Swiss Re

Life claims: balance of risk

Summary

This report is written against a backdrop of the FCA's proposed Market study into the Distribution of Pure Protection Products to Retail Customers (MS24/1.1).

While much of the initial market commentary following the launch of the draft Terms of Reference concerned remuneration and commission models, we would expect the Study to go deeper and build on the expectations set by the Consumer Duty, including the wider aspects of products and propositions such as fair value and demonstrating that products meet a need.

In the context of death benefits, clearly the need is to make sure that the proceeds reach the intended beneficiary and to do so in good time.

In the report, we consider the balance of risk of potential poor outcomes relating to single own life term policy setup, and reveal the rate of progress made in 2023, following on from our previous report, *Life claims: a beneficial direction (October 2023)*. Unless otherwise stated, the data used are extracted from material provided to Swiss Re by UK insurers for its Term & Health Watch reports and subsequent enquiries.

Market risk factor movements in 2023

- **% policies in trust** – just 1.6 percentage points up to 18.2% of all term (including joint life), making the estimated **beneficiary gap** down only 1.7 percentage points to 77.2% of single own life policies
- **% non-advised level term assurance (LTA)** – another plummet of 28% in non-advised sales appeared to have little effect on overall trust uptake this time
- **% single life policies** – inched up again to 79.8% from 78.8% in 2022 for all new term policies
- **beneficiary nomination** – positive effects on persistency, payout speeds and reduced administration overheads compared to trusts.

External changes in balance of risk

- **% unmarried** – proportion of cohabitees increased, representing 40% of couples under 45 in 2022, up from 37% in 2020
- **intestacy exposure** – down for married couples but up for cohabitees
- **probate delays** – in 2023, the average time for issues of all grant types reached an all-time high of 13.9 weeks
- **Inheritance Tax (IHT)** – the number of estates affected increased to 4.62% in 2021–22, but still likely <1% of estates holding term cover
- **Financial Conduct Authority (FCA)** – growing retail protection focus and closed books now in scope of the Consumer Duty

With so much at stake for claimants to lose, there's no more time to lose in closing the beneficiary gap.

We are grateful to all those who have contributed responses and data in this report.

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Introduction: FCA focus on pure protection

The FCA has already taken a close look at one feature of protection policies affecting outcomes at claim. The findings of *its review of terminal illness*, published in October 2023, highlighted several areas with potential for poor terminal illness claim outcomes to address.

This was also referenced in its insurance market *portfolio letter* published in September 2023, where life insurers were called out for "slow transfer and claim settlement times… and poor service standards targets".

There is potential for the regulator to look into claims processes again in its *proposed market study* into the distribution of pure protection products to retail customers.

Naturally, consideration of "whether the market is functioning well and whether consumers are receiving good outcomes" will focus to a great degree on competitive financial "value" aspects, such as potential conflicts of interest in the structure of commission, and the structure of commercial relationships across the industry.

However, the first of the four themes listed in its draft Terms of Reference for exploration is about **Consumer needs, engagement**, **and understanding**. Topping the list of issues under this heading are not just "the benefits and the value of pure protection products to consumers", but also "the nature and complexity of products and whether they are presented in a way that is understandable to consumers".

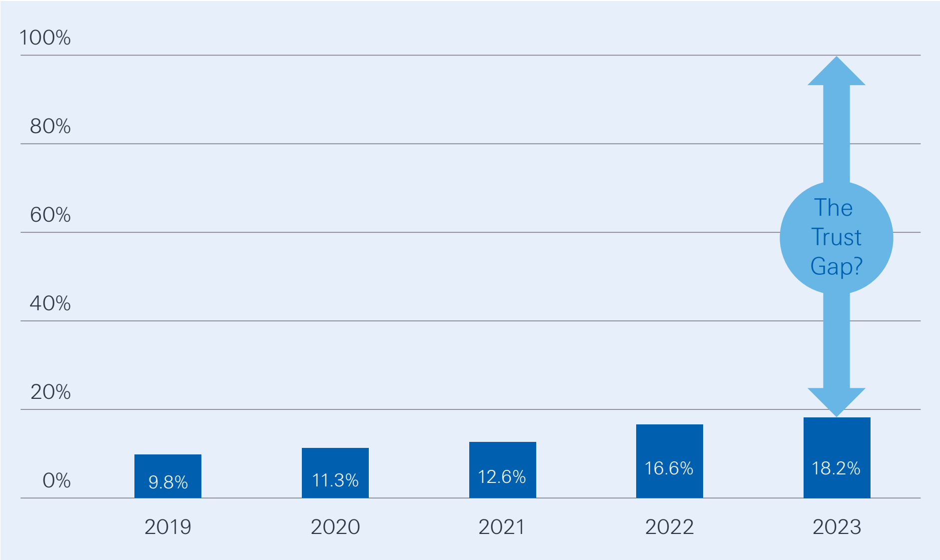
When it comes to the complexity of payout of death benefits according to how the policy has been set up, the data in this report indicate that consumers (and even some intermediaries) still don't understand well enough to ensure their intentions are met.

Regardless of potential FCA interest, there is clearly an opportunity here to enhance new business processes in order to improve claims outcomes.

Trust uptake increase rate slowed

In 2023, the proportion of **all** new term policies (including joint) increased by only 1.6 percentage points, having increased by 4.0 percentage points in 2022.

Term life policies in trust



The three other factors affecting the total number of term policies not written in trust also continued in the same direction as in 2022:

- the proportion of new single own life policies increased to 79.8% (78.8% in 2022)

BUT

- total new term sales fell by 165,484 (10.7%) compared to 96,287 (5.9%) in 2022.
- non-advised term sales fell by 110,703, nearly a quarter compared to 122,821, over a fifth, in 2022.

