joint £25 - 3 years single £39 - 3 years joint
Royal Bank of Scotland	GEFI	L U AS	- 30M 30M	72p per £100	£5000 10% of O/B - Max 12 months 10% of O/B - Max 12 months	Not provided	Provided up to £50,000	£10 - 1 year £25 - 3 year
Shell (R B of S)	GEFI	L U AS	- 30M 14M	74p per £100	£6000 10% of O/B - Max 12 months 10% of O/B - Max 12 months	Not provided	Not provided	£10 - 1 year £25 - 3 year
Woolwich	London & Edinburgh	L U AS	- 14R 14R	70p per £100	£10,000 10% of O/B - Max 12 months 10% of O/B - Max 12 months	Cover within 100 days of purchase £25 franchise Max £500 per item Max £2500 per year	Not Provided	£10 - 1 year single £16 - 1 year joint £25 - 3 years single £39 - 3 years joint

CARD PROVIDER (ISSUER WHERE APPROPRIATE)	PPI INSURER	COVER	QUALIFYING PERIOD	COST	BENEFIT	PURCHASE PROTECTION	TRAVEL ACCIDENT	CARD PROTECTION
Yorkshire Bank	London & Edinburgh (Life Captive)	L U AS	- 14M 14M	68p per £100	£7500 10% of O/B - Max 12 months 10% of O/B - Max 12 months	Not provided	Provided up to £50,000	£10 - 1 year single £16 - 1 year joint £25 - 3 years single £39 - 3 years joint

PERSONAL LOAN

COMPETITOR ANALYSIS

Key:

Cost is based on Total Amount Repayable (TAR) unless stated otherwise

L	=	Life
AS	=	Accident and Sickness
U	=	Unemployment
H	=	Hospitalisation
CI	=	Critical Illness
ADB	=	Accidental Death Benefit

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LENDER	INSURER	COVER	INITIAL EXCLUSION	QUALIFYING PERIOD	BENEFIT	COST	APR	NOTES
Abbey National	CGU	L U AS	- 30 days -	- 30E 30E	O/B less arrears 12 months term of loans	12M - 6.43% 24M - 8.76% 36M - 9.33% 48M - 10.13% 60M - 10.99%	£1000 - £2950 - 16.9% £3000 - £4950 - 14.4% £5000 - £7450 - 12.9% £7500 - £9950 - 12.7% £10000 - £12450 - 11.9% £12500 - £15000 - 10.9%	
Alliance & Leicester	G E Financial Insurance	L U AS	- 30 Days -	- 14M 30M	O/B less arrears 36 months term of loan	12M - 6.10% 24M - 8.20% 36M - 8.95% 48M - 11.20% 60M - 11.90%	£500 - £2499 - 18.5% £2500 - £4999 - 12.9% £5000 - £9999 - 11.9% £10000 - £15000 - 10.9%	APR 9.9% with loan protection
Barclays	Captive	L U A/S H CI	- 30 Days - - -	- 14R 14R 1R -	O/B less arrears max 12 month Term of loan Term of loan o/b less arrears	12M - 7.65% 24M - 9.30% 36M - 11.25% 48M - 12.25% 60M - 13.20%	£500 - £3900 - 19.9% £4000 - £6900 - 17.9% £7000 - £11900 - 15.9% £12000 - £15000 - 13.9%	
Bradford & Bingley	Pinnacle	L U AS	- 30 days -	- 30M 30M	O/B less arrears max 12 months agg 35 months term of loan	24M - 10% 36M - 13% 48M - 15% 60M - 17%	£1000 - £2999 - 19.9% £3000 - £6999 - 16.9% £7000 - £9999 - 13.9% £10000 - £15000 - 12.9%	Premium charged % of principal loan amount

