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An Ethical Introspection of selling Life Insurance in India

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ABSTRACT

The landscape of Indian life insurance industry changed to a great degree due to opening up of insurance sector to private entry in India. Now as many as 22 private joint ventures and the public sector giant LIC are trying to entice the Indian consumers with well-designed products and benefits. In the process, the competition to lure the insurance buyers has reached such a feverish pitch where a lot of manipulations and unethical practices are taking place, in spite of stringent regulations of IRDA. These issues begin with unscientific appointment of insurance advisors, selling insurance policies without a proper need analysis of the investors, resorting to superficial health checkups as a part of the procedure, absence of follow-up of the existing policies as promised at the time of sale, ultimately leading to an increase in premature lapsation of insurance policies especially in private insurance companies. These are the ethical issues they can ill afford to ignore at this point in time as the corporate India is still coming to terms with the fallout of global meltdown. This paper attempts to throw light on these ethical dimensions of life insurance business and probable suggestions to lend dignity to insurance business thereby the industry can attract best human talent to cope up with challenges posed by liberalization and global economic meltdown.

Key words: Ethics, TCF, IRDA, ULIPs

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INTRODUCTION

Insurance is regarded as a social tool, which reduces or eliminates the risk of life and property. It is a contract between two parties – insurer (the insurance company) and the insured (the person or entity seeking the cover) where, the insurer agrees to pay the insured for any financial losses arising out of any unforeseen events in return for a regular payment called "premium". The principles of insurance works on the concept that large number of people exposed to a similar risk makes contribution to a common fund and those who suffer loss due to the occurrence of any uncertainties or risk are compensated from this fund. Life insurance products cover risk for the insurer against eventualities like death or disability.

Life insurance in India has its history dating back to 1818. It began when Oriental Life Insurance Company was started by the Europeans in the Bengal presidency to cater to the needs of the European community. Insurance regulations began formally by the passing of the two Acts in the year 1919 namely, the Life Insurance Companies Act and the Provident Fund Act. However, the first comprehensive legislation was introduced with the Insurance Act of 1938, which provided strict state control over insurance business in the country. Though the first legislation was enacted in 1938, it was only on 19th January 1956, that Life insurance in India was completely nationalized, through the Life Insurance Corporation Act, 1956. The result was the emergence of the Life Insurance Corporation of India on 1st September 1956.

While the early 90's brought forth liberalization on all major economic fronts, the insurance was left untouched in India. With effect from 1st, January, 2000, with the passage of the IRDA Act, the Indian Insurance Industry was privatized or deregulated. The deregulation was brought about with the following

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objectives: to increase coverage of population, propel a choice of better products with informed decisions, promote competition, encourage the entrance and joint partnership of foreign players with the Indian insurers, boost innovation, advance economy of operations, enhance customer centricity and service excellence and improve the efficiency of the public sector companies. The Insurance Regulatory and Development Authority (IRDA) was formulated as an independent body that would monitor and shape the insurance business in India.

The insurance industry has experienced significant change over the past decade. But never before have the changes been so pronounced, the pace so rapid and the scope so broad. Insurers are in the midst of a true paradigm shift. Their overning rules are changing. Their functional bodies are blurring. Buyers are becoming more sophisticated about services and value, and are ever more demanding. This heightened form of consumerism is spurring a new demand pressure on insurance products. At the same time, the industry is experiencing traditional financial pressures, as well as new competition, new market entrants, new substitutes for traditional insurance offerings. The industry is responding in many ways. There are at present 22 life insurance companies in India along with the public sector giant LIC offering various types of products—insurance, annuity, pension and health care to millions of people through a variety of distribution channels such as individual sales force, bank assurance and corporate agents. Providing a right product to a customer requires assessment of his needs and future implications. Therefore, agents and other entities involved in selling life insurance products not only need to be knowledgeable and technically qualified but also need to follow ethical standard to protect the interests of the policyholders.

