Surviving critical illness financially

WOO SIEW CHIN looks at what you need to know about critical illness insurance

Do you need critical illness insurance? Ask yourself the following question: If you were struck by a critical illness, would you have enough money to cover lost income and pay for medication not covered by a traditional health plan and other related rehabilitation costs?

Basically, critical illness insurance covers the financial gaps when you are diagnosed with a major illness such as cancer or when you need a heart transplant. Critical illness policies usually cover 36 types of dread diseases based on a standard definition set by the Life Insurance Association of Malaysia (LIAM). The coverage will provide a monetary benefit (lump sum or periodic) in the event that the policyholder has any of the defined critical diseases.

With insurance, the irony is that you purchase it not knowing if you will need it in the future. Perhaps a more pertinent question to ask then is "Who needs a critical illness policy the most?"

Do you need it?

According to Teh Loo Hai, executive vice-president and head of customer management for Great Eastern Life Assurance (Malaysia) Bhd, it is highly probable that every person would suffer some form of critical illness at one point or other.

Insurance adviser Teng Luen Foong agrees. "Though they have lower risks, children should also have critical illness policies mainly because of the low level of premium at their entry insurable age."

Plus, children's medical bills are just as high as that of an adult's. "A bone marrow transplant alone can cost up to RM100,000 if done in Malaysia and up to RM250,000 overseas," says Laurence Lim, chief operating officer, life division, of Hong Leong Assurance Bhd.

The general high cost of healthcare is another important factor.

"Critical illness insurance policies are necessary because of the general high cost of healthcare, especially the high recuperation cost, as well as the general inadequate coverage by hospital and surgical or medical policies," says Teng. With the latter, the maximum payout per illness is usually far below the cost of critical illness expenses.

"Critical illness policies are important as the payout can act as a replacement of lost income in the event of the policyholder's inability to work, especially during the recuperation period," says Teng.

It has often been said that with current advanced medical technology, people are expected to live longer. Thus, to sustain oneself and pay for medical expenses, a critical illness cover is necessary, says Lim.

"Many people are now surviving the ravages of a dreaded disease, but in the process of seeking treatment, the cost leaves them financially ruined," he says.

This would be a double blow to the family and dependants: Not only is the breadwinner unable to earn an income for the family, his illness and medical needs become a burden, he adds.

It was this need for financial support that led to the development of dread disease or critical illness insurance products.

Great Eastern's Teh believes that the average Malaysian who is diagnosed with a critical illness is likely to suffer a substantial financial setback.

Lim Yan Chang, director of Standard Financial Planner Sdn Bhd, believes that even the well-to-do might face financial problems if they were saddled with medical and recuperation costs of more than RM100,000. "They might not have enough liquid assets and end up selling their stocks or property."

What is available

According to Teng, there are basically two types of critical illness policies. "One is a stand-alone basic policy, issued by general insurance companies, and the other is attached to a life policy."

According to Lim of Standard Financial Planner, coverage for critical illness is available in a basic life policy that includes critical illness and disability. "When the policyholder either dies, become permanently disabled or suffers from critical illness, the policy will pay and the contract is performed."

Critical illness coverage can also be obtained through several types of riders, some of which may affect the basic sum assured of the life policy.

Take a person with RM50,000 life cover in the basic policy and RM50,000 critical illness rider.

The planners say a standard rider typically pays in the event of critical illness without reducing the basic sum insured, thus a person who makes a claim for RM50,000 upon diagnosis of critical illness will leave the RM50,000 death benefit untouched.

Then, there is what is commonly termed as accerelated benefits. According to Teng, a basic life policy is normally only payable upon death or maturity of the policy, but a critical illness accelerated rider can trigger a full payout if the policyholder is diagnosed with a critical illness. In the earlier example, a claim upon critical illness would accelerate the payout for the benefits of the RM50,000 basic policy, and the contract will end.

