

# Commission Disruption and Change in Retail Life Insurance

Presented by John Trowbridge, Clive Levinthal,  
Greg Martin and Dr Joseph Daley

## Scrapping upfront commissions death knell for independent advisers

3 Feb 2015 28 comments

A swift move away from upfront commissions could spell the end of non-aligned advice, with only the large independents and aligned groups able to survive the inevitable drop in revenue, stakeholders...

### Recommendation 24

Better align the interests of financial firms with those of consumers the power to ban individuals from management and ensure remuneration stockbroking do not affect the quality of financial advice

## Mission: Interim report on Retail Life Insurance Advice

19, 2013 INSURANCE, NEWS, REPORTS AND SUBMISSIONS, SUBMISSION  
Financial Rights Legal Centre, Choice and Maurice Blackburn Lawyers  
report on Retail Life Insurance Advice.  
have provided comment on the report

## Ban Up.

December 7, 2014

The Financial System Inquiry

## Life inst of comm

PM

Updated 10 Feb 2015, 8

Consumer groups at insurance industry to commission payments.

A report by ASIC last year i all life insurance advice give, comply with the law.

Cons. are conce.

have applauded the Murray inquiry's recommendation about how reforms will be delivered and enforced.

**Insights - Actuaries Institute**  
**Thursday 19 February 2015**

**Commission Disruption and Change in Retail  
Life Insurance**

1

**THE BACKGROUND**

**JOHN TROWBRIDGE**

**CHAIRMAN**

**Life Insurance and Advice Working Group**

# Recent Public Initiatives

2

- 1. ASIC: Review of retail life insurance advice**  
issued October 2014
- 2. Industry Response:**  
formation of LIAWG - October 2014  
two independent Trowbridge reports -  
Interim Report - issued 17 December 2014  
Final Report - to be issued 26 March 2015
- 3. Financial System Inquiry**  
Report - issued 8 December 2015  
Submissions to Treasury - 31 March 2015
- 4. Parliamentary Joint Committee –**  
Inquiry into proposals on professional, ethical and education standards  
Report issued 14 December 2014

# The ASIC Review -

3

**Expressed concerns about high lapse rates, quality of advice**

**Recommended that insurers –**

- ✦ **address misaligned incentives**
- ✦ **address high lapse rates**
- ✦ **review remuneration to support quality advice**

**Recommended that licensees –**

- ✦ **ensure that remuneration supports quality advice on client needs**
- ✦ **review business models to support strategic advice**
- ✦ **review and monitor training and competency of advisers**

# The FSI Report -

4

## **Recommendation 24**

***“Better align the interests of financial firms with those of consumers ... and ensuring remuneration structures in life insurance ... do not affect the quality of financial advice”***

### **The Inquiry**

- **acknowledged the high initial arranging costs of insurance**
- **was explicit that it does not recommend banning all commissions**
- **recommended a level commission structure**
  - ... that is sustainable**
  - ... and consider the findings of the LIAWG during the development and implementation phases**

# The Trowbridge Interim Report

5

## **First phase of industry response to the ASIC Review**

**Covered four topics –**

- 1. Quality of advice**
- 2. Remuneration and other incentives**
- 3. Insurer practices and product offerings**
- 4. Industry productivity**

