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PIS Talking Risk

Pitfalls of commoditising life insurance

Life insurance application forms stacked beside lolly shelves at supermarket checkouts are becoming a common sight in the UK. Tesco supermarkets now promote their own brand of life insurance, with in-store flyers encouraging the consumer to go online and apply. Tesco aren't alone either, other mega brands are tapping into the insurance industry in other countries too. Baby food brand Gerber recently sold $30 billion worth of life insurance policies in an online campaign in the U.S.

Whether or not these particular brands eventually target the Australian insurance market, it is evident the insurance industry is evolving and the way advisers do life business is being challenged.

There is now an increasing amount of 'do it yourself' (DIY) insurance consumers who are perhaps unaware of what professional advice can bring to the table. A recent ING study showed that, for those who reject financial advice, lack of a perceived need for this advice (23%) is a sizable barrier.[1]

This lack of need for advice has roots in the internet. Why pay an adviser to find the right product when you can quickly do an internet search on insurance products and apply online?

Yet this is precisely where the need for advice lies. The product itself can only do so much. The real value of advice for insurance consumers is unlikely to become apparent until a claim needs to be paid.

According to ING's National Sales Manager for Life Risk, Paul Jones, "All insurance companies these days advertise the fact that they pay 100% genuine claims, as we would expect. However, if the product is bought with no advice, you can't guarantee the outcome, i.e. that the expected amount will go to the right person, in a timely manner and with the right tax treatment. Only with advice can this be achieved."

When insurance is bought without advice, certain important considerations may not be taken into account and may have an effect when a claim is made. For example, the consumer may not be aware of the tax consequences of leaving superannuation benefits to non-dependants. Advice can highlight the seemingly simple issues that can become potential minefields down the track, such as who should own the policy, who should pay the premiums and who should be a beneficiary.

Given a third of all marriages fail, these decisions should not be skimmed over.[2]

Providing advisers with the tools to compete with the apparent ease and speed of 'click, click, you're covered' insurance is vital to prevent business going out the door and onto the internet. This is where innovation and flexibility with service, products and delivery can prove its worth. For example, pre-populated forms like ING's OneCare Express dynamic application form can help speed up the process for the consumer.

The important thing is to forget about what we're selling and think about what the consumer is buying. If the consumer wants quick and easy, we give it to them. If the industry is evolving, we must evolve with it.

Upcoming events

AFA QLD GenXt Christmas Party
Date: Friday 28th November 2008.
Time: From 5pm.
Venue: "THE BOO" Borrodobin Bowls Club, 126 Breakfast Creek Road, Newstead QLD.

AFA Toowoomba Chapter Lunch
Date: Tuesday 16th December 2008.
Time: 12 - 4pm.
Venue: Downs Club, 16 Mylne Street, Toowoomba QLD 4350.

AFA Brisbane Chapter Christmas Lunch
Date: Thursday 18th December 2008.
Time: From 12pm.
Venue: Victoria Park, Golf Complex, Herston Road, Herston QLD 4006

While consumer choice is vital for any industry, it is important the consumer realises the potential pitfalls of DIY insurance. Commoditising the insurance industry, an industry that is there to create certainty, takes a considerable amount of that certainty away.

[1] ING commissioned Neilsen research, August 2008

[2] Australian social trends 2007, Australian Bureau of Statistics

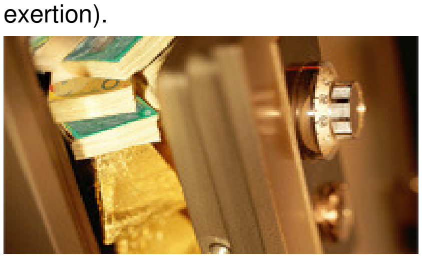
Source: ING Australia Ltd

Income protection without fears

Verifying your clients' income at application time for income protection policies will ensure there are no unpleasant surprises when a claim is lodged.

Unless the required financials are submitted upfront and the policy is endorsed as such, insurers reserve the right to request a client's financials when an income protection claim is lodged. Why? To substantiate that the level of cover applied for was appropriate at the time.

Needless to say, what should be a relatively routine step in the claims process can lead to devastating consequences if the client has overstated their income at the outset, whether consciously or by accident (i.e. misunderstanding what constitutes earnings from personal exertion).



What agreed value and indemnity policies have in common

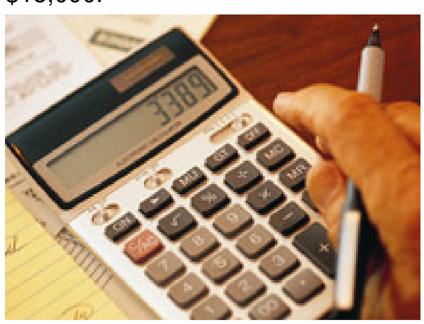
'Agreed value' policies are just that, so long as your client can prove (if need be) that they were actually earning the income at the time that they nominated the amount on their application.

The same goes for 'indemnity' policies, contrary to the commonplace misconception that indemnity policies have less disclosure requirements than agreed value policies.

Even though indemnity policies will be reassessed 'income-wise' at the time of claim, the insured must still comply with the duty of disclosure at the time of application (i.e. not state in the application the income that is expected to be earned, but an actual income that has been earned).

Indemnity - past income is important

Let's say your client discloses that he or she is earning $50,000 per year on their application. The policy goes into force for this amount because the insurer relies on the disclosure by the client. The following year, the client lodges a claim and is asked to supply financials. Upon receipt of the financials, the client's actual income for that year turns out to be only $15,000.



Unfortunately, what happens next is not good news for the client. To begin with, most insurers have a minimum income level required to obtain cover. For example, an insurer might only offer cover to clients with an income of $24,000 or more, i.e. minimum cover level of $1,500 per month. So there is the potential in this situation for the policy to be cancelled and premiums refunded (plus the commission if the policy has been in force for less than 12 months). The client has not met the minimum requirements and is then left without cover and without a claim.

Safeguards advisers can take

While the onus is ultimately on the client to provide accurate information to comply with their duty of disclosure, here are some safeguards advisers can take to ensure the information on the application can be supported down the track.

- Encourage your client to provide their financials wherever possible when applying for the policy, even if the sum insured applied for is under the limit where financials are required.
- Bear in mind that when deriving income figures, drawings, distributions or dividends are not usually regarded as insurable income. Could it be, perhaps, that the majority of your client's income is drawings? If so, this is not insurable income. Focus on income that is actually generated by the insured and will therefore be impacted upon claim.
- As a general rule of thumb, income as declared to the Australian Taxation Office (ATO) should marry up to what's on the policy.
- Projected earnings are not insurable, only actual earnings.

The bottom line

When a client nominates an inflated amount of income when applying for cover, this is treated as a misrepresentation, irrespective of whether the policy is agreed value or indemnity. So if you're in any doubt about a potential client's income, clarify the details before the policy goes into force to avoid any problems at claims time.

Source: Zurich Financial Services Australia