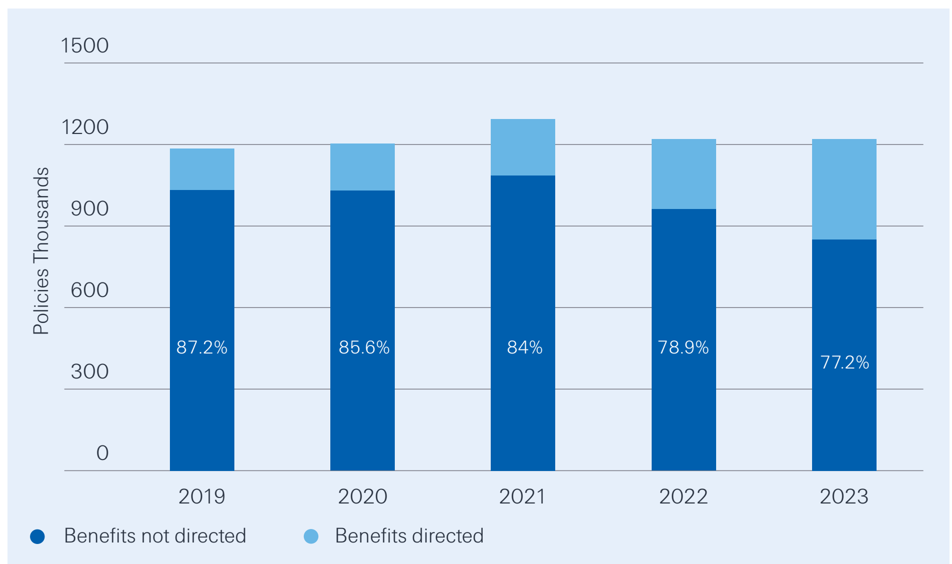
If there is a silver lining to the drop in sales, it is that fewer single own life term policies not written in trust (or beneficiary nomination) were added to the cumulative total for existing business. This total will have increased by approximately 852,000, compared to 962,000 in 2022 and over a million in each of the three years prior to that.

Beneficiary gap nears three quarters

18.2% of all new term policies were written in trust in 2023, which implies a maximum of 22.8% of single own life policies placed in trust in the same period, up from 21.1%.

This implies a minimum of 77.2% of single life term policies were still not written in trust, a modest improvement from 78.9% in 2022.

Single own life policies – beneficiary gap



The beneficiary gap estimates shown assume:

- proportions of trust uptake from those able to supply trust data are representative of the whole market,
- all trusts are of single own life policies, and
- the latter are found from the aggregated average market splits between joint and single policies

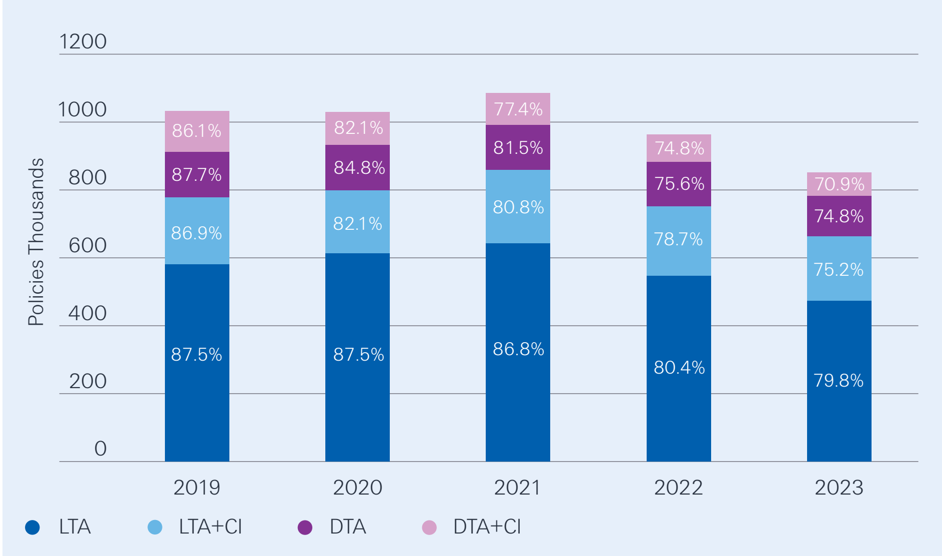
In fact, a few trusts are of joint policies, reducing the numbers actually applying to single life policies, but this can be expected to be set off a little by some policies having benefits directed by beneficiary nomination.

As before, comparing like with like, we have assumed that the above two factors cancel each other out.

However, as momentum is showing signs of building for beneficiary nomination, we intend in future to collect the actual numbers in both categories where possible.

Indications from the insurers who offered beneficiary nomination in 2023 suggest that **inclusion of the beneficiary nomination policies could have reduced the beneficiary gap to 68%**, accounting for another nine percentage points worth of single life policies with direction of benefits.

Single term not in trust



On the current basis, the totals are still dominated by LTA which masks the progress of about 3.5 percentage points in both products where critical illness cover is included.