NEED FOR ETHICS IN LIFE INSURANCE SELLING

Ethical selling means selling the right policy for the right sum assured, the right term and mode based on customer need. Ethics in insurance selling has always been an often debated subject among insurance people. The fact that the subject is often talked about is a sure enough indication of its importance and the concern that insurance selling should be 'ethical'. The questions that come up in this context naturally are the following: Are the sales taking place in the insurance market place by and large ethical? Has there been any significant change in this matter after opening up of the insurance market? And the more basic question: is ethical selling of insurance at all possible? In other words, is selling of insurance possible without resorting to unethical practices such as making untrue averments and the more common half truths and nondisclosure of material information regarding what the policy covers and what it does not? The following paragraphs attempt to throw light on those distinctive features of selling life insurance in India that further demonstrates as to why being fair and ethical is the need of the hour.

a. Insurance, still an enigma

Life insurance products continue to be aggressively sold and still considered as an unsought product. Liberalization of insurance industry which was supposed to add glitter and dignity to insurance business has not taken off in that direction since an insurance advisor continues to the most unwanted guest on our premises. In addition, LIC continues to be perceived by the investors as the only trustworthy player in the life insurance market in spite of 22 other high caliber life insurance companies.

b. Competition

Indian life insurance industry has entered into a new phase of growth after liberalization of the insurance industry and the setting up of the IRDA on 25 October 2000. While liberalization allowed domestic and foreign companies (as joint ventures) to operate in the Indian market, but whether the emergence of the new companies has brought about any significant change with regard to ethics in selling insurance is a big question mark. The intense preoccupation with producing results in the short term and beating the competition has been such an overwhelming concern that there is little evidence that anything is being done to promote ethics in selling. This is where corporate integrity comes in handy to distinguish the companies.

c. Built on "principle of utmost good faith"

In order to appreciate the main issue in ethical selling of insurance one has to only turn to the most fundamental principle of insurance, that is, the principle of '*utmost good faith*' Mere good faith is not good enough; it has to be 'utmost good faith'. Observance of the principle of utmost good faith applies with equal force to the insurer and the proposer. Court decisions have also confirmed that the need for observance of utmost good faith is also the bounden duty of the insurer's representative, the Agent. The observance of the principle of utmost good faith is thus not merely on essential requirement in an insurance contract; it is also the bedrock of 'Ethical selling' by the insurance agent.

d. Myths about private insurance

As far as the prospective entrants are concerned, the greatest challenge is to establish their presence in the minds of the public. Insurance, particularly life insurance, it is said, is never bought but sold. To convince a large population, which is comparatively not well informed about the intangible benefits of life insurance is indeed an onerous task. On top of that, to establish the brand equity of a new name in a new field is quite a challenge. The second most important challenge facing a new entrant is that of setting up infrastructure and to reach out to as many areas as possible, since life insurance is based on probability and the wider the spread, the greater are the chances of success in maintaining the expense ratios at a reasonable level. Add to the discomfort, large portion of India's insurable population perceive the new private entrants negatively and hence they cannot afford to keep even a step wrong since they are under constant scrutiny.

e. Regulatory needs

The biggest challenge faced by the Government today is that of a regulator with the prospect of about 30 or 40 players, each represented by thousands of agents, brokers and intermediaries. To evolve a free and fair method of assessing the companies, to ensure fair play between the competitors and to safeguard the interests of the largely uninformed customers are the main tasks ahead. The other and equally serious aspect is to ensure that the vast amounts collected by the insurance and pension funds are utilized for the welfare of the people.

ETHICAL ISSUES IN SELLING LIFE INSURANCE

As the insurance industry poised for robust growth in the years to come, there are a few reasons for worry. The competition among the 23 players has reached such a feverish pitch that the temptation to go over the board to corner the ever reluctant Indian life insurance customer is strong. The following paragraphs make an attempt to enlist some of the questionable standards of behavior being followed in Indian life insurance industry;

a. High pressure emotional selling

Life insurance has always been sold exerting a high degree of pressure since ages. An insurance agent has always been the most unwanted guest on our premises only because he literally pleads to accept his offer, most of the times, bombarding the customers with his own tragic stories and paints an image as if by accepting his offer, we are giving him a lease of life. In the process, the advisor ends up with misleading promises, overestimating future returns and undermining the risks associated with the concerned investment. Hence the buyers of insurance will always have a negative preference towards investment in life insurance.

