



# LIWMPC Life Insurance Industry Update

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*This presentation has been prepared for the Actuaries Institute 2014 Financial Services Forum.  
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## Agenda

- Current life insurance environment
- Issues facing life insurance and wealth management industries
  - Financial Systems Inquiry submission
  - Lapse rates, group risk and income protection claims
  - Superannuation regulation
- The next steps for the industry....



Jim Minto - CEO TAL –  
“It is hard to know if [the market] has bottomed out or not. That is the enormous risk we all face.”

(October 2013)

Craig Dunn - CEO AMP –  
“The Australian insurance industry is suffering poor lapse rates and claims experience across the board, with *industry lapse rates at a 10-year high.*” (June 2013)

AFR article– “Hostplus, which caters to employees in the hospitality sector, *raised its premiums by 85 per cent*, while *premiums at State Super in NSW increased by 60 per cent.*”

(March 2014)

## A turbulent environment....

Kelly Power - Head of Platform Product BT -

“I think the level of discretionary investment outside of regulatory change has dropped... focusing on *implementing regulations is a significant cost for us* [as an industry].”

(April 2014)

Money Management article – “*Lapse rates plaguing AMP’s life insurance business* will likely get worse before they get better, the company’s CEO has said. “  
(February 2014)

Financial Standard Online – “Life insurer AIA Australia has launched a paper exploring ways of getting employees suffering from mental illness back into work, after a *spike in total and permanent disability (TPD) claims* has put serious pressure on the life insurance industry.”

(August 2013)



## A turbulent environment....

- The current uncertainty in the life insurance market has created a period of turbulence rarely seen in Australian life insurance.
- The last 12 – 24 months has seen:
  - Increased lapse rates, leading to large experience losses reported by insurers
  - Large claim losses reported by group risk schemes, accompanied by large premium rate increases across the market
  - Governmental review into financial systems (Financial Systems Inquiry)
  - Deterioration in income protection claims experience, leading to large claim losses accompanied by premium rate increases
  - Regulatory reform, regulatory reform and more regulatory reform
- Management focus on compliance has impacted product innovation
- There is significant pressure on life insurance margins and profitability, causing insurers to move to address these issues, and take advantage of emerging opportunities.



# Changing demographics

- By 2050, nearly 25% of our population will be 65+ (more than U/18s).
- ... and expected to live to 90+ (!)
- Ratio of '65+ : Working Age Pop.' - currently over a 1:4 - by 2050, less than 1:3.
- 85s+ population is expected to treble.
- 60% of the \$1.7 trillion in superannuation assets held by 50+
- Who is funding whose retirement? What about aged care?
- How quickly is the retirement age heading upwards?
- Sacred cows?



