

Overview of insurance underwriting



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By
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It has been said that responsible people buy life insurance for one of two reasons – they either love someone or they owe someone. However, purchasing life insurance is not as easy as buying any other type of financial product. Just because someone wants it and is willing to pay for it, doesn't mean an insurance company will offer to insure

them. Once someone applies for life insurance coverage, the application must go through a strict underwriting process by the insurance company before an individual is eligible to even purchase the policy.

The underwriting process is still a mystery to most financial professionals, even more so to their clients.

In essence underwriting includes the following three steps:

- Examination of the application
- Decision as to whether to insure
- Determination of the premium

It is as true today as it was when Albert Einstein originally said, "Make everything as simple as possible, but not simpler." The aim of this month's column is to demystify underwriting.

The insurance acts in each Canadian jurisdiction detail that

an applicant for life insurance is obligated to report all relevant information about their health and finances that will allow an insurance company to properly evaluate suitability for coverage. The applicant must provide four types of personal information:

- Details on income and lifestyle
- Medical history
- Medical history of applicant's family
- Hazardous occupation or activities

A life insurance policy is referred to as a contract of 'uber-rima fides' translated as 'in utmost good faith.' The insurer depends on the applicant for complete disclosure. The negative consequences that can result from misrepresentations on an application may range from a delay in approval to voiding the policy.

For an individual to sell life insurance they have to be registered as an agent with the provincial licensing regulator and hold an errors and omission insurance policy. The agent's primary role in the underwriting process is to record the client's information on an application. This process is called field underwriting.

The responsibilities the agent has regarding the application include collecting information accurately and completely, educating the client on the consequences of incorrect information and witnessing the client's signature on an application.

If the applicant qualifies they may receive a *Temporary Insurance Agreement (TIA)*. The TIA provides coverage while the underwriting process is completed. Applicants can receive the TIA provided that they qualify as a standard risk and include one month's premium with the application.

The TIA insures the applicant for 90 days after the application has been signed or when the insurance company has completed the underwriting process. The maximum amount that can be insured for under the TIA is \$500,000.

The agent must inform the applicant that by signing the application they are authorizing that their medical history to be released to the Medical Insurance Bureau (MIB).

The MIB is somewhat like a credit bureau and exists to share medical information among insurers. There is an MIB pre-notice form that is left with the applicant to read after the application is signed.

Lastly, after the application is signed by the applicant and before it is delivered to the insurance company, the agent is required to fill out what is referred to as an agent report. The agent provides notes and comments about the applicant that might assist in the underwriting process.

Insurance legislation across Canada states that once someone is offered a life insurance policy that was based on truthful information provided by the insured, the insurer must honour the contract. Therefore the insurance company must be sure that providing coverage to an insured is a good investment.

In essence both the insurance company and the policy holder make a bet with each other. The insured is betting that one day they will die and the insurance company is betting that the insured is not going to die today.

The policy is issued only after the insurance company underwriters have reviewed the inspection and medical report. This report is prepared by a third party interviewing the applicant to confirm the information. The objective of the inspection report is to

determine whether or not the insurance value applied for is justifiable. The size of the amount will determine whether there needs to be a medical exam, either by a paramedical service or a physician.

The inspection report verifies information on the application, especially information related to financial matters. After all this information has been collected and reviewed the coverage can be approved. The premium rates are based on the insured's age, gender, and health.

The final requirement in creating a contractual agreement between the policy owner and the insurance company occurs only when the policy is delivered to the applicant. The policy holder is only bound to the insurance contract after receipt, examination and acceptance of the policy.

The prompt delivery and proof of delivery are very important for insurance policies because a delayed delivery creates a danger of a change in insurability from the time the underwriting is completed and the policy is delivered.

A delivery receipt with a health statement that certifies no change in insurability status must be signed by the insured before the permanent policy is in force. If there is a change in the health of the insured and the policy is signed, and the insurer has not been notified of this change, at the time of death the insurance company can legally deny the claim and may only be required to return paid premiums.

At your next annual review meeting with a client, when you may recommend they purchase a life insurance policy for tax or estate planning purposes, it is imperative that your client receive the right advice and be sold the right policy.

It is wise to work with an agent who is experienced and has the proper recognized professional designations. Certified financial planners (CFP) and chartered life underwriters (CLU) are technically competent in the area of life, disability, critical illness, long-term care, medical and dental insurance.

These individuals must continually meet educational, examination, experience and ethical standards. Most importantly working with these types of professionals is the public accountant's best insurance that both his and the client's interests are protected.

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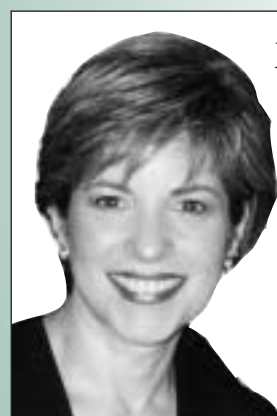
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