A recent phenomenon is to rope in management students of graduate and postgraduate level to log in a few life insurance policies as part of their internship and project reports to fulfill their academic requirements. The more you log in, the more marks you get. Most of the students pursuing research in life insurance start with a back foot and may end up with changing their area of study.

b. Over selling, under selling and mis-selling

Over selling in fact is bad for all the stake holders as it invariably results in lapsation. Under selling can be really tragic if the insured dies prematurely as what insurance pays is not adequate to meet the family's

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need. Many a time underselling takes place as the agent is afraid that he may be bluntly refused and lose the business if he suggests a bigger policy which is what the customer actually needs.

There is a growing concern today about mis-selling in the insurance market place. This concern is an indication of the awareness about the problem. Unless this awareness leads to corrective action by the companies there is little hope that anything much will happen.

c. Unscientific appointment of Insurance advisors:

With the qualification for an Insurance Advisor being plus 2, there is a huge risk of taking under qualified college dropouts as advisors. The essence of life insurance is building a long term relationship between the insurer and the insured and an advisor happens to be the most important link between the two. He needs to be not only knowledgeable but also a thorough professional in his approach, besides enjoying the job on hand. But, instead, we have a situation where an insurance advisor takes up the job just as a stop gap arrangement and with an air of casualness. This has resulted in high percentage of new licensed advisors but importantly a higher percentage of license cancellations as well. Unless the advisors enjoy a reasonable stability of tenure, there is highly likely possibility that they are tempted to make exaggerated promises to close an insurance deal hoping that they would not be around when it comes to keeping up the promises.

d. Callous Advisor Training Programmes:

The very purpose of any insurance training programme is to impart the required knowledge, sharpen the tactical skills and acclimatize the insurance advisor to the company's environment. This is one programme that needs to be taken up seriously if at all any company wants to ensure sanctity in its operations. But most of the advisor training programmes are run so superficially that it is more of a formality than any serious interaction. Some of the influential candidates may even skip attendance and get away with it. Unless an ethical sense is instilled in the very first programme that a potential advisor attends, ethical behaviour cannot be expected from him later. Even the exam at the end of the training is also an eye wash and hence, the whole ambience in which this exercise is undertaken definitely has standards that are ethically questionable.

e. Absence of Customer needs analysis:

This is the crux of the life insurance business. It requires that an advisor has to understand the financial needs of an individual depending on his earning capacity, dependents, future productive years etc. and calculate human life value of the person in question. Accordingly, the advisor has to advise him on the best insurance policy that suits his requirements. But what is actually being done is that most of the advisors keep their commission needs as the top priority and sell those policies that give them the maximum remuneration. There is an increasing tendency among the advisors to get selfish and take the customer for a ride. The company is also pressurizing on them to reach the targets in terms of commission earned and the number of policies logged in. In this high pressure race, the customer ends up with a policy which is contrary to what his needs are. Ethical selling of insurance is also about 'need' based selling. But whose need? Sales Manager's and Branch Manager's; or the customer's? Make no mistake about it, ethical selling has only one meaning in insurance selling: the customer's need. The agents need (in some cases greed) for commission, his desire to qualify for MDRT, the Sales Manager's dream to become eligible for a foreign jaunt, the Branch Manager's ambition to earn quick promotion with high perks are all needs indeed. But all these are totally irrelevant in the context of selection of the plan term and sum assured. The marked reluctance to sell term and pension polices, the penchant for pushing ULIPs without explaining what risks this policy is exposing the customer to - are all classic examples of selling without the customers' interest in view.

f. Superficial Health Check-ups:

Insurance is definitely a cover against health hazards, risk of life, accidental deaths etc. Every person taking out a policy needs to be checked for his health

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conditions since they are an important determinant in finalizing the premium amount to be paid. We know it for sure that the seriousness with which this particular aspect is being approached. We hardly have any comprehensive health checkups; instead the company and the approved medical officer would have completed the task even without our physical presence. This is one issue where the company stands to loose since it may have to shell out for huge medical expenses for the inappropriate medical checkups done. Of course, the competition might have led to this situation, but these are those small little things which go a big way in adding dignity to the insurance profession. Factor in the relative lack of sophistication of the Indian market, there is every reason to believe that the managed health care racket will grow without restraint until it causes deaths — which is usually when the government steps in and constitutes yet another enquiry commission which will achieve little other than keeping one more member of the legal fraternity in continued employment.

