FACING THE BIGGER PICTURE WITH WHOLE-LIFE INSURANCE

The Three Dimensions of Hedging

By Patrick Lim

The recent standoff between the management at SIA and the pilots union ALPA-S reminded me of a similar situation in 1980 when Senior Minister Lee Kuan Yew, then prime minister, was quoted as saying, "I don't want to do you in, but I won't let anybody do Singapore in."

In other words, he was looking at the bigger picture, just like he is now: the advances in aviation technology that might render stopovers unnecessary; the threat posed by regional budget airlines; and competition from international airports in Malaysia and Thailand, and even in Dubai.

Personal risk management is also about three factors, namely premature death, disability and diseases, but unlike Singapore Airlines you can insure against future loss of income and the costs of treatment.

LIVING LONGER

A basic whole-life plan, for example, covers all these events. Most of us can expect to live to be octogenarians, and a whole-life plan comes with a lifetime of coverage that usually extends until age 99 or 100 years, thus addressing longevity risks.

Term plans, on the other hand, mostly provide coverage up to age 70 or 75, and there are relatively few that extend beyond that. The exceptions are AXA Life's Living Term, which runs to 85, Aviva's Wealth Protector and Asia Life's Enhanced Crisis Assurance, which both run until age 99, and HSBC's Value Long Term Plus, which runs until age 90.

ACCUMULATING CASH VALUES

Whole-life plans also accumulate a cash value as your premiums build up over the years, whereas term plans simply offer protection until their expiry date. Most whole-life plans start to accumulate after the first or second policy years, and policy loans are available that let you borrow against the cash value of your policy. Your insurer will charge interest (the lowest rate is 5.5% a year from NTUC Income, while the highest at the moment is 8%) but this could still be a lifeline for cash-strapped policyholders looking for instant cash.

And because the cash value of investment-linked products (ILPs) fluctuates along with market conditions, policy loans are not available to all ILP policyholders. NTUC Income offers loans up to 70% of the cash value, but that's still lower than the stipulated minimum of 90% available to the whole-life policyholder.

LUMP-SUM PAYMENTS

Insurers will admit claims upon diagnosis of one of the 30 dreaded diseases included in the policy (there is an agreed list of 37 critical illnesses amongst Singapore's insurers, and an insurance plan can cover any 30) and pay out a lump sum up to a limit of S$650,000. Almost all insurers impose this maximum, but it still means a policyholder can receive the benefit while they are alive, helping them to seek the best medical treatment available.

Almost all catastrophic medical plans (CMPs) available only reimburse hospital expenses after the policyholder has paid the first bill, and these plans typically reimburse expenses dollar for dollar, once deductibles and co-insurance have been taken care of (in other words, when the portion of the bill that must be paid out of the insured's own pocket has been settled).

That could be a problem if the size of a substantial hospital bill reflects the severity of the medical condition and the prolonged period of hospitalisation. A payout of up to S$650,000 upon diagnosis, however, goes a long way towards alleviating any cash crunch with regard to deposits and upfront payments, making a whole-life plan in many ways an ideal complement to a CMP.

PARTICIPATION

A participating whole-life plan shares in the profits of the insurer, and insurers must distribute to participating policyholders a minimum of 90% of bonuses derived from surpluses in every policy year. Everything being equal, such bonus payouts are largely contingent on the insurer's assumption of the PIROR, or projected investment rate of return (this is stated in the benefit illustration), and the actual net rate of return from life funds.

Of course the higher the assumed PIROR, the greater the potential for projected non-guaranteed values to be lowered, something that has been evident from the rounds of bonus cuts that the life-insurance industry has experienced since the onset of the Asian crisis of 1997.

Most of the life insurers have chosen to use the highest assumed PIROR of 5.25% in their benefit illustrations, though AIA deserves mention for using three different PIRORs in their whole-life benefit illustrations, with the lowest at just 2.5%. The main benefit illustration shows a PIROR of 4%, and this is the lowest amongst life insurers in Singapore.

Two other supplementary benefit illustrations assume the much higher 5.25% and an even lower 2.5%, and in addition to these lower PIRORs, AIA has included an explanation that the terminal bonus (TB), which is a special non-guaranteed discretionary bonus payable upon surrender or death, may be reduced to nil under conditions of substantial decline in investment returns. That is an extremely realistic statement, and by using the 4% figure in their main benefit illustration AIA has set the right example.

WHICH WHOLE-LIFE PLAN?

Last year, life insurers inserted clauses into whole-life plans stating that premiums for critical illnesses would be subject to review. That means the insurer has effectively reserved to right to hike up non-guaranteed premiums for the benefit covering 30 dreaded diseases, whether it is bundled with the whole-life plan or offered as an additional 'rider'.

In the event of a premium increase the policyholder has three options. They can either pay the extra amount, reduce their sum assured to keep premiums at the same level, or discontinue the policy. But if none of these options appeals to you, there is good news, because Aviva is still offering whole-life plans bundled with coverage for 30 dreaded diseases with guaranteed premiums.

Aviva's ELA, or Enhanced Living Assurance, is a participating whole-life plan that comes bundled with a benefit for 30 dreaded diseases. The basic ELA is an affordable plan priced with premiums to be paid up to the policyholder's 85th birthday. This plan is available to anyone aged from 20 to 60 years old. ELA 12, meanwhile, is a limited 12-year-premium whole-life plan. What this means is that premiums are payable for just 12 policy years, and this plan is open to juveniles with a minimum age of just one month. ELA 21 is similar, but requires premiums to be paid for 21 policy years.

GUARANTEED PREMIUMS

Life insurance premiums are priced based primarily on mortality tables, and the lower a person's age, the lower the mortality risks assumed, generally speaking. This is true of all life plans, but a trend has developed in overseas markets to increase dreaded-disease premiums by an average of 20%, directly resulting from higher re-insurance costs from poor claims experiences.

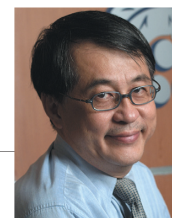
NTUC Income, in underwriting SAFRA's Group Term and Living Plans, announced an increase of premiums from April 2004, for example. For SAFRA's Group Living plan for those aged 51 to 65, the impending increase for a sum assured of S$10,000 (currently at S$17.50) was to be revised to S$38.50 per year, a rise of 120%. Since then, however, after appeals from policyholders NTUC Income has magnanimously withdrawn the increase, but it warned of premium rises of no more than 10% in the future.

FOR LIFE

Aviva's ELA, ELA 12 and ELA 21 plans also have no stated expiry date in the policy document, so as long as no claims have been admitted and paid (meaning the policyholder is alive and well), the policy will continue to provide lifetime coverage for death and 30 dreaded diseases.

Total and permanent disability coverage expires when the policyholder reaches 65, which is the industry standard. As for hospitalisation and surgery plans, not to mention other medical plans, there is none that comes with a lifetime of coverage except for NTUC's IncomeShield Plans B & C, something that underscores the importance of the lengthy coverage offered by whole-life plans.

Aviva has indicated that it will endeavour to keep the guaranteed premium for the 30 dreaded diseases benefit as long as it can, but has warned that they have no absolute control over this as it will hinge largely on the existing agreement with their re-insurer. Even so, is there a better alternative than to hedge the inherent risks of the three 'D's through Aviva's whole-life plans? **si**



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