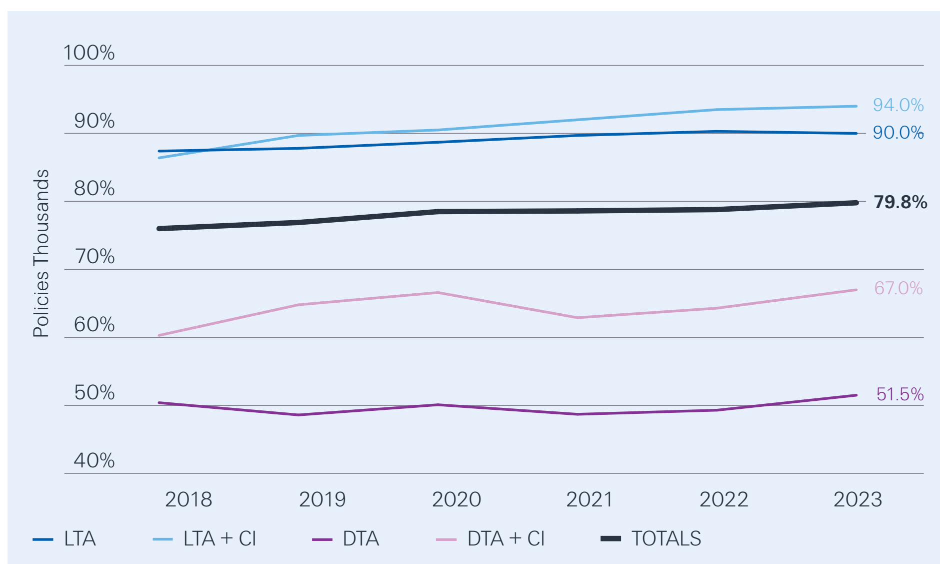
Beneficiary gap factor changes

Single life term continues to increase – up to 79.8%

LTA single life is a little down from its peak of 90.3% to 90% compared to joint life. However, single life policy uptake among the other three term products, reached their highest proportions so far. This took the overall proportion of single life sales to 79.8%, up from 78.8% in 2022.

The move is most noticeable for both DTA types of policy. In 2023, single life policies for these broke out of their previous fluctuating ranges.

% single own life



This upward trend in single own life, being a factor in increasing volumes of policies affected by the need of an extra step to achieve direction of benefits, is unlikely to reverse.

Sums assured linkage?

We wanted to understand whether the level of sum assured had any impact on whether a new policy was written into trust. For the first time this year, we are showing the average new sums assured for new decreasing and level term policies (without critical illness cover) in trust compared to the overall new average sum assured for all policies.

New decreasing term assurance (DTA) policy sums assured are driven more by the amount of the loan to be insured and reflect the current state of the mortgage market. There is little difference between those in trust and those which are not.

The average new sum assured for new DTA policies written in trust in 2023 ranged between £173,151 and £275,549.

	New DTA SA in trust	New DTA SA overall
2021	£208,198	£207,555
2022	£218,519	£216,848
2023	£211,796	£213,182

For new LTA policies, we were unable to verify all the data for 2022 and we have, therefore, decided to show just the numbers relating to 2021 and 2023. The average new sum assured for all new level term written in trust in 2021 was 3.6% higher than the market average overall, rising to 4.3% in 2023.

The average new LTA sum assured in trust reported by individual insurers in 2023 ranged between £134,515 and £272,458.

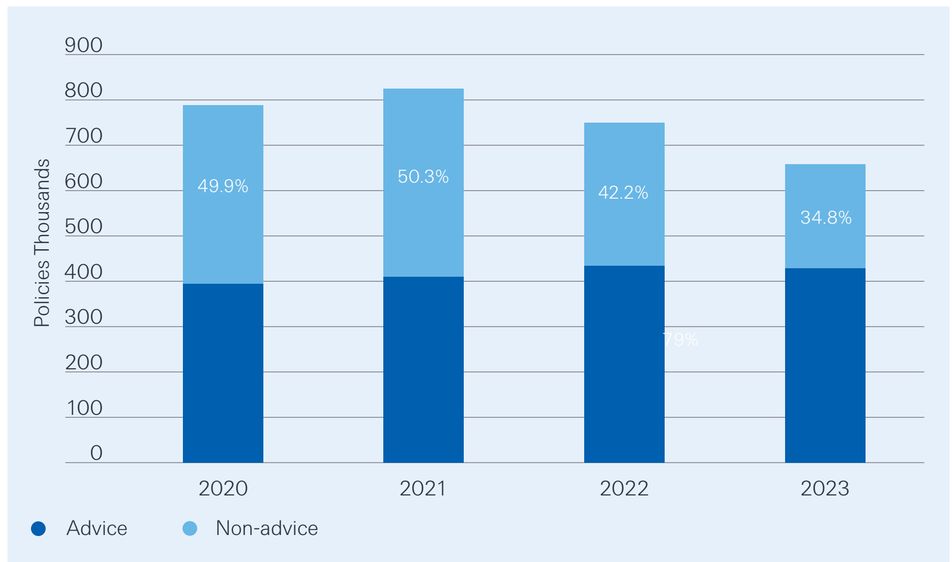
	New LTA SA in trust	New LTA SA overall
2021	£185,860	£179,430
2023	£197,885	£189,709

It is possible that slightly higher averages seen for LTA policies in trust could be due to a higher propensity to use trusts among a few policies at the higher sum assured range. But otherwise, the link to sum assured level looks weak.

Non-advice sales retreat

The big change in term sales in 2023 was the further drop-off of level term without advice, with little change in the volume of those sold with advice.