g. Customer relationship management and Transparency:

These are the two words which are increasingly used in the context of understanding the ethical conduct of an insurance business. There is of course a huge difference in transparency levels that we see today than when only LIC was operating. Now, an Indian insurance customer has the access to the information as to how his money is being managed by the company in which he invests. Use of the sales illustration, the inclusion of the policy proposal form, and the free look period offer has been served to win customers' trust. By giving customers the option to track investments online and by publishing the performance of the funds against benchmark indices, transparency has reached dizzy heights. But all said and done, does every customer have the required knowledge and passion to monitor his investment options? Is it not the responsibility of the insurance companies to keep him updated about his money and be a constant advisor to ensure a long term customer relationship? Insurance contracts combine traditional actuarial risk and financial risk. A simple example is a unit-linked pure endowment contract with guarantee. With this life insurance contract, the sum insured payable to the policy-holder at the term of the contract is contingent upon survival but linked to the development of some stock index and guaranteed against falling below some amount. The actuarial risk in this contract stems from the uncertainty of not knowing whether or not the policy-holder will survive until the term of the contract, and the financial risk is related to the performance of the underlying index. To convince a large population, which is comparatively not well informed about the intangible benefits of life insurance is indeed an onerous task. In a business such as life insurance, where the customer entrusts the companies with his / her financial savings, ethics has a direct relation to sales. Hence, transparency should start from the bootstraps and integrate itself to all aspects of the relationship till it boils down to settlements.

h. The controversial ULIPs

This discussion would not be complete without comments on the controversial ULIPs. There is nothing wrong with the 'ULIPs' per se. What is wrong is the way they have been designed by some companies giving scope for unethical selling and mis-selling. This has forced the regulator to come out strongly to 'Clean up' the act by issuing a set of guidelines. The guidelines make it clear what was wrong with the products put in the market and the manner in which they were being sold. The flaws identified by the regulator are (i) there was no fair insurance cover (ii) there was no transparency in the product terms and conditions. (iii) the long term character of the insurance product was given the go by and (iv) the disclosures by the company as well as the sales persons were grossly inadequate making it impossible for the prospective customer to take an informed decision. In view of these difficulties what was conceived as an insurance product with an investment element ended up becoming an investment product with an insurance element and sold as such. The terms and conditions offered ample scope for abuse and misselling by the salesperson who earned huge commission. The product was good for the insurer too who saw unprecedented premium growth. But was it good for the customers who were exposed to market risk in the context of the falling sensex?

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THE WAY AHEAD: TREATING CUSTOMER FAIRLY

The mantra 'Treating Customers Fairly' (TCF) has been around in the statutes of all financial market regulators and remains a key strand of any consumer protection agenda. The TCF initiative is aimed at helping customers to understand the features, benefits, risks and costs of financial products. It is designed to minimize the sale of unsuitable products by encouraging best practice before, during and after a sale. Many insurance players have taken steps to improve their focus on consumers. It is in the industry's interests to define and establish good practice. Given that the emphasis should be on the prevention of problems, a focus on what insurers should not do is helpful in closing the door on specific bad practices, but to avoid perpetuating the cycle of crisis followed by clean-up, it is important to look at what good practice should be, perhaps in the context of new developments. Here are some ideas on how things could be improved besides making a serious impact on improving insurance services for consumers, and ultimately for the industry itself.

a. Change in culture

No amount of generic advice will overcome the lack of confidence consumers have in the market unless insurance market players change their culture and develop strategies to treat customers fairly that are not only talked about in head office, but also implemented in the market. Whilst firms talk about raising standards, there is little change in the way that some firms treat their customers on a day to day basis. The commitment in the boardroom must embrace every aspect of the service chain – a company's operations, from the way it presents itself through symbols and logos, through to its day-to-day working practices. The sense of consumer disappointment is enhanced by the continuing tendency to stress performance at the expense of less exciting factors such as cost and flexibility. Insurers appear to rate themselves on short-term factors such as sales, funds under management and distribution deals. If they can develop a set of values that recognize how closely consumer confidence is bound up with customer service, and instill these values throughout their workforce, then treating customers fairly should be natural consequences.

