

## Perspectives of the Life Insurer

### Topics:

- Hardening of Life Insurance in Australia
- Developments in Case Law
- Stronger Super and Prudential Standards

# 2014: Superannuation. Beyond the Fringe

## A challenging time for the life risk industry!

- TAL news article – “There is plenty of evidence of insurers and reinsurers suffering considerable losses from this [higher claims costs] and it is a reality that wholesale insurance prices were simply too low in the past.” (Dec 2012)
- CBA 31 December 2012 profit announcement – “Wholesale Life revenue declined due to a rise in claims.” (Feb 2013)
- CBA 30 June 2013 profit announcement – “while claims experience improved overall, Wholesale Life net revenue declined significantly due to unfavorable claims experience and claims reserve increases (particularly in the second half of the year)”. (August 2013)
- Dai-ichi Life (TAL) June quarter profit announcement – “ordinary profit and net income decreased significantly, affected by .....and increased claims as a result of deterioration of the Australian economy.” .....”TAL significantly increased its group insurance ANP from AUD 27 million to AUD 121 million, predominantly because TAL revised its group policy terms, including premium rates, in its Group insurance business. (August 2013)

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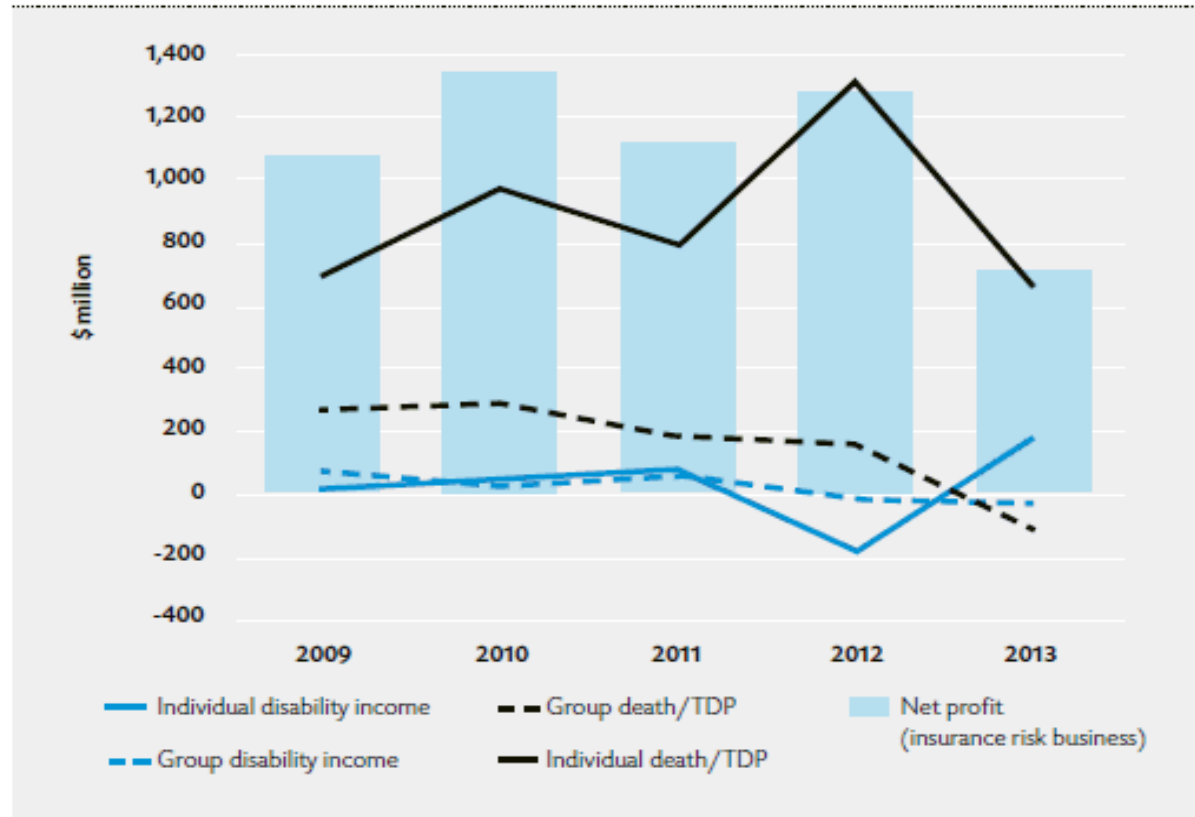
The Australian Life Risk group market is the largest group market in Asia, led by life and disability benefits issued to superannuation funds.