LENDER	INSURER	COVER	INITIAL EXCLUSION	QUALIFYING PERIOD	BENEFIT	COST	APR	NOTES
Colonial	G E Financial Insurance	L U AS	- 60 days -	- 30E 30E	O/B less arrears 12 months 60 months	24M 10.5% 36M 12.5% 48M 14.0% 60M 14.5%	with insurance without insurance - £2,000 16.5% 18.5% £2,000-£3,999 15.5% 17.5% £4,000-£4,999 14.5% 16.5% £5,000-£7999 13.5% 15.5% £8,000-£14,999 11.5% 13.5% £15,000 9.5% 11.5%	
Halifax	GE Financial Insurance	L IU AS	- 60 days -	- 30E 30E	O/B less arrears 12 months 60 months	12M - 6.81% 24M - 8.70% 36M - 10.00% 48M - 10.85% 60M - 12.43%	With Insurance Without Insurance £500 - £3000 18.9% 20.9% £5000 - £7000 15.9% 17.9% £10000 - £15000 13.9% 15.9%	Discount up to 5% of APR to customers who have other Halifax products
Hamilton Direct	Hamilton	L U AS	- 30 days -	- 30R 30R	O/B less arrears 12 months 12 months	all terms 14% of principal loan amount	£500 - £2,999 16.4% £3,000 - £4,999 14.5% £5,000 - £9,999 12.5% £10,000 - £12,499 10.8% £12,500 - £15,000 9.9%	
HSBC	CGU & Midland Life	L U AS	- 60 days -	- 15E 15E	O/B less arrears 12 months term of loan	12M - 7.00% 24M - 8.70% 36M - 9.35% 48M - 10.25% 60M - 11.75%	£500 - £2990 - 16.9% £3000 - £4990 - 14.9% £5000 - £6990 - 13.9% £7000 - £11990 - 11.9% £12000 - £15000 - 10.9%	
Lloyds TSB	Lloyds TSB, M & G Life & GE Financial Insurance	L (includes Cancer Cover) U AS H - Over 65 years	- 30 days - -	15R 15R - 5E	O/B less arrears 12 months term of loan 12 months	12M - 8.57% 24M - 9.55% 36M - 10.00% 48M - 11.57% 60M - 13.35%	£500 - £1400 - 21.9% £1500 - £2900 - 18.8% £3000 - £4900 - 16.9% £5000 - £9900 - 14.9% £10000 & over - 13.8%	

LENDER	INSURER	COVER	INITIAL EXCLUSION	QUALIFYING PERIOD	BENEFIT	COST	APR	NOTES
Marks & Spencer	Cornhill	L U AS	- - -	- 29M 14M	O/B less arrears 12 months term of loan	12M - 6.44% 24M - 8.34% 36M - 10.1% 48M - 10.35% 60M - 11.2%	with Insurance / without Insurance £500 - £999 17.9% 18.9% £1000 - £2999 15.9% 16.9% £3000 - £4999 14.4% 15.4% £5000 - £9999 12.9% 13.9% £10000 11.9% 12.9%	
MBNA	CGU	L U AS	- 60 days -	- 15R 15R	O/B less arrears 12 months term of loan	12M - 6.34% 24M - 7.57% 36M - 8.90% 48M - 10.37% 60M - 11.71%	-£2,000 17.9% £2,000 - £5,000 14.9% £5,001 - £10,000 12.9% £10,001 - £15,000 11.9%	
Natwest	London & Edinburgh & Royal & Sun Alliance	L U AS	- 30 days -	- 14m 14m	O/B less arrears 12 months 60 months	12M - 8.40% 24M - 12.00% 36M - 14.40% 40M - 17.60% 60M - 21.10%	£1000 - £1500 15.9% £2000 - £3000 13.9% £4000 - £6000 11.9% £7000 - £9000 10.9% £10000 - £12000 8.9%	Premium charged % of principal loan amount
Nationwide	CGU	L U AS	- 60 days -	o/b less arrears 30E 30E	o/b less arrears Max 12 months Term of Loan	12M - 5.65% 24M - 7.16% 36M - 8.07% 48M - 9.32% 60M - 11.49%	£1000 - 16.7% £3000 - 12.7% £5000 - 11.7% £10000 - 10.7% £15000 - 9.7%	
Royal Bank of Scotland	Direct Line Insurance & Royal Scottish Assurance	L U AS	- 60 days -	- 30E 30E	o/b less arrears 12 months 12 months If PTD pay o/b less arrears	Quote as 60M - 13.40%	£4000 - 16.4% £7500 - 15.2% £10500 - 12.0% £20000 - 11.1%	Discount available up to 1.5% APR reduction

LENDER	INSURER	COVER	INITIAL EXCLUSION	QUALIFYING PERIOD	BENEFIT	COST	APR	NOTES
Sainsburys	St Andrews	L U AS CI	- - - -	- 30R 14R -	OB less arrears 12 months 12 months O/B less arrears	12M 5.2% 24M 9.5% 36M 12.8% 48M 15% 60M 17.1%	£1,000 - £2,999 16.5% £3,000 - £4,999 12.7% £5,000 - £7,499 11.9% £7,500 - £9,999 10.7 £10,000 - £15,000 9.9%	Additional £5,000 paid if death result of accident
Woolwich	London & Edinburgh	L U AS	- 90 days -	30E 30E	o/b less arrears 12 months Term of loan	12M - 7.49% 24M - 8.25% 36M - 8.61% 48M - 8.32% 60M - 8.99%	**Woolwich Cust** / **New Cust** £500 - £2999 17.0% 17.5% £3000 - £4999 17.4% 13.9% £5000 - £9999 12.4% 12.9% £10000 - £12499 10.4% 10.9% £12500 - £15000 9.9% 10.4%	
Yorkshire Bank	London & Edinburgh National Australia Life Co.	L U AS	- - -	- 30M 30M	o/b less arrears 18 months Term of Loan	24M - 9.85% 36M - 10.72% 48M - 11.60% 60M - 12.15%	£1000 - 19.3% £2000 - 18.0% £3000 - 16.3% £5000 - 14.5% £7500 - 13.7% £10000 - 12.7%	