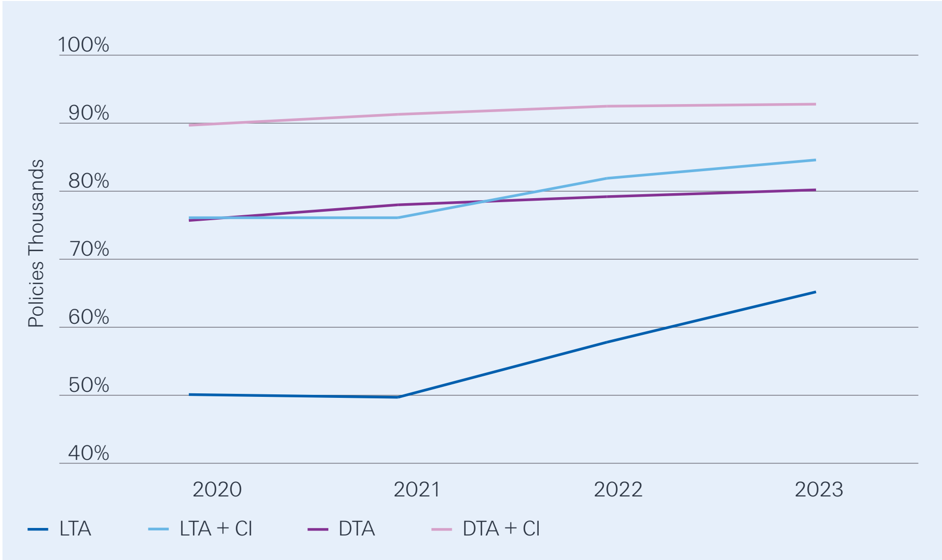
Non-advice level term (life only)



The 87,767-policy reduction in non-advised LTA policies sold compared to 2022 exceeded the total 77,717 reduction in all advised term sales and in the other non-advised term product types put together. LTA non-advised policies fell by 28%, compared to a drop of 17% for the other non-advised products.

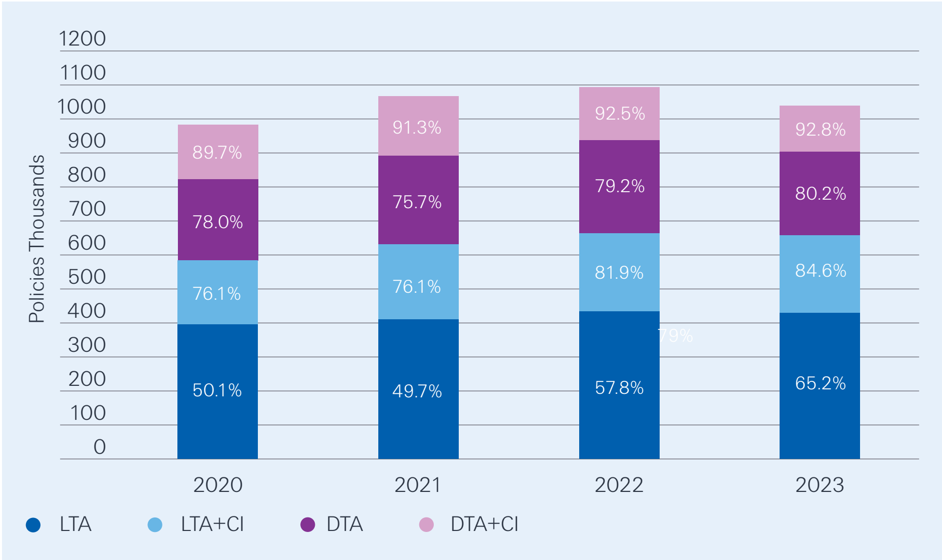
In other words, the 2023 contraction in term sales by 10.7% was driven by the retreat in non-advised LTA sales, even more than the contraction in the mortgage market of about 11%.

Advised policies %



Despite the large non-advised LTA drop in 2023, the market totals are still dominated by LTA policies and what happens with policy setup for those has a big effect on the overall results for direction of term death benefits.

Advised policies



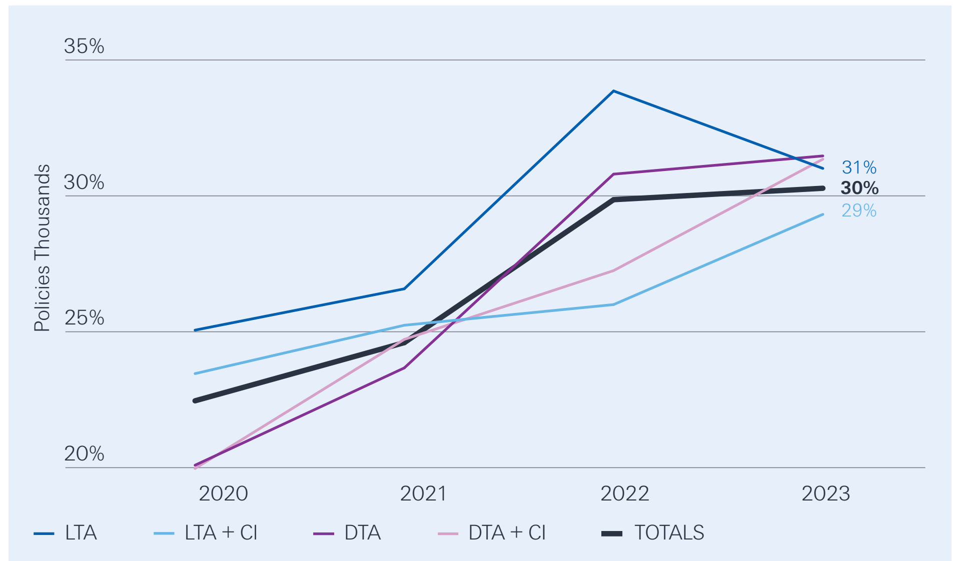
Trust gap amongst advisers

It could be assumed that the larger proportion of advised LTA sales would lead to an increase in the overall proportion of policies placed in trust.