Premium levels have hovered around 4 to 5% of superannuation contributions. But the market has been experiencing a significant deterioration in claims experience, particularly in the Industry Funds segment.

From 2011, Industry Fund claims began to move up and spiked in late 2012 and into 2013. As rate guarantees work their way out significant increases in premium have been advised on group risk business.

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## Life insurers – Net profit by major insurance risk product groups (12 months ending 30 June)



Source: Life Insurance Quarterly Performance publication, APRA

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## Causes of increase in claims and premium

- Increased stress in the general populace from corporate downsizing/ weaker economy
- increased mental health problems in the community.
- Benefits and claims definitions have been regularly improved.
- Changes went through without appropriate adjustments to prices; in fact, prices were seen to regularly reduce!
- Consumer awareness of the availability of substantial insurance benefits offered by superannuation funds without evidence of health= anti selection especially via financial adviser and due to heavy advertising.

(per *Life Insurance Overview*, Insights Issue 3, 2013)

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## Policy terms and conditions contributing to increases in claims and premium

- At same time underwriting rules, such as automatic acceptance limits and eligibility terms, were regularly relaxed.
- Higher benefit limits which increase the incentive to not return to work.
- Especially for TPD where the large sums insured are where Australia stands out globally. The TPD benefit levels in most other countries are a few thousand dollars or limited income streams and not the \$1M+ you can see in Australia.
- Definitions are subjective, especially TPD, and result in winner vs loser mentality.
- The courts have also generously interpreted policy terms.

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## NSW Workers compensation reforms also a major indirect contributor

2012 \$4.1 B deficit in the NSW Workers Compensation Scheme. Employers facing a 28% increase in premiums in NSW.

Amendments to the scheme rushed through parliament and passed 27 June 2012:

- 5 year cap on entitlements;
- access to benefits restricted by reference to severity of injury;
- no costs;
- administrative reviews only of weekly payments;
- removal of entitlement for payments for “pain and suffering”.

### Result

Aggressive legal activity, including advertising by lawyers, whose practices had previously relied on workers compensation, to review Life Insurance claims and potential claims.

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## Was the tide changing before Stronger Super?

### Manglicmot v Commonwealth Bank Officers Superannuation Corporation Pty Ltd [2011] NSWCA 204

- Bank teller commenced working part time after injury.
- Common form TPD definition:  
*... in our opinion being incapacitated to such an extent as to render the Insured Person unable ever to engage in or work for reward in any occupation or work which he or she is reasonably capable of performing by reason of education, training or experience*
- **Held:** being TPD under the common form TPD definition means being totally disabled from work which the member is reasonably capable of performing by reason of education, training or experience. The trustee and insurer do not have to read “work” as being full time work under this definition.
- Also, the Trustee should ensure that the definition reflects the bargain it struck.
- When changing insurance arrangements, in discharging its duties, the trustee must have a robust due diligence processes including gap analysis.



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## ***Hannover Life Re of Australasia Ltd v Dargan [2013] NSWCA 57***

*“common form “ of TPD definition: is unlikely ever to be able to engage in any Regular Remuneration Work for which the Insured Person is reasonably fitted by education, training or experience.”*

Part time taxi driver but needed to obtain ancillary certification or set training.