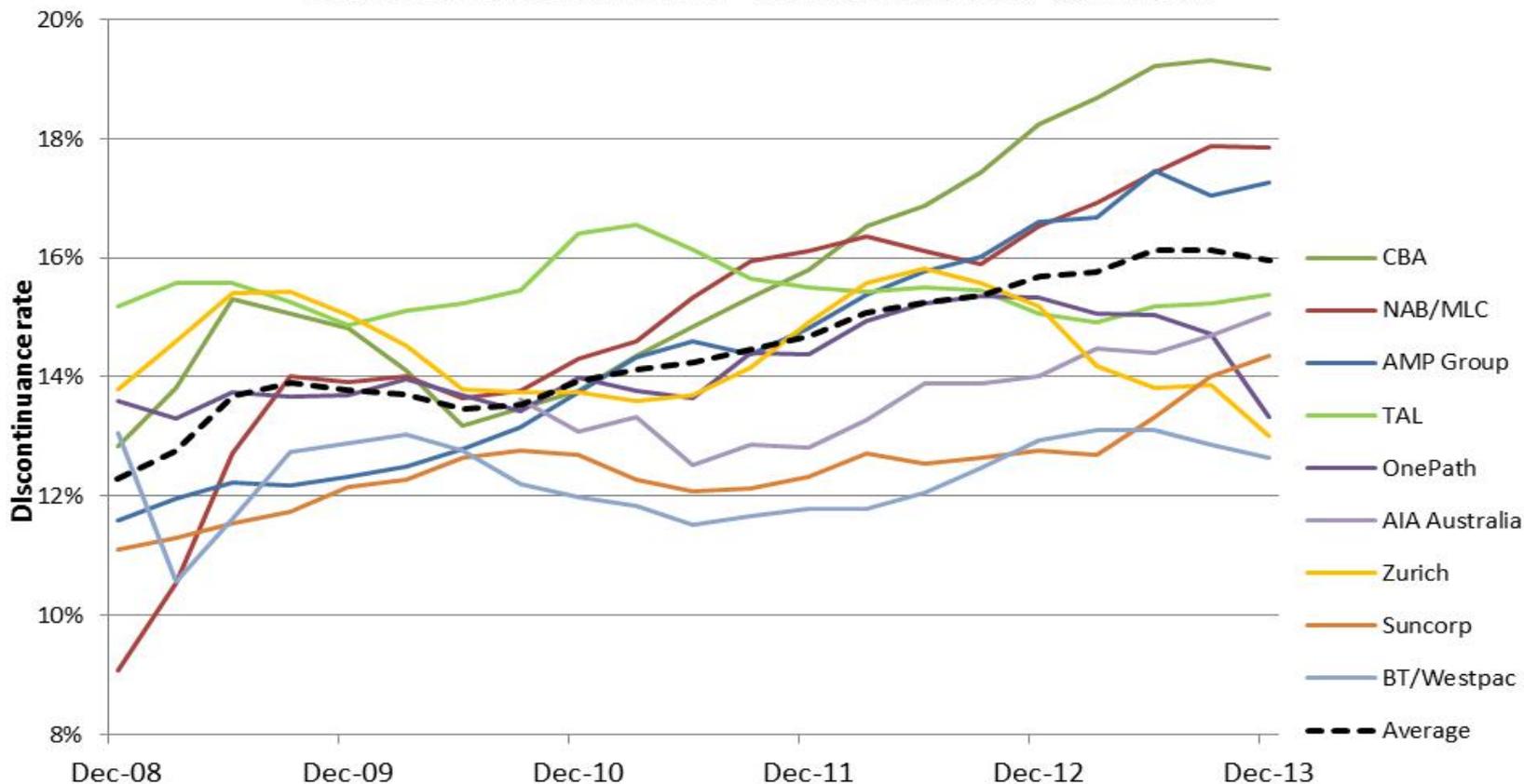
## Financial Systems Inquiry – Actuaries Institute

- Largest inquiry into the Australian Financial System since Wallis (1997)
- AI submission focused on our expertise and made 3 major recommendations:
  - Deal with demographic change with a comprehensive framework for policy formulation to manage all issues relating to sustainable financing of our aging population
  - Establish a Financial System Policy Commission (FSPC) with a longer-term focus
  - Create an open data regime to allow increased analysis of government data
- It is expected that the FSI will deliver its report to the Federal Treasurer in November 2014.
- The outcome of the FSI is likely to have a significant influence on the financial services industry for some time.