Surprisingly, this was not the case in 2023.

Even if we look at the maximum possible proportion of advised policies in trust, assuming that no trust cases were non-advised (which is not the case), it appears that this fell by nearly a tenth from 34% to 31%.

Maximum % advised single own life in trust



More positively, the proportions continued to increase for the other three product types, with rates converging around 30% for the whole product set. This shows that there is still much room for improvement here.

Market insights

More beneficiary gap claims

While fewer policies with no direction of benefits are being added at the new business stage, having dipped below a million a year in 2022 and 2023, we expect that the number of these policies causing potential problems at claim must be increasing.

As we have already reported, the trend in policy setup has been steadily moving from joint life to single own life for many years. While, historically, many claims have been payable to the surviving joint owner, the business mix at claim will steadily catch up with the new business trend towards single policies.

The number of death claims under term assurance has been rising too. After deducting group life claims, the number of life cover claims paid under policies other than whole life has risen by 39% from 26,200 in 2017 to 36,458 in 2023.[1]

Possible reasons for this which may be expected to increase include:

- **Increase of policies in force** – Although term sales have fallen back over the last couple of years, they are likely to increase in the coming years as the financial crisis for households begins to ease and the pent-up demand for housing is unleashed.
- **Increase in term and age at commencement for new policies** – The cost of housing is likely to continue to push up the age of first-time buyers and put pressure on affordability of mortgages which can only be relieved by longer loan terms, even when interest rates reduce.

Insurers' experience

It seems that there was little change in 2023 from 2022 for most insurers' experience of trust and beneficiary nomination take-up.

iptiQ again reported beneficiary nomination take-up exceeded 90%. Guardian and Royal London continue to have the next smallest respective beneficiary gaps for single life policies, at similar levels to 2022, thanks to their beneficiary nomination options being used in greater numbers than trusts.

New information, however, came from Guardian, relating to persistency and to speed of payout for its policies with Payout Planner (beneficiary nomination).

It has been a matter of general knowledge for some time, that policies in trust have better persistency. Lapse rates for policies in trust can be over a fifth lower in each of the first four years in force[2]. Similarly, Guardian has found that policies with Payout Planner enjoy better persistency.

Guardian also revealed in its 2023 claims report[3] that seven months was saved at claim on average by using Payout Planner in 2023.

Elsewhere, a very rough current estimate of resource absorbed by dealing with various aspects of administering trusts illustrated that a current headcount of several employees dedicated to this work would need to be multiplied by nearly five if the beneficiary gap was to be reduced entirely just by trusts.

The burdensome side of trust administration is also reflected in the following comments by advisers explaining why they don't use trusts.

1 Source: ABI and GRiD
2 Source: Legal & General
3 https://content.guardian1821.co.uk/literature/2023-claims-report.pdf

Adviser comments on not using trusts

The beneficiary gap amongst advised polices is not just down to customers not completing the process. Advisers can find trusts difficult too.

We are grateful to Gregor Sked of Royal London who has collected a number of quotes from advisers attending his trust training webinars, which go a long way towards explaining this:

"The legal jargon puts off clients – and me!"

"It's too complicated to explain to clients"

"I don't have time to discuss trusts"

"Clients often struggle to think of suitable trustees"

"Trying to get clients to return the trust form is a battle"

"I don't have wealthy enough clients"

That last point really highlights a big perception problem. If IHT is the main reason to set up a trust, as much marketing material suggests, then most people really don't need a trust.

Other major impediments which are occasionally put forward prevent some advisers from tackling trusts altogether. A few have been known to say "I'm not authorised to advise on trusts" or "My professional indemnity insurance doesn't cover me to advise on trusts".

But this, of course, leads to a "catch 22" when it comes to doing the right thing for setting up life policies correctly to achieve their aim.

Existing business

Unfortunately, slightly reducing the rate of increase of policies with no direction to beneficiaries is not enough to reduce the overall problem. It is merely adding to the existing business mountain with more such policies being likely to crystallise in a claim.

In our previous report, we estimated that around eight million single own life term policies could be in force with only 10% in trust, meaning possibly two million policies could be meant for cohabiting partners who would not automatically receive the payout if intestacy rules were applied. With trust and beneficiary nomination uptake progressing for new business, we expect this will have improved and we wished to see if evidence of this is available.

After the new business data collection, we took the opportunity to seek additional comments from insurers about if and how they were intending to look at in-force business, in part driven by the extension of the Consumer Duty in July 2024.

A few firms were able to share data on the full details of their in-force policies in trust or subject to a beneficiary nomination while others currently have systems restrictions, including data on legacy books of business. These limit what they can produce, but they are in the process of creating a dashboard now as part of extending their management information.

"We have challenges on being able to report precisely, mainly due to the complexity of systems. We are expecting to deliver a system change in Q4 this year," one insurer replied.

Another said, "Unfortunately, the answer is no. If you ask again in three months, I'm sure the answer should be different as we are building a dashboard with this detail and more as we speak".

Where insurers were able to share an accurate figure, as might be expected from their attention to the matter, their numbers indicated they must be at the top end of the market for achieving direction of death benefits under single own life term policies.