Teh: A good starting point of coverage would be RM50,000

Yan Chang: Even the well-to-do might face financial problems

"Insurance companies may have their own names for the different types of critical illness riders, so policyholders need to look at the terms and conditions for their respective benefits," adds Teng.

However, the amount of add-on riders is subject to financial underwriting, says Teh.

"For example, some people may already know they have cancer or belong to a high-risk group, so they want more coverage. The coverage may be much more than the actual financial loss incurred," Teh explains. Coverage that is more than the actual financial loss or economic life value is unjustifiable and is therefore considered a form of abuse.

So, given the many types of critical illness cover available, which is better? It is a matter of individual needs and choice, and the overall benefits and premiums.

"For instance, some standard riders and stand-alone policies may only cover up to age 60, 65 or 70, while some critical illness accelerated riders may provide cover for the duration of the basic life policy, which can be up to 100 years," Teng says. "Also, different insurance companies would have different variations of the riders."

However, a good gauge is looking

at the three main influencing factors — duration of the critical illness cover, the kind of premium (whether it is level or increasing), and the benefits offered.

If you are looking for a mixture of coverage and investment, you could opt for investment-linked policies that offer critical illness coverage as well. However, you would need to understand the risks involved with investment-linked products.

Critical illness policies either have guaranteed or non-guaranteed premium rates. According to Great Eastern's Teh, non-guaranteed rates are generally lower than guaranteed rates but the former may be adjusted in future.

In end-2003, K H Chia, then president of LIAM, said more products would be designed with non-guaranteed premium rates because almost all reinsurers worldwide had stopped providing guaranteed premium terms.

"A policy with non-guaranteed premium rates means that an insurer may revise the premium rate of that entire block of policies if the claims experience is adverse," he clarified in a statement.

Apparently, the trend of selling insurance products with non-guaranteed premium rates is going worldwide. "Countries such as the UK, Japan, New Zealand, South Africa, Australia and Hong Kong are offering non-guaranteed premium rates, as are Canada and Singapore," says Teh.

In Taiwan, guaranteed premiums are given for short periods such as five years and below, he adds.

How to choose?

As with most things, it is crucial to study and compare the different products available before making a decision. Look at the terms and conditions. Consumers should read and understand the contractual terms and note the duration of coverage. "Policies with favourable contractual terms have a shorter waiting period before the coverage takes effect," says Teng. This waiting period differs from one insurance company to another and could range from 60 to 90 days. Policies with guaranteed renewability would ease the mind of policyholders. Such information would be available in the policy clauses.

Laurence: Sum assured should be two to four times your annual income

Find out if the policy provides coverage increases. "There are policies in the market that increase coverage over time while maintaining premium rates," says Teng.

You would be able to see your money grow over time without paying extra for it because such products have a deferred term built into the policies, says Yan Chang of Standard Financial Planner.

Have an old critical illness policy?

WHEN CRITICAL ILLNESS policies were introduced locally in the late 1980s, they covered less than 10 types of critical illnesses. However, competition in the insurance industry has pushed the number of critical illnesses up to the current 36. Competition has also resulted in the lengthening of coverage duration, while definitions of the critical illnesses covered have also changed through the course of time. About three years ago, the Life Insurance Association of Malaysia standardised the definition of critical illnesses, which is now stated in every policy document.

Should consumers replace critical illness policies bought before the changes were made? If one just considers the number of critical illnesses stated in the policy, the newer policies would appear to have better coverage. But that might not be the case. The definitions of the illnesses 10 years ago might be more liberal than the current one. Of course, the converse could be true. "Definitions varied from one insurance company to another before the standardisation," says Teng Luen Foong, an insurance adviser with 25 years of experience.

Thus, consumers should study and compare their old policies with current ones. "Consumers must understand the types of critical illnesses covered, the definition of each type of critical illness, and the duration of the cover," says Teng.

