



CASE STUDY # 3



Is financial underwriting just eligibility calculation?

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In a global context, whenever we talk about Life Insurance Underwriting, inadvertently the focus is on medical underwriting. In some markets, the aspects of group underwriting or High Net worth underwriting has gained importance. In India, the focus is widespread and encompasses additional aspects like Fraud, Risk Scoring Matrix, Financial Underwriting and Surrogates Analysis. In fact, it is often said that an underwriter spends majority of his or her time in complex financial assessment than traditional medical underwriting. It is also true that with the increase in sum assured the medical grid doesn't change drastically (only few medicals like 2 D Echo, USG Abdomen get added), however the financial grid changes exponentially (array of financial evidence is required to justify high sum cover applied).

In this blog, we turn our focus to a major discussion point in Indian insurance industry i.e. business insurance and corresponding financial underwriting. Traditionally, we have seen 3 kinds of business insurance in this market. Most common form is Keyman Insurance, where a company takes insurance cover to mitigate potential financial loss to business in the event of death of a key person. From a financial underwriting perspective, the focus is more on the company than the individual. The underwriter would be evaluating 3 key aspects:

- Is the company in good financial health and does the mathematics work out in terms of eligibility (5 times of Net Profit or 3 times of Gross Profit)?*
- Is the life to be assured a true keyman for the company?*

- *Is there a legitimate need for cover?*

Another form is Partnership Insurance, where a partnership firm takes insurance cover to fulfil its liability towards a partner if an unfortunate event were to happen to other partner. Again, from financial underwriting perspective, the focus is more on the firm than the individual. A relatively new form of business insurance is Employer Employee Insurance, which is positioned as a unique step to retain the top talent of the company in a tax efficient manner. From a financial underwriting standpoint, an underwriter is required to make sure that life to be assured is an employee of the company and is eligible for cover basis salary drawn from the firm. The company's financials are evaluated from a premium paying capacity perspective.

Our team received an application for keyman insurance on the life of a 24-year-old male. Sum assured applied was Rs 10 Crores, product opted was pure term plan with no return of premium option, benefit term and premium paying term was 36 years. We looked at the company financials and everything looked great. It was a closely held private limited company with last 3 years turnover being Rs 142 Crores, Rs 128 Crores and Rs 102 Crores respectively. Profit Before Tax was Rs 14 Crores, Rs 9.8 Crores and Rs 8.6 Crores. The company was in business for last 3 decades, had good reserves & surplus, limited external borrowing and excellent credit ratings. All the ratios which indicate financial health of the company, like Debt Equity Ratio, Quick Ratio and Acid Test Ratio were favourable. If one would take an average of last 3 years profit and multiple it by 5, cover applied would be easily justified. So, the first question is answered.

Moving on to the next aspect, is life to be assured a true keyman for the company? How do you judge that? In general, position held and responsibilities handled are good indicators, a stake in the company makes the proposition stronger. In this case, life assured was a director in the company holding 4.59% share. So, prima facie, some logical correlation can be made. However, on a deeper dive, we realised majority of shares were held by family members only. Father had 62.67%, Mother had 18.26%, elder brother had 12.34% and a sister concern had 2.14%. Father was the Chairman & Managing Director; Elder brother was also a director. Further, when we looked at the financials of second last year, life assured's name was not mentioned either as a director or as a shareholder. It came through clearly that life to be assured has been inducted in the family business last year only.

We asked for individual financials before making our final decision and a consistent picture was portrayed. Individual returns were made available for last year, gross total income was Rs 10 Lakhs with Rs 6 Lakhs drawn as a salary from the proposing company and rest was income from other sources. When we insisted on further 2 year's financials, the response was individual returns have been filled for one year only. It was concluded that though the company is eligible for cover applied, life to be assured is surely not a keyman for the company and hence no cover can be offered to him.

So, financial underwriting is not just eligibility calculation, it requires a lot of judgement & understanding. **INCHES** underwriting team has been trained extensively to evaluate such complex cases. We do more than 10,000 transactions a month with due adherence to quality standards. We are adoptable to your needs and geared up to do large volumes.

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