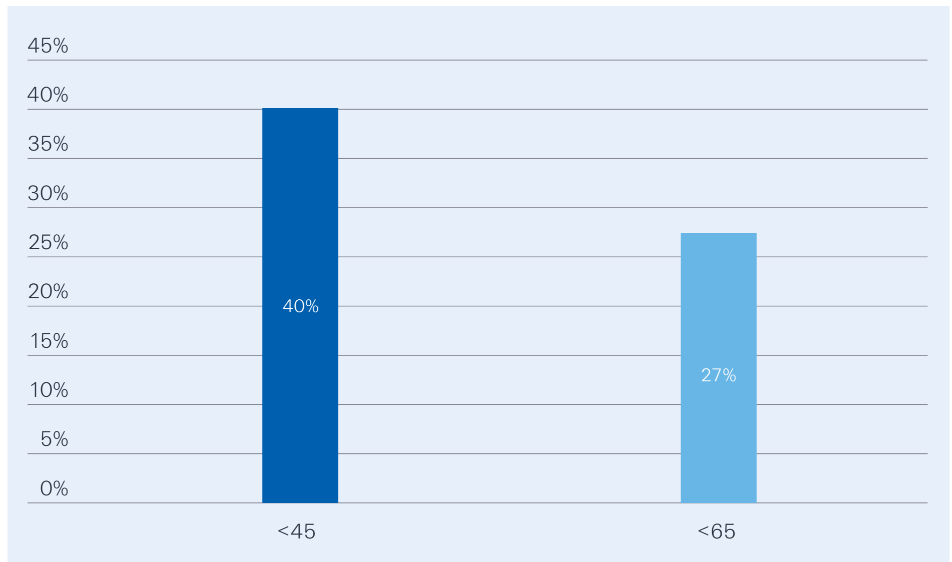
In future, we hope to be able to give a better indication of how the overall market stands, once more firms are able to supply data for this.

External factors

Cohabitee risk pool

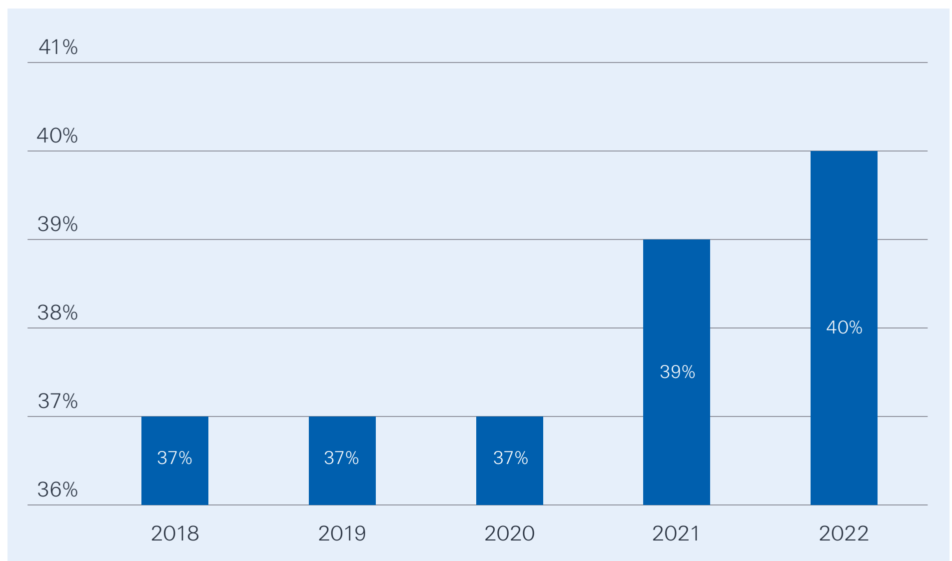
In our previous reports, we have indicated the following rule of thumb can be assumed: **One in three couples who take out life cover could be at risk of the money intended for the partner not reaching them, if some means of directing it to them is not put in place.** The most recent ONS analysis of living arrangements continues to underpin this.[4]

Cohabitees % of couples 2022



The proportion of couples under 45 living together without being married broke out from the previously established level of 37%. It reached 40% in 2022, up from 39% in 2021. For all couples under 65, it was 27%, up from 26% in 2020.

Cohabitees % of couples <45



This growing cohort of customers who stand to lose the whole of the proceeds intended for them if no step to direct the benefits is taken can no longer be ignored.

[4] Source: National statistics, 25.1.24 Population estimates by marital status and living arrangements, England and Wales, 2002 to 2022

Intestacy

The most important thing that intestacy rules of Scotland and Northern Ireland have in common with those of England and Wales is that **none give cohabiting partners any rights at all**.

This means that any **cohabitees will not get the policy proceeds meant for them** if the policy has not been set up to direct the benefits to them unless there is a will which does so that can't be challenged (which isn't always the case).

It's worth remembering that even life policy trusts may not help them if they have not been named as a beneficiary, because no life policy trusts included cohabitees as potential beneficiaries until Royal London addressed this in its discretionary trust launched in March 2024.

It is difficult for life insurers to identify which policyholders may be subject to this risk as they have no data to show who has an up-to-date enforceable will. Nor do they even know which policyholders are cohabitees since they stopped asking for marital status in application forms.

What gets mentioned even less is that even some married couples can stand to lose a portion of the proceeds under the intestacy rules of the three jurisdictions, albeit to a different extent in each one.

This is because the survivor is only entitled to keep a certain amount of the estate. Amounts in excess of that have to be shared if there are surviving children of the deceased.

The silver lining here is that recent changes have reined in the potential scope of loss of policy proceeds to widows and widowers, both in England and Wales and in Scotland.

However, it's extremely difficult to calculate the potential average scope of this risk. In the absence of any published data directly quantifying the outcomes of it, all that can be said is that in some cases the loss can exceed 40%. At the extreme, the higher the sum assured goes, in Scotland, the more the intestacy loss tends towards 66%.