**Held:** that the need to obtain a licence and as a condition of maintaining it undertake a limited qualifying course would not preclude a person from being reasonably fitted for a particular occupation. Otherwise the word “reasonably” in the common form definition did no work.

Affirmed *Maglicmot*

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## Issues with Claims Review Committees

Broader use of contractual internal and external dispute resolution methods which lack transparency, amenability to submissions and access to the courts.

Are they bound by law anyway?

In many cases, these CRCs are binding on the insurer, although not on the insured.

Usually done on the papers with no ability for reasonable (usually nil) interrogation of the claimant.

If a binding decision is it via simple majority, chair decides or unanimous?

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## Reinsurance pressure

In reaction to claims experience, several reinsurers have pulled back from the Australian market.

As capital capacity is constrained in the direct writers, prices are rising quickly (particularly for Industry Funds) and it is difficult to get more than one or two carriers to quote in many cases.

RGA profit announcement – “\$184 million after-tax charge due to increased claims liabilities in Australia. ... we are suspending all quoting activity in the Australian group total and permanent disability market indefinitely and will continue to be extremely selective in other aspects of that group market until it stabilizes and the products become more sustainable”. (Jul 2013)

Swiss Re profit announcement – increased Group Risk reserves by 82m USD. (August 2013), and an additional \$121 million in Q3.

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## Stronger Super- what has changed for insurance benefits?

Post 1 July 2014 members- standardisation of insurance benefits.

SIS REG 4.07DA trustee of a regulated superannuation fund must not provide an insured benefit in relation to a member of the fund unless the insured event is consistent with a condition of release.

Relevantly:

Death (Schedule 1, Item 102);  
Terminal Medical Condition (Item 102A);  
Permanent Incapacity (Item 103); or  
Temporary Incapacity (Item 109).

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## Terminal medical condition (reg 1.06A)

If the following circumstances exist:

- (a) two registered medical practitioners have certified, jointly or separately, that the person suffers from an illness, or has incurred an injury, that is likely to result in the death of the person within a period (the **certification period** ) that ends not more than 12 months after the date of the certification;
- (b) at least one of the registered medical practitioners is a specialist practicing in an area related to the illness or injury suffered by the person;
- (c) for each of the certificates, the certification period has not ended.

Compare with the following common definitions:

‘Terminal illness’ means an illness that, in our opinion, will result in your death within 12 months, regardless of any treatment that might be undertaken.

### Issues:

Insurer forming opinion vs doctors

Treatment

No IMEs?

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## Permanent Incapacity, aka TPD Insurance (Item 103, reg 103C)

a member of a superannuation fund ... is taken to be suffering **permanent incapacity** if a trustee of the fund is reasonably satisfied that the member's ill-health (whether physical or mental) makes it unlikely that the member will engage in gainful employment for which the member is reasonably qualified by education, training or experience.

Compare with the "common form of wording":

"incapacitated to such an extent as to render the member unlikely ever to engage in or work for reward in any occupation or work for which [he] is reasonably qualified by education, training or experience".

### Issues

- Any occ vs own occ
- Per APRA and FSC:
  - TPD definition need not be word for word SIS permanent incapacity
  - definitions which are more restrictive, like ADL, can be offered
  - definitions which are less restrictive, like loss of limb, can not unless they are underpinned by a test against ETE
- Waiting periods
- Insurer forming opinion as well

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## Temporary Incapacity, aka Group Salary Continuance (item 109, reg 6.01)

"**temporary incapacity**" , in relation to a member who has ceased to be gainfully employed (including a member who has ceased temporarily to receive any gain or reward under a continuing arrangement for the member to be gainfully employed), means ill-health (whether physical or mental) that caused the member to cease to be gainfully employed but does not constitute permanent incapacity.

### Compare with:

**Disabled** or **Disability** means:

Members who are Employed or have been unemployed for less than six months:

in our opinion, after consideration of medical evidence that, solely as a result of Illness or Injury occurring whilst this Policy is in force a Covered Person is:

- unable to perform at least one Income Producing Duty of his or her Occupation; and
- not working in any occupation, whether or not for reward; and
- under the regular care and following the advice of a Medical Practitioner.