# Lapse experience

## Discontinuance rates - individual risk business





## Lapse experience (continued)

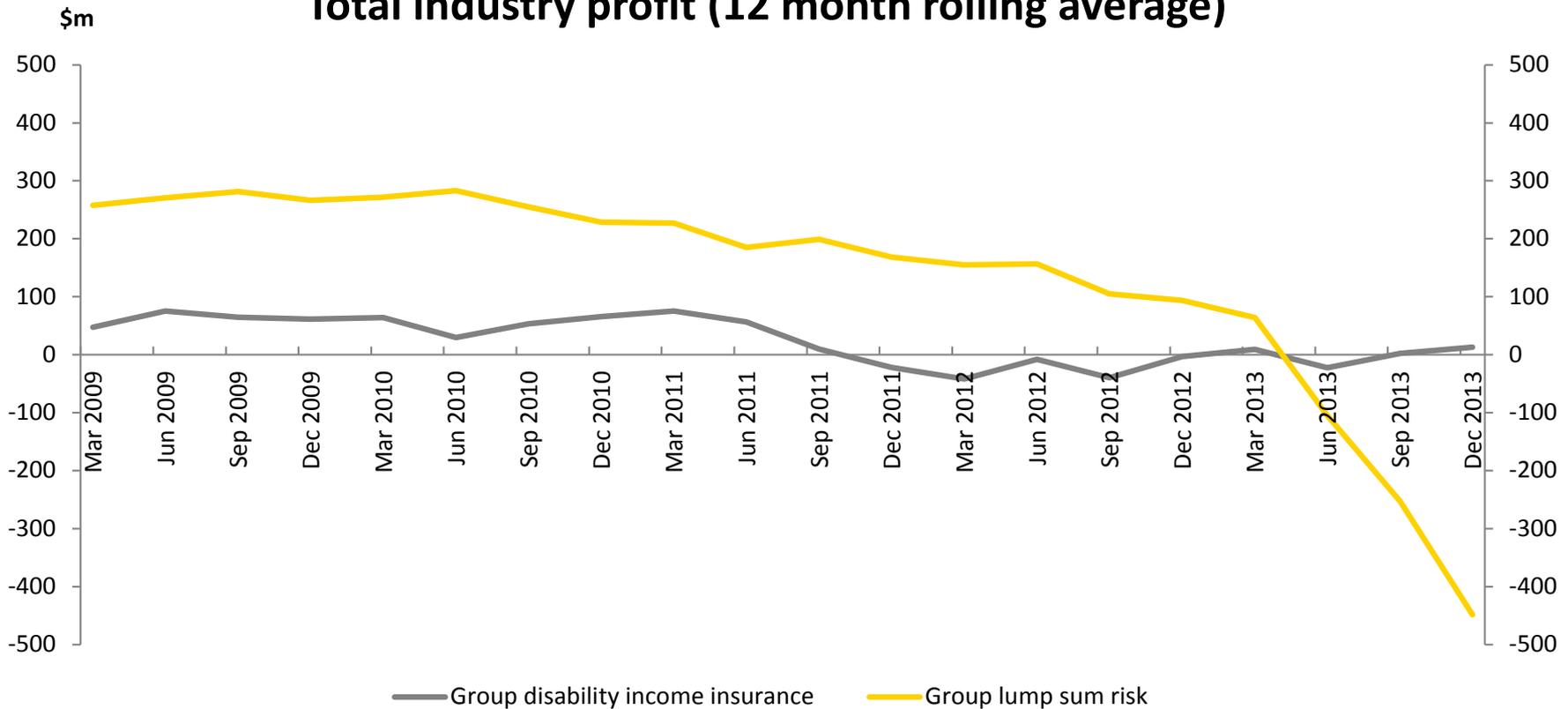
- While it is difficult to determine the total amount of losses incurred across the industry, it is clear from the observed data that experience has deteriorated markedly.
- Factors contributing to the deterioration in experience include:
  - Affordability
  - Uncertainty
  - Churning
  - Product design