b. Product design

An insurer should be able to show that its products have been designed to meet the needs of its selected target market. For example, consider a new unitized with profits contract designed to offer investors the benefits of a smoothed return on a pool of assets, to meet the savings needs of certain policyholders. Suppose, in line with recent trends, the new with-profits product does not offer any significant guarantees and the investment policy is biased towards higher risk assets such as equities. Through stress testing, which involves modeling how the product performs in different situations, the in house actuaries should be in the best position to ascertain the risks inherent in the product structure and help assess for which groups of customers the product is most suited. Stress testing may also indicate if the product is suitable for customers who are willing to risk losing part of their initial investment in the short term in order to seek better returns. In the longer term, it is important for developing this understanding and should ideally form part of the product development process. An insurer should also assess whether the policy conditions are unnecessarily complex and hence difficult for consumers to understand. Moreover, changes to the policy design, such as the addition of a particular exclusion may change the target customer base. Hence, there might be knock-on effects for pricing assumptions such as average propensity to claim; decline and fraud rates; and adverse selection.

c. Identifying target markets

The industry needs to look for new markets and new ways of distribution which reflect consumer diversity. Insurers should be given an incentive to introduce socially responsive product innovations and alternate distribution channels that reduce costs overall. The aim of increasing saving cannot be met alone if firms continue to concentrate on 'high net worth individuals'. Commissions are only part of the cost. In so far as target-setting is concerned, past experience has shown, pure sales targets can backfire if they lead to low quality sales, complaints and compensation claims.

How can quality, rather than quantity be rewarded? Are companies setting the right targets?

d. Incentives and costs

Getting the incentives right is part of the process. Currently, the culture is sales based where the most prominent figure is the rate of commission. This is a form of market distortion that tars the reputation of those advisers who truly put their clients' interests first. It can directly affect the quality of products offered to consumers, not to mention the effect on company costs.

Commission rebating is also not the answer: it benefits the well-informed at the expense of the less savvy, and may actually inflate commissions in order to allow the extra to be rebated. One needs to find ways of rewarding continuing service. Can mystery-shopping be used to reward good practice? The financial rewards that senior managers get should reflect the rewards received by policyholders, not just shareholder value. Policyholders find it galling to see bonuses awarded to management when the value of their investments has declined.

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e. Marketing and sales literature

Consumers need both clarity and frankness. The drive towards plain language and issuance of documents in local languages can make some documents more attractive and easier to read. However, some important information may still be hidden away in small print and technical language. Improvements in consumer education, if achieved, imply that insurers should be prepared for a more knowledgeable market, asking more difficult questions. Better communication cannot be solved purely by regulators telling companies what to do. Necessary steps also need to be taken to develop a common terminology. This is an area where some common industry approach might help consumers. Insurers should provide clear information, which will instill consumers with the confidence to make appropriate decisions and give them the ability to question the information and advice they receive. For example, the marketing material used to promote the product will need to be reviewed to ensure that risks are clearly stated. Many policyholders and their advisers naturally associate the word 'withprofits' with 'guarantees' and should be clearly highlighted to the marketing and sales personnel as well as in the product literature.

Consumer education should not just teach consumers how to understand the industry. The IRDA and others must improve the way that insurers communicate. They should be asking what customers find easy or difficult and using this information to improve their practices. Some may be doing this already, but it would improve the industry's standing if it were carried out in a more transparent, industry-wide basis. Although firms could have a role in ensuring the provision of generic advice, this needs to be separate from the sales process. Further work may be needed to ensure the introduction of consistent, acceptable standards and monitoring.

Often the problem is not the language, but the concepts. As an absolute minimum, consumers need to understand all the factors that limit performance of an investment, even if they do not need to know exactly how it is engineered. amount of charges deducted during the year. That makes it difficult for consumers to judge whether they are getting value for money and whether they might be getting a better return on their investment if they took it somewhere else. Customers need to know if they are paying out more than an investment is actually earning.

f. Claims

For most insurers and insurance intermediaries, the main point of contact with the policyholders after the sale is at the point of claim. TCF in a claims department will entail ensuring that genuine claims are paid and handled promptly. It is important that the level of evidence requested from the policyholder is reasonable and not perceived to be putting off claimants. Fraud detection approaches need to balance fair treatment of customers, particularly the elderly who may be caught out by more aggressive questioning techniques. Where elements of the process are outsourced, it is important to ensure that any outsource providers adhere to the same TCF standards as the insurer.

