



# LIFE INSURANCE UNDERWRITING

Underwriting a life insurance policy is similar to making any major investment - a lot of time and research goes into the decision making process. The insurance company reviews all applications for life insurance carefully to decide which ones they want to accept and how much to charge each insured. Simply put, it is a process of risk assessment, selection, and classification.

## RISK ASSESSMENT AND SELECTION

The main risk a carrier faces is that of an early death claim (when an insured passes sooner than expected). Life insurance carriers invest premiums from life insurance policies and early death payments remove money from the investment pool, lowering returns. It is this mortality risk that an insurance carrier seeks to control through the underwriting process. The higher the risk of an early payout, the higher the premium charged for coverage. Consequently, if the risk of a payout appears immediate or if an estimate cannot be made due to a preponderance of risk factors, the life insurance carrier will likely choose to not make an offer of insurance.

The risk factors that carriers concern themselves with in their underwriting assessment can be broken down generally as medical and non-medical. Medical risk factors include both your current and past health history. Non-medical risk factors include avocations, occupations, tobacco use, and travel.

Underwriting begins with a formal application for life insurance and the completion of routine requirements. The routine requirements depend on your age and the amount of life insurance desired and can include labs, a physical exam, medical and driving records and/or financial information.

As you go through the underwriting process, should other information arise that is of concern to the life insurance company, you may be asked to complete additional requirements. For example, if it is discovered in the medical records that you are an avid skydiver, the insurance carrier may ask you to complete an avocation questionnaire. Once all requirements are reviewed, if the insurance carrier considers an offer for insurance, you will be placed in a particular risk class and asked to pay a particular premium for the coverage.

## RISK CLASSIFICATION

Risk classification is designed so applicants pay their fair share of premium. Higher risks pay higher premiums; lower risks pay lower premiums. Each class is made up of insureds with similar expected mortality. For example:

- Preferred class - better than average expected mortality
- Standard class - average expected mortality
- Sub-Standard class - worse than average expected mortality

Insureds who appear to represent too great a risk are not accepted and their applications are either declined or postponed for reconsideration at a later date. Mortality and probability statistics help make all of this moderately predictable for insurance companies.

Finally, it is important to remember that because the financial health of the insurance company can have an impact on how well individual policies perform - it is in everyone's best interest to patiently work through the underwriting process.

## CLINICAL VS. INSURANCE MEDICINE

Clinical medicine deals with the diagnosis and treatment of diseases and the maintenance of a patient's health. Insurance medicine deals with risk selection and classification based on an insurance company's underwriting manual.

Having "a clean bill of health" from a medical doctor does not necessarily mean you will get the lowest premium from an insurance company. The rate you receive depends on the specifics of your medical history and how the particular insurance company prices those specifics. For example, the medical doctor may feel a skin cancer from eight years ago is no longer something to be concerned about and will not shorten life expectancy. However, an insurance carrier may not give the lowest premium - they may offer a standard class premium. It is important to remember that standard to a life insurance company does equal an expectation of average life expectancy, just not better than average.