Teh Loo Hai, executive vice-president, head customer management for Great Eastern Life Assurance (Malaysia) Bhd, agrees. "One should examine the coverage of the existing policy to see if it still meets one's needs before replacing or buying an additional policy or increasing one's critical disease policy coverage amount," he says.

Consumers should also carefully evaluate the financial loss they may suffer, as each time they surrender their policy, they may get back less than what they had paid in the past, he adds.

It is therefore advisable for those with "older" policies to seek advice from their insurance advisers before making any decisions. ■

Teng: Have surgical and hospitalisation insurance as well

GLOSSARY

RIDER: Supplementary contract (usually for accident, medical and disability coverage) attached to the basic policy or plan

GUARANTEED RENEWABILITY: A contract that the insured has the right to continue in force by the timely payment of premiums for a substantial period of time as set forth in the contract. During that period of time, the insurer has no right to make any change in any provision of the contract other than a change in the premium rate for all insured in the same class.

DEFERRED TERM: A term cover that is guaranteed to increase slowly

CRITICAL ILLNESS ACCELERATED RIDER: A supplementary contract whereby the sum assured is paid out from the sum assured of the basic life policy in the event of diagnosis of a critical illness

TOTAL PERMANENT DISABILITY RIDER: A supplementary contract whereby the sum assured is paid out from the sum assured of the basic life policy in the event of total permanent disability (dismemberment of two limbs, irrecoverable loss of sight of both eyes, and so on)

STAND-ALONE CRITICAL ILLNESS POLICY: Critical illness plan issued by general insurance companies

or not the premiums are guaranteed.

"It is easier to make allocations with guaranteed premiums when you do your financial planning," says Yan Chang, while Teng feels that it is fairer to the consumers to have guaranteed premiums for critical illness policies.

If you are considering investment-linked products with critical illness coverage, do bear in mind that they are more suitable for those familiar with investment risks, says Teh, adding that consumers should consult their insurance advisers first.

With investment-linked policies, policyholders may also need to top up their premiums if the investments do not perform as expected.

"If a critical illness rider is attached to an investment-linked policy, the policy can terminate if the investment returns cannot be sustained," says Yan Chang. Because of the non-guaranteed nature of investment-linked insurance products, the policy may lapse if the investments do not perform as expected, he adds.

For those who are afraid that they might lose their coverage in such a situation, Teh advises them to opt for a high premium and low coverage.

However, investment-linked products offer more flexibility. "Policyholders have the option to increase or decrease the sum assured with or without altering the premium payable or increase and decrease the premium payable with or without altering the sum assured," he says.

How much coverage?

Another important factor to consider is the amount of coverage. The policy should cover all medical-related costs if possible, especially the cost of the primary treatment.

"A good starting point of coverage would be RM50,000. Treatment for cancer would cost RM50,000 to RM100,000, depending on the complexity," says Teh. Stroke treatment, for example, would cost RM20,000 to RM50,000, depending on the complexity of the condition.

Other costs incurred would include rehabilitation cost, he says. Also, consider if you have other sources of income and explore your options with an insurance adviser or financial planner on the appropriate amount of coverage, Teh adds.

However, Teng believes that the coverage should also be dependent on one's finances. For example, if you are the sole bread-winner in the family, you would need to calculate the replacement of income lost for the family's needs, he explains

He advises consumers to have higher critical illness coverage compared with life insurance coverage because of the recuperation and healthcare costs involved. "The average person should purchase a policy that gives between RM100,000 and RM300,000 worth of cover."

"As a rule of thumb, your sum assured should be two to four times your annual income," says Laurence of Hong Leong Assurance. Insurance companies normally do not insure more than that and will certainly not insure more than RM1 million per life, he adds. Therefore, for coverage of more than RM1 million, you may need to make additional purchases from other insurance companies. Other than a critical illness policy, one should also have surgical and hospitalisation insurance, says Teng. "It is better to have both, especially if you prefer to go for treatment at private hospitals." He notes that at such hospitals, you need to pay a relatively high deposit upon admittance. ■