### Issues:

- Critical issue: Ill health must be cause of stopping work- what if had been temporarily unemployed and got sick? Currently before APRA;
- No trustee or insurer opinion required;
- No waiting period;
- No capacity for being partially employed;
- Should payment of IP benefits cease when the claimant is assessed as permanently incapacitated?

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## SPS 250

An RSE licensee is generally required to provide, death benefits and permanent incapacity benefits to all MySuper beneficiaries on an opt out basis.

An RSE licensee can also make certain types of insured benefits available to choice members.

### **Data quality**

APRA has impressed upon life insurers and superannuation trustees the need to improve the quality of member and claims data, including that data made available during a group insurance tender. APRA has introduced specific requirements and guidance for superannuation trustees in this regard and believes that the life insurance industry has embraced this effort. APRA also has issued draft guidance to life insurers on what it considers good practice for tendering for group insurance business, improving the quality of the claims data being kept in relation to insurance through superannuation and the provision of that data in the tendering process

Continued...



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- Sustainable insurance benefits
- Reflect key plan design and risk features which make a case more or less attractive.  
In some cases, this will require new questions being asked of the client before agreeing to bid.
- APRA will be looking to see that the plans are sustainable

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## SIS covenants re insurance

52(7)(b) and (c)- Trustee must weigh up costs of insurance vs erosion of retirement savings.

52(7)(d) new duty of Trustee to “do everything that is reasonable to pursue an insurance claim for the benefit of a beneficiary, if the claim has reasonable prospects of success”.

Trustee’s resources are finite and obligation to preserve the fund for the benefit of all beneficiaries according to the terms of deed- ALCOA v Frost [2012] VSCA 238

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## Prudential background

Australians still under insured

Typical Australian worker needs insurance of 84% of income until retirement age in the event of disability.

Analysis suggests insured coverage is only 35%

- *Underinsurance- Disability Protection Gap in Australia, KPMG 2014*

APRA is concerned about the sustainability of pricing for large schemes given the recent experience of substantial reduction in premium and generous profit sharing and the limited data used for pricing.

APRA will continue to maintain and monitor a register of the larger schemes that are won (including those retained) or lost and regular discussions will be held with life insurers and reinsurers involved.

- *APRA Insights, Issue 3, 2012 Life Insurance Industry Overview 'changes of business environment'*

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## SPS 250 and draft LPG 270

Requirement for RSE to formulate, review regularly and give effect to an Insurance Strategy.

Flexible depending on business operations and objectives of fund provided requirements of SPS 250 are met.

Key component of Insurance strategy is Insurance Management Framework.

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## IMF

**Purpose: identification and management of risks relating to insured benefits:**

- Types and level of benefits;
- Administration of benefits including underwriting eligibility, claims management;
- Holding and accessing adequate data;
- Due diligence and selection criteria for insurer;
- Claims philosophy;
- Policies documentation; and
- Review at least every 3 years.

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## Data

**Details:** claims experience including event types, dates of events, dates notified, date admitted, disputes, dates paid and amount of claim,

Going back at least 5 years;  
Required to support tender process; and  
Outsourcing OK- but RSE responsible;

**Issues:**

Life insurers are not PI insurers.  
Risks to beneficiaries if data is accurate -including S29 ICA.

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## Claims Philosophy

Important focus for APRA in 2014

Philosophy is a process to assess the willingness and ability of insurers to pay legitimate claims including:

- SLAs;
- claims paid vs denied;
- Rate of appeal; and
- Appeals overturned.

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## Policies and documentation

To be in place before cover commences!

Must deal with:

- Underwriting,
- Reductions or loadings;
- Conditions when claims paid or denied; and
- Liability or indemnity for outsourcing and when data inaccurate.



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