MORTGAGE PAYMENT PROTECTION

COMPETITOR ANALYSIS

KEY

30E - means 30 days excess with benefit due daily from day 31

30M - means 30 days waiting period with benefit due monthly but paid back to the first day of the claim

30R - means 30 days waiting period with benefit payable daily and paid back to the first day of the claim

Cost is based on the Monthly Benefit selected by the customer

L	=	Life
AS	=	Accident and Sickness
U	=	Unemployment
H	=	Hospitalisation
CI	=	Critical Illness
ADB	=	Accidental Death Benefit

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LENDER	SCHEME NAME	INSURER	COVER	INITIAL EXCLUSION UNEMPLOYMENT	QUALIFYING PERIOD	COST INC. IPT	BENEFIT	AVAILABILITY to Non Borrowers/ Existing Borrowers	ADDITIONAL NOTES
Abbey National	Payment Care	Commercial Union Underwriting	ASU AS U	60 days If arranged within 30 days of completion for new mortgage - no exclusion	28E for all options	6.04% 3.26% 4.31%	12 months	Both	
Alliance & Leicester	Mortgage Payment Cover	Pinnacle	ASU	60 days	30E	5.20%	12 months	Ex borrowers	
Barclays Bank	Mortgage Care	Captive	ASU U	60 days	30E	5.6% 4.6%	12 months		
Bradford & Bingley	Payment Protection	G E Financial Insurance Company	ASU	60 days 120 days if existing customer	30E	5.60%	12 months	Existing borrower	
Bristol & West	Incomesure	London & Edinburgh	ASU	60 days	60E	50p per £1000 of loan	12 months	Existing borrower	
Britannia	Payment Protection	Guardian	ASU	30 days	**30E 60E 90E** 7.14 6.00 5.08 8.66 7.26 6.06 9.20 7.68 6.30		12 months 18 months 24 months	Both	
			AS	-	3.57 3.00 2.54 4.33 3.63 3.03 4.60 3.84 3.15		12 months 18 months 24 months		
			U	30 days	3.57 3.00 2.54 4.33 3.63 3.03 4.60 3.84 3.15		12 months 18 months 24 months		

LENDER	SCHEME NAME	INSURER	COVER	INITIAL EXCLUSION UNEMPLOYMENT	QUALIFYING PERIOD	COST INC. IPT	BENEFIT	AVAILABILITY to Non Borrowers/ Existing Borrowers	ADDITIONAL NOTES
Cambridge	Mortgage Payment Protection Plan	Cassidy Davis, SCOR UK & Zurich Insurance Co.	ASU	60 days	60E	5.72%	12 months		
Chelsea	Payment Protection	Guardian	ASU plus H	60 days 90 days if existing borrower	30E 7E	4.50%	12 months	Both	Hospitalisation Cover 1/20th paid from day 7 to day 30
Cheltenham & Gloucester	Payment Protection Plus	Lloyds TSB	ASU	60 days 90 days if existing borrower	60E	50p per £1,000 of loan	12 months	Existing borrower	
	Mortgage Payment Protection	Pinnacle	ASU	60 Days 90 days if existing borrower	60E	5.25%	12 months	Existing borrower	
Clydesdale Bank	Mortgage Protection	London & Edinburgh	ASU	60 days	60E	5.98%	12 months	Both	
Coventry	AS U Cover A & S Cover U only cover	CGU	ASU AS U	60 days – 60 days	30E	5.20% 3.10% 3.10%	12 months	Existing borrower	
Derbyshire	Mortgage Payment Protection	Norwich Union	ASU AS U	60 days — 60 days	30M/60M	5.25%/4.62% 2.99%/2.63% 2.99%/2.63%	12 months	Existing borrower	
Future Mortgages	Future Guard	Pinnacle	ASU	60 days	30R	6.5%	12 months		
Halifax	Mortgage Repayments Insurance	G E Financial Insurance Company	ASU	None	30R	5.30%	24 months		Payment holiday available. No exclusions on policy at all