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g. Complaint handling

Avoidance of double standards, such as following complaints-handling procedures to the letter but having a policy for turning down as many complaints as possible is part of the process. Insurers need to be straight with their customers to gain their trust in the long term. Despite regulatory standards for the handling of complaints, the rhetoric often undermines this. There is even a tendency in the industry to ascribe complaints to a ‘compensation culture’ that encourages people with weak cases to complain. The industry as a whole should conduct research on how they can promote confidence without encouraging false expectations.

‘Consumer audits’ are used as management tools in some service-oriented organisations. They provide a customer’s perspective of the organisation by using, for example, customer surveys of key indicators (not just ‘satisfaction’) and analysis of outcomes, including complaints volumes and trend data. Such initiatives should be championed at Board level, perhaps through the non-executive directors or through some consumer representation. Insurers could be required to demonstrate publicly – perhaps through the annual report – what they have done to satisfy the TCF principle.

h. Management Information

Appropriate key performance indicators (KPI) are important to enable senior management to monitor TCF and whether the product is being sold to the appropriate target market and meets the needs of the customer. For example, on a life policy, the age of policyholders at entry, duration of specific lapse rates, and number of complaints. The distribution of the age of the policyholders can be compared with the target market identified during the product-development process. Duration specific lapse rates will enable identification as to whether the product met the needs of the policyholders. A similar array of management information tools including retention rates, loss ratios, claims decline rates, etc, is available for general insurance. Loss ratios and claims decline rates can provide an early indication that the product may have TCF related issues.

i. Consumer panel

The insurance industry needs to engage in serious dialogue on a regular basis with consumer bodies and other interested parties on issues such as access for the less affluent and general consumer confidence. There is a need for the industry, the regulator and consumers to establish a collective, forward-looking joint agenda. This should particularly focus on how the industry can better serve its customers. The IRDA may consider establishing a broad ranging forum, including representatives from all parts of the industry, consumer groups, the IRDA and Government. This should meet regularly with the aim of agreeing priorities, monitoring progress, giving early warning of problems that might be arising and putting pressure on laggard.

CONCLUSION

Life insurance has today become a mainstay of any market economy since it offers plenty of scope for garnering large sums of money for long periods of time. A well-regulated life insurance industry which moves with the times by offering its customers tailor-made products to satisfy their financial needs is, therefore, essential if we desire to progress towards a worry-free future.

It may be observed here that a ‘good sale’ which of course will be the result of ethical selling is a satisfactory proposition for all the stake holders - the customer, the agent and the company. Such sales can be described as win-win situations and they enhance the image of the agent as well as the company and become a model for others to follow.

Ethics is an attitude that needs to touch every aspect of the customer relationship. It entails having great reverence for the customer’s needs, being open to suggestions and insights that might enhance his / her comfort levels, building in riders and flexibility options that address these needs, providing assistance and clarity in documentation and upgrades, and settling claims on time. Ethics means being fully accountable, not just to the company and to its customers, but to the industry we serve. The inspiration for ethics thus comes from the highest source - from a need to impact the industry.

On the flip side, a lack of ethics can have serious consequences. Litigation and costs of settlement, business losses, a reduction in ratings, and increased scrutiny are not half as damaging as the loss to image and reputation. It's a fact that good ethics makes good business sense. Of course, the mandate for good ethics always stems from the top. Which explains, all the players in the insurance industry have to introduce a system of checks and balances that guards against concealment and why we follow norms of compliance and adhere to IRDA regulations so scrupulously that books and processes are open to audit at all times. While top management can lay down a code of ethics and request adherence, its implementation depends on the individual. As Albert Einstein said, "Ethics is an exclusive human concern without any superhuman authority to back it." To this it can be added that ethics is that discipline, that momentum that challenges us to rise above ourselves and raise the bar each time we interact. It is the means by which we measure ourselves, the strength by which we progress, and the light by which we shall be remembered. It is the way ahead - for each of us and for every industry and more so for life insurance business.

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