- FoFA reforms continue to add uncertainty to the selling of life insurance business, and insurers are considering what impacts from the reforms will be felt on lapses.

AFR - **“Some of Australia’s biggest insurers, including AMP and CommInsure, are recording *increasingly high lapse rates in an alarming trend* that could progressively bleed companies’ bottom lines.”** (March 2013)



## Group risk profitability

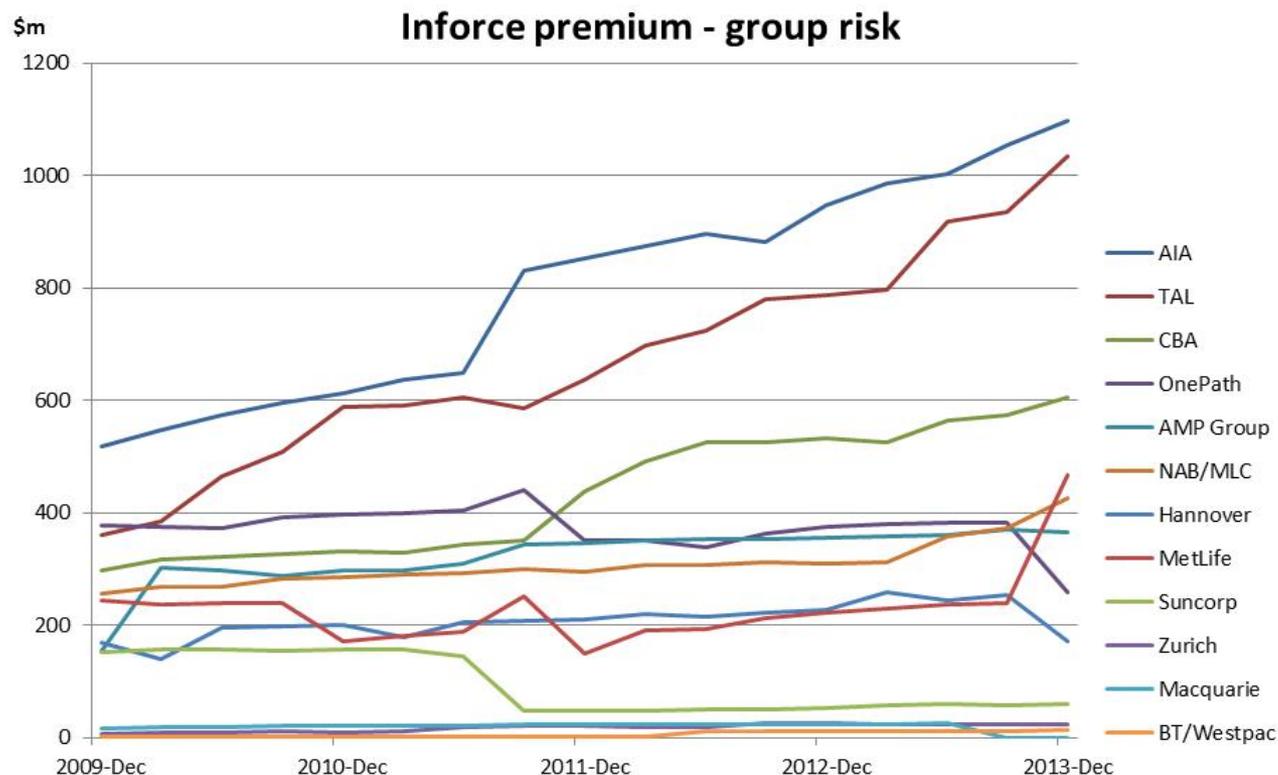
Total industry profit (12 month rolling average)