LENDER	SCHEME NAME	INSURER	COVER	INITIAL EXCLUSION UNEMPLOYMENT	QUALIFYING PERIOD	COST INC. IPT	BENEFIT	AVAILABILITY to Non Borrowers/ Existing Borrowers	ADDITIONAL NOTES
Economic	Mortgage Care	Pinnacle	ASU	60 days	60E	5.5%	12 months	Both	
HSBC	Mortgage Repayment Protector	Royal & Sun Alliance	ASU	60 days	30E	5.88%	12 months	Existing borrower	
Lambeth	Mortgage Cover	Norwich Union	ASU	60 days	60E	6.10%	12 months		
Leeds & Holbeck	Mortgage Payment Protection	Norwich Union	ASU + H AS + H U + H	60 days -- 60 days	30E + 5E	5.50% 2.50% 4.00%	2 months	Both	Hospitalisation Cover £20 per day from day 6 up to day 30
Leek United	Mortgage Care	Pinnacle	ASU AS U	60 days 120 days if existing borrower	30E	5.98 2.74 4.06	12 months	Both	Only ASU available to existing borrowers
Mansfield	Mortgage Care	Pinnacle	ASU	60 days	30E	5.95%	12 months		
Nationwide	Payment Guard	CGU	ASU AS U ASU AS U	60 days - 60 days 60 days - 60 days	30E 30E 30E 60E 60E 60E	4.99% 2.58% 3.39% 5.99% 3.31% 4.20%	12 months 12 months 12 months 24 months 24 months 24 months	Existing borrower	
NatWest	Mortgage Repayments Protector	Royal Sun Alliance	ASU + ADB	60 days	30R	5.12%	12 months	Both	Accidental Dealth Cover of £30,000 provided
Newcastle	Payment Protection Plus	Pinnacle	ASU AS U	60 days -- 60 days	30E	5.90% 5.25% 2.25%	12 months	Both	5% added to benefit if 3 years with no claims to a maximum of 15%

LENDER	SCHEME NAME	INSURER	COVER	INITIAL EXCLUSION UNEMPLOYMENT	QUALIFYING PERIOD	COST INC. IPT	BENEFIT	AVAILABILITY to Non Borrowers/ Existing Borrowers	ADDITIONAL NOTES
Northern Rock	Paysafe Payment Protection Insurance	CGU	ASU +CI AS + CI U	60 days	60E	5.90% 3.90% 3.90%	12 months	Both	Critical Illness cover of 1 year's benefit provided
Norwich & Peterborough	Safeguard	Norwich Union	ASU	60 days 90 days if existing borrower	30E	6.09%	AS-24 months U-12 months		
Nottingham	Mortgage Payment Protection	London & Edinburgh	ASU	60 days	60E	5.57%	12 months		
Portman	Mortgage Care	CGU	ASU AS U	not specified		5.50% 2.98% 3.94%	12 months		
The Principality	Mortgage Payment Protection Plan	CGU	ASU	60 days	60E	4.76%	12 months	Both	
Mortgage Services	Mortgage Care	Pinnacle	ASU	60 days	60E	6.00%	12 months		
Royal Bank of Scotland	Mortgage Loanguard	Direct Line	ASU U	30 days 90 days if existing borrower	60E	5.45% 3.45%	12 months	Both	
Scottish Widows	Mortgage Payment Protection	Pinnacle	ASU	60 days	30E or 30M	5.60% 6.80%	12 months		
Skipton	Mortgage Payment Protection	London & Edinburgh	ASU U	None	56E	4.94% 3.15%	12 months	Both	ASU free for 6 months if continue house & contents insurance for 12 months

LENDER	SCHEME NAME	INSURER	COVER	INITIAL EXCLUSION UNEMPLOYMENT	QUALIFYING PERIOD	COST INC. IPT	BENEFIT	AVAILABILITY to Non Borrowers/ Existing Borrowers	ADDITIONAL NOTES
Staffordshire	Mortgage Payment Protection	CGU	ASU	60 days	30E or 60E	6.88% 4.20%	18 months 12 months		First 6 months free
Tipton & Coseley	Mortgage Care	Pinnacle	ASU	60 days	30E	4.95%	12 months	Both	Free cover from start of mortgage to 31st December
Universal Building Society	Mortgage Care	Pinnacle	ASU	60 days 90 days if existing customer	30E	6.34%	12 months	Both	
Woolwich	Payment Protection Plan	London & Edinburgh	ASU Plus H	60 days 120 days if existing customer	60E	5.75%	12 months	Both	£50 per day Hospitalisation Cover provided
Yorkshire Building Society	Mortgage Payment Insurance	CGU	ASU AS U	60 days 60 days	60E/30E	4.13%/4.83% 2.17%/2.66% 2.17%/2.66%	12 months		