It is also plausible to expect that the proportion of estates holding term cover affected by this is greater by several multiples than those liable to inheritance tax.

Probate delays all time high

It used to be the case that the main time taken for obtaining a grant of probate, or any equivalent, was dictated by the speed of action of executors or administrators of the estate, their lawyers and organisations they need to deal with to prepare the application for the grant. A survey of estate settlement times by the Legal Services Board some time ago[5], indicated that the whole process would typically take seven months. Within that, it would only be a few weeks from submission application to grant issue. Since reorganisation of the Probate Service for England and Wales a few years ago, the grant process has slowed down considerably, reaching an all-time high of delays in 2023.

Instead of under a month, the average time from submission of grant application to issue for all grants exceeded three months in 2023, being 13.9 weeks. If the rest of the estate settlement process is broadly the same as previously, that would mean an average nine months wait for beneficiaries.

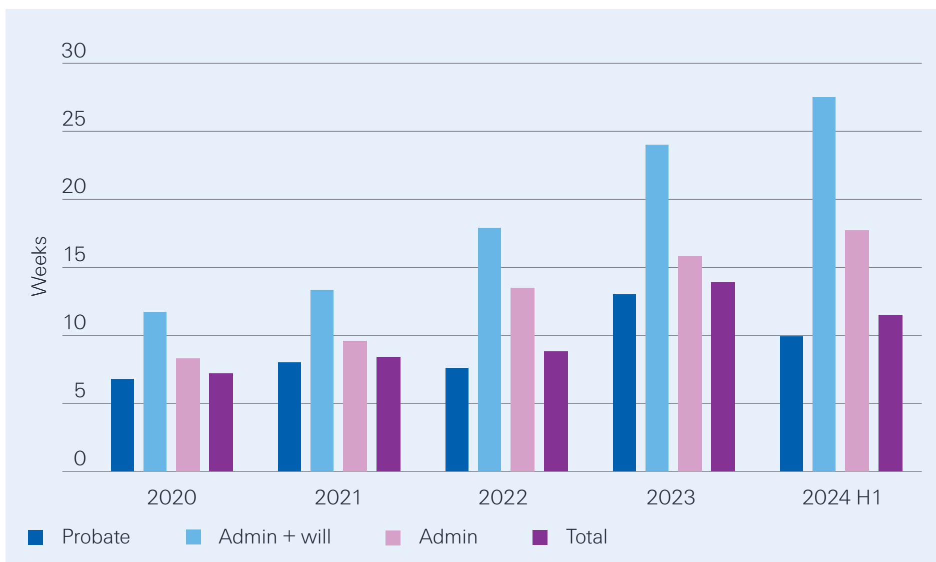
average nine months wait for beneficiaries

In 2024, there are signs of improvement in speed at the Probate Service[6], but only where there is both a valid will and executors able to act. The wait for administrators, with or without a will, has actually gone up.

[5] Probate and Estate Management Services Survey Report 2012

[6] Table 25, *https://www.gov.uk/government/statistics/family-court-statistics-quarterly-april-to-june-2024*

Grant application to issue



Fortunately, since the ABI issued guidance in 2011 encouraging insurers to pay without probate wherever possible, subject to claimants indemnifying them, increasing numbers of claims can be paid that way.

However, it can be a bit of a lottery for claimants as to whether they will benefit from this process. Probate limits vary widely and don't seem to feature as a factor in advice. Consequently, the claim in question may or may not be eligible for the process, even if within the limit.

Furthermore, the basis of the indemnity must seem a worry to some claimants. As the process was described at the time, "Claimants will also agree to pay back any money they receive from the policy if the legal process decides they were not entitled to receive the payout."[7]

IHT minor relevance to term policies

"I don't have wealthy enough clients"

The legacy of focus on inheritance tax as the top reason why a life policy should be put in trust can be seen with a quick Google search and explains why the majority of people might immediately think a trust isn't important for them.

If asked "why put a life policy in trust?" Google's AI Overview lists inheritance tax as the top reason, presumably because that has been the most common emphasis presented from many sources historically.

The two lines of summary text shown for each of the top ten website results shown for this query, all targeting mass market customers, still features a mention of tax in half of them. This is despite tax being the factor relevant to the least numbers of buyers of protection.

Only the result from Legal & General (updated in March 2024) highlights the most crucial point: "Setting up a trust is especially important if you're not married or in a civil partnership as, otherwise, your assets may not transfer to the intended recipient."

Admittedly, this only addresses a minority of life cover buyers, but it's a large one.

By contrast, for all the tax years from 2001–02 for which the statistic has been published, the proportion of all deaths resulting in an IHT charge has always been under 6%. From 2007–08 it has remained in the range of 2.7% – 4.62%, most recently being reported at 4.39% for 2021–22.[8]

[7] Money Marketing, *ABI issues guidance to speed up death claim payouts 23.5.2011*
[8] Source: https://www.gov.uk/government/statistics/inheritance-tax-liabilities-statistics/inheritance-tax-liabilities-statistics-commentary

However, life policies only account for a fraction of these. Furthermore, term life policies will only be a subset of these, with life investment bonds, endowments and whole life policies being included in that sub-set.

For deaths under age 75, the more relevant group for term, only about a fifth (21.2%) of taxpaying estates contained life policies, according to the last available asset breakdown, which was for 2020–21[9].

For under 65s in that data set, if the total number of deaths for that age group of adults was similar to the highest number of deaths of adults under 65 in the previous three years (about 78,500 in 2018[10], which can be assumed to be an underestimate for 2021–22), then only 2.6% of overall deaths at that age resulted in a tax charge. Only 0.55% of those deaths resulted in a tax charge and had any life policies in the estate.