# Group risk pricing

Recent repricing of group risk schemes (particularly in relation to large industry funds) has seen significant premium rate increases.



InvestorDaily – **“Group insurance premiums for not-for-profit superannuation funds have risen between 30 and 50 per cent in the last year – and further increases could be on the way.”**  
(August 2013)



## Group risk challenges (continued)

- What is driving the deterioration?
  - Relaxing of product definitions and policy terms
  - Improvements and increases in benefits
  - Legal involvement driving increased awareness of benefits available to customers
- Joint working groups from the LIWMPC and the GIPC have been formed to increase understanding of legal involvement in lump sum claims, drawing on past experience from public liability insurers. Ideally, this research will yield some useful strategies for actuaries to assist insurers in managing this effect.
- Other working groups are investigating IBNR reserving techniques and, drawing on the deep understanding of long tailed claims in general insurance, looking to provide some guidance on reserving for this type of business.

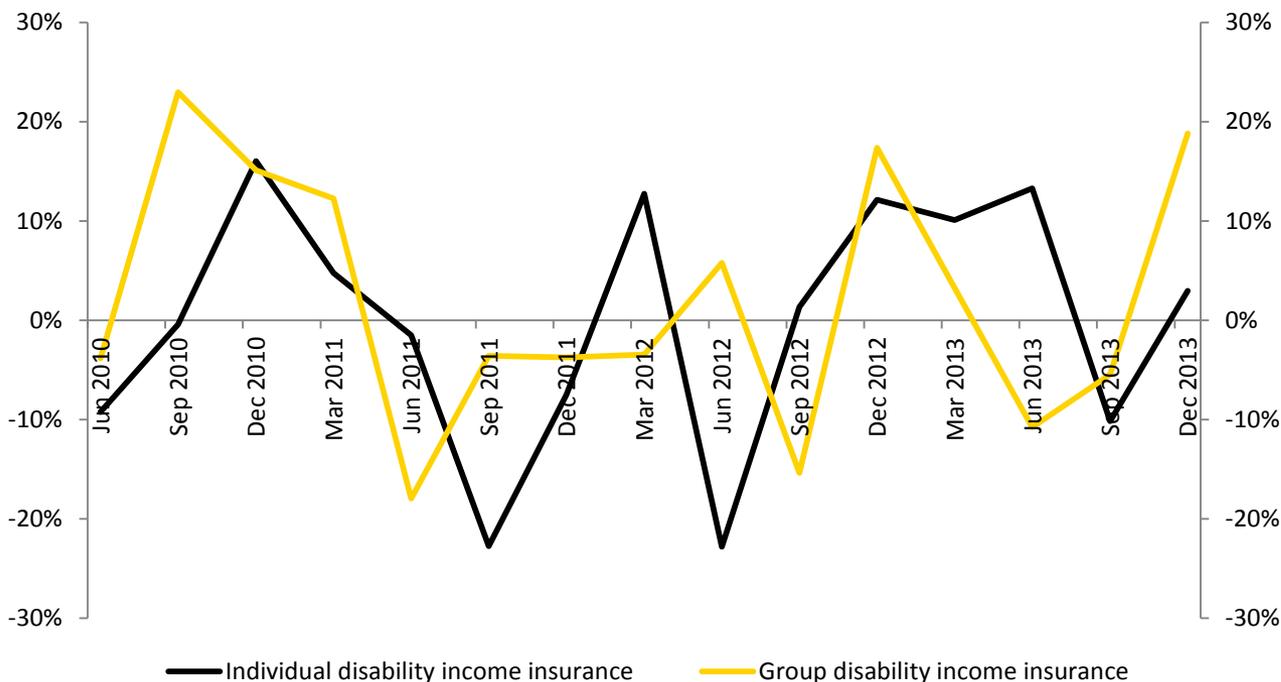


"Unfortunately Mr. Brown, there's nothing in your policy that covers taking the bull by the horns."



# Income protection claims

## Profit/Premium



Canberra Times - "Jim Minto [MD, TAL] said the September-half results were dragged down by higher than expected claims, including claims dating back a decade and shepherded by lawyers, rather than people giving up their policies. "The trends are quite remarkable," he said, pointing to *more mental health claims* over the past few years as the economy has weakened." (November 2013)



## Income protection claims (continued)

- The average net profit after tax as a proportion of annual premium has been in decline since 2008.
- Some of the potential driving factors behind increased claims are:
  - Increased incidence of mental illness claims
  - Economic impact
- There are a number of initiatives in place to better understand deteriorating experience.

TAL results article – “**The *life insurance industry continues to suffer strong headwinds* and TAL certainly saw higher claims levels flowing through in disability lines especially**” (May 2013)



## Stronger Super

- Government reforms aiming to strengthen and improve the integrity of the Superannuation system with an aim to maximise retirement income for members.
- Key aspects:
  - MySuper
  - SuperStream
  - Governance
  - Self Managed Super Funds
- Compliance aspects
- Product development opportunities?

Graeme Russell - CEO (&CIO) Media Super –  
**“We are a small fund with limited resources and I have had to reshuffle the pack. We are all wearing a lot of additional costs through Stronger Super and product development.”**  
(March 2014)





# FOFA – Future of Financial Advice

- Complex and wide ranging reforms as part of the GFC aftermath
- Can be distilled into three big obligations
  - Ongoing advice and fee disclosures (increase transparency / boost engagement)
  - Conflicted remuneration (align interests of advisers and clients)
  - Best interests (increase trust, professionalism, strengthens relationships)
- Compliance challenges
- Opportunities in product offerings, productivity & client relationships
- Timeframes and special interest groups? How unscathed will it remain?

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INVESTMENTS AND  
FINANCIAL SERVICES



“The good news is, nobody will ever hate you for being rich.”



## FATCA – Foreign Account Tax Compliance Act

- US law designed to counter offshore tax avoidance by US persons.
- Part Five of the HIRE Act, signed into law on 18 March 2010:
  - Hiring Incentives to Restore Employment Act also included:
    - Incentives for Hiring and Retaining Unemployed Workers
    - Expensing (Increasing expensing of depreciable business assets)
    - Qualified tax credit bonds
    - Extension of Current Surface Transportation Programs (Highway and public transport administration)
- Hardly any US customers? Why would FATCA matter?
- Don't directly invest in US securities?
- What about insurers and other non-ADIs? What is the scope of FATCA?
- **Your business suddenly becomes less attractive to do business with.**



## FATCA – Foreign Account Tax Compliance Act

- Final regulations came out in January 2013, with implementation date of ~~1 July 2013, 1 January 2014, 1 July 2014?~~ **But wait... breaking news!**

FSC - "Treasury has worked closely with the US government to get this IGA signed"

"It is significant for the financial services industry in reducing red tape and will **save hundreds of millions of dollars in compliance costs.**" – John Brogden (April 2014)

**InvestorDaily** - "Everyone working in the financial services industry needs to be aware of FATCA and exactly what their compliance requirements are,"

**"Non-compliance could have a significant impact on returns."** – Suzanne Gibson (April 2014)

- Who is next?



## Where to next....

- Findings of the FSI to influence decision makers regarding the long term future of financial services
  - Co-ordination of regulation
  - Removal of barriers to innovation
- Risk product development
  - Flexible product design
  - Claims management practices
  - Advisor remuneration models
  - Greater data transparency
  - Importance of insurance within superannuation
- Investment and retirement product development
  - Changing demographic profile
  - Retirement income needs
  - Client engagement & SMSF
  - Investment offerings & costs