A reasonable conclusion which could be drawn from the above is that there's less than a 1% chance of a term life policy being in a taxable estate.

Even in the light of the changes announced in the Budget, this would change little, while speed of payment and to the intended beneficiary will remain the primary reasons for using a trust or beneficiary nomination.

[9] Source: https://www.gov.uk/government/statistics/inheritance-tax-statistics-table-125-assets-in-estates-by-sex-age-and-marital-status-of-deceased
[10] https://www.ons.gov.uk/aboutus/transparencyandgovernance/freedomofinformationfoi/deathsofunder80sandunder60sintheuk2000to2020

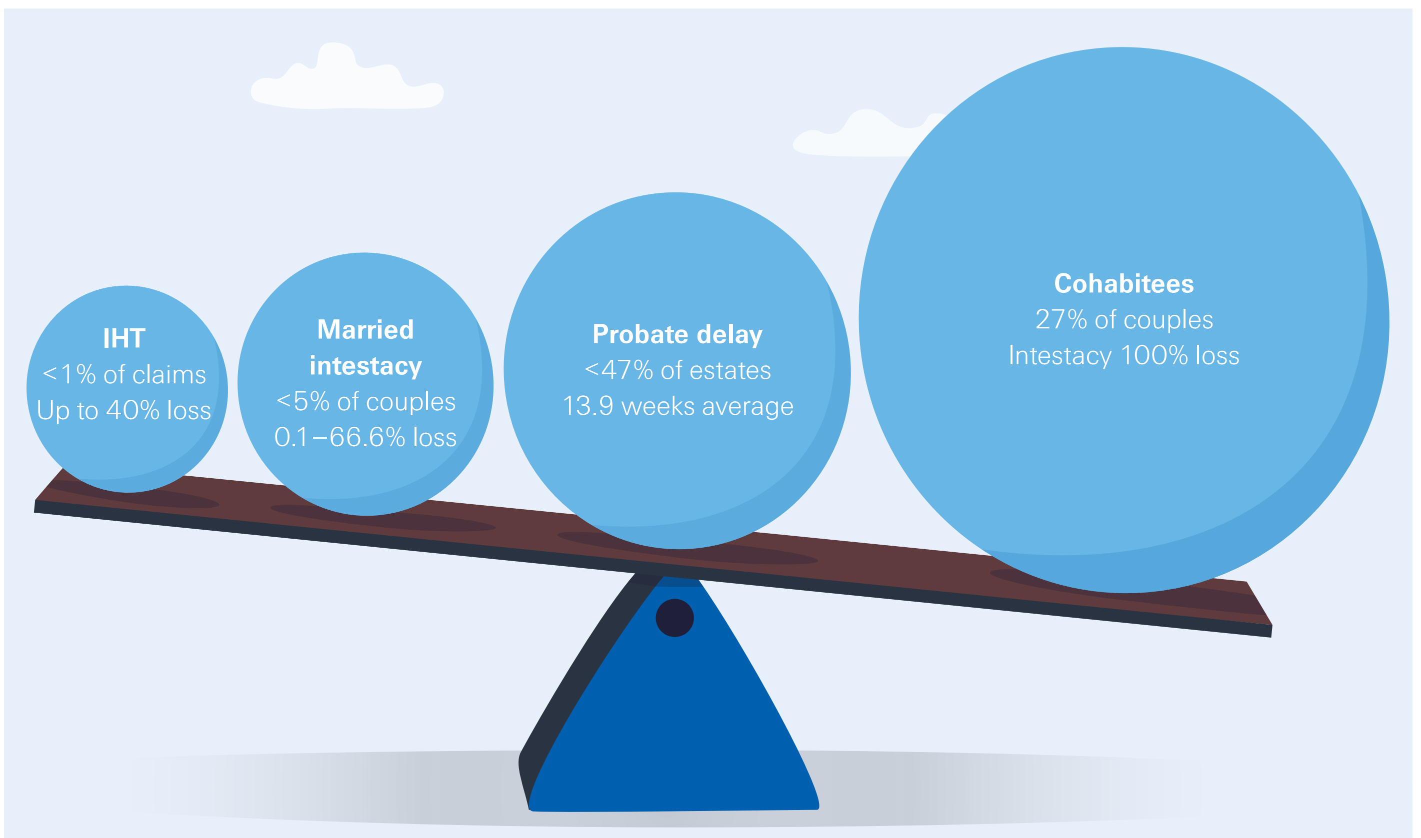
Balance of risk

The picture is clear on where most harm lurks for consumers and their insurance providers and advisers.

For a few, a partial loss to IHT (or even to intestacy, if a married couple's children are due a share) might be relevant.

For everyone whose policy doesn't fit insurer probate limits, delay can be stressful, but losses will generally be limited.

But for intestate cohabitees 100% loss of the proceeds will always be devasting, not just for the intended beneficiary, but potentially for the business called upon to compensate them.



Conclusion

Life cover has one job: On death of the life assured, to provide money in a timely manner to someone – not just anyone, but the particular person it is in place for.

The balance of risk of this not happening continues to weigh more heavily on cohabitees and those who are responsible for ensuring their access to the money intended for them. Whilst cohabitees remain a minority, they continue to represent a growing proportion of couples and stand to lose the whole of the proceeds meant for them on death.

This means that it is more important than ever that direction of life cover proceeds is embedded in life insurance propositions and advice or sales processes.

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11/24, Swiss Re Europe S.A., UK branch

Title: Life claims balance of risk

Graphic design: Swiss Re Corporate Real Estate & Services/Media Services, Zurich

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