**Sought submissions on ideas, options and questions raised in the report**

**On remuneration sought submissions on 5 models (level, hybrid, modified hybrid, level plus fees, level funded)**

**Final report with findings and recommendation now being prepared**

# Commission Disruption and Change in Retail Life Insurance

## Players, Stats & “Sold v’s Bought”

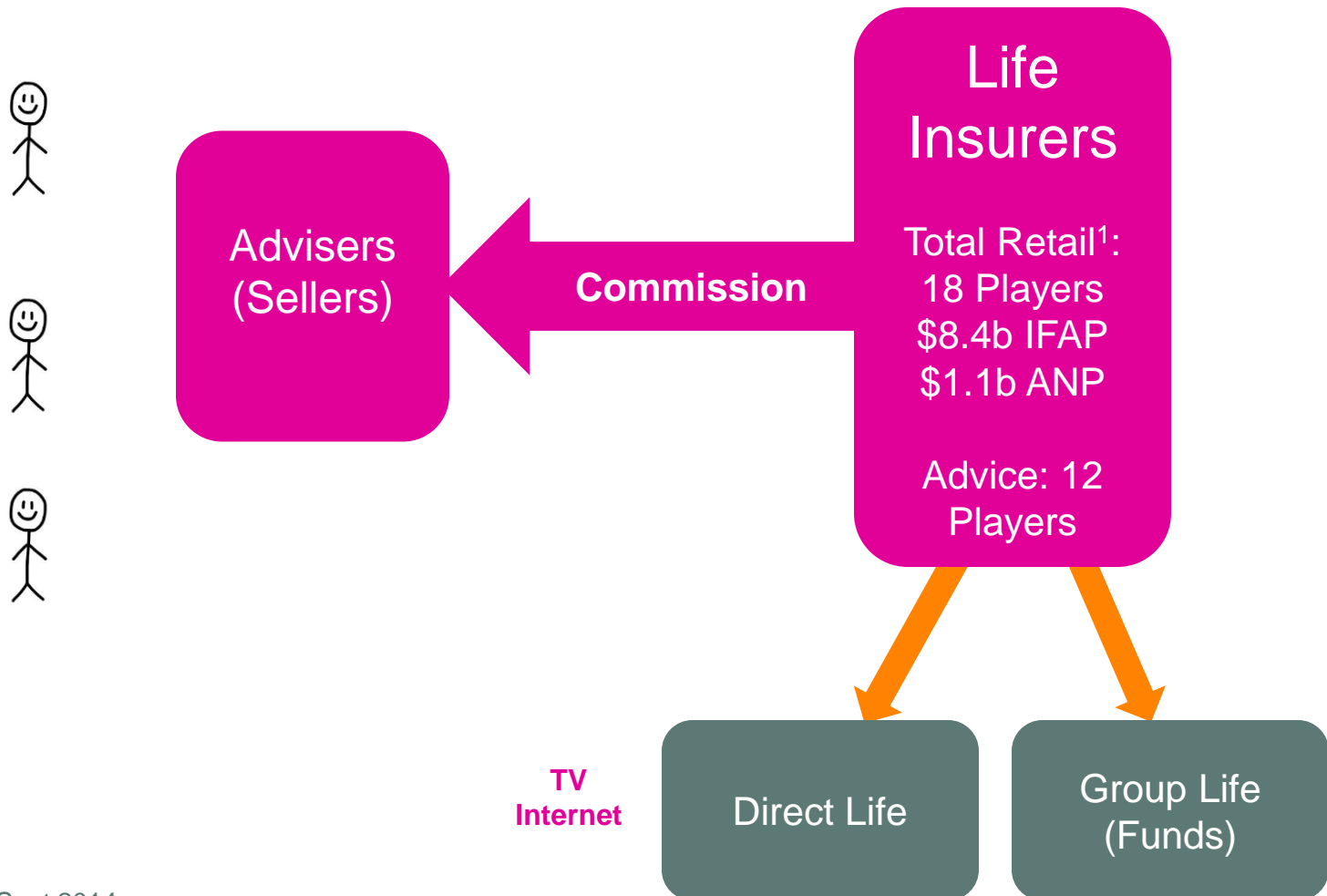
Greg Martin

19 February 2015

- A quick overview of the players
- Sold v's Bought Debate
- ASIC Report - Analysis on Certain Aspects

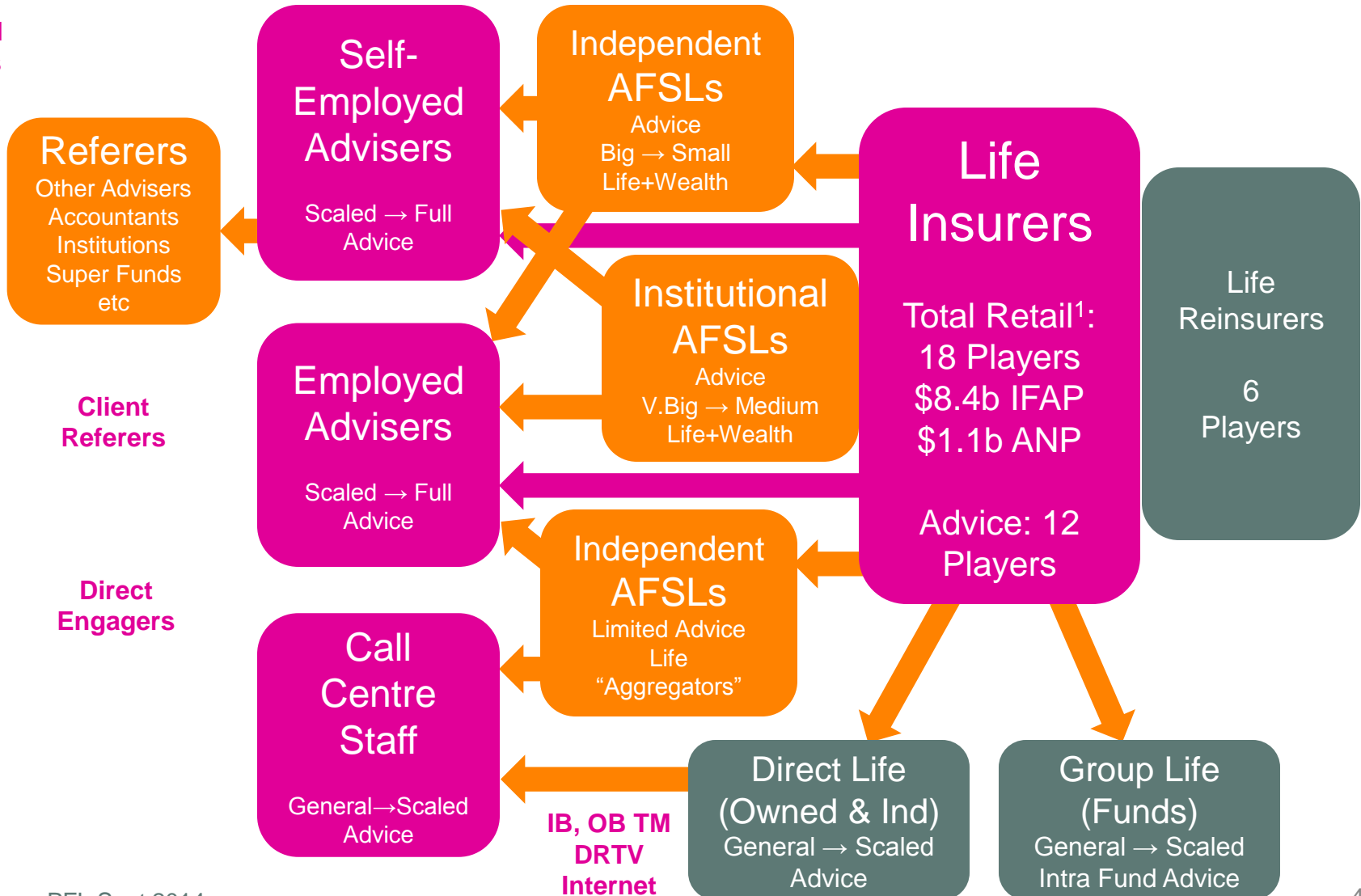


## Customers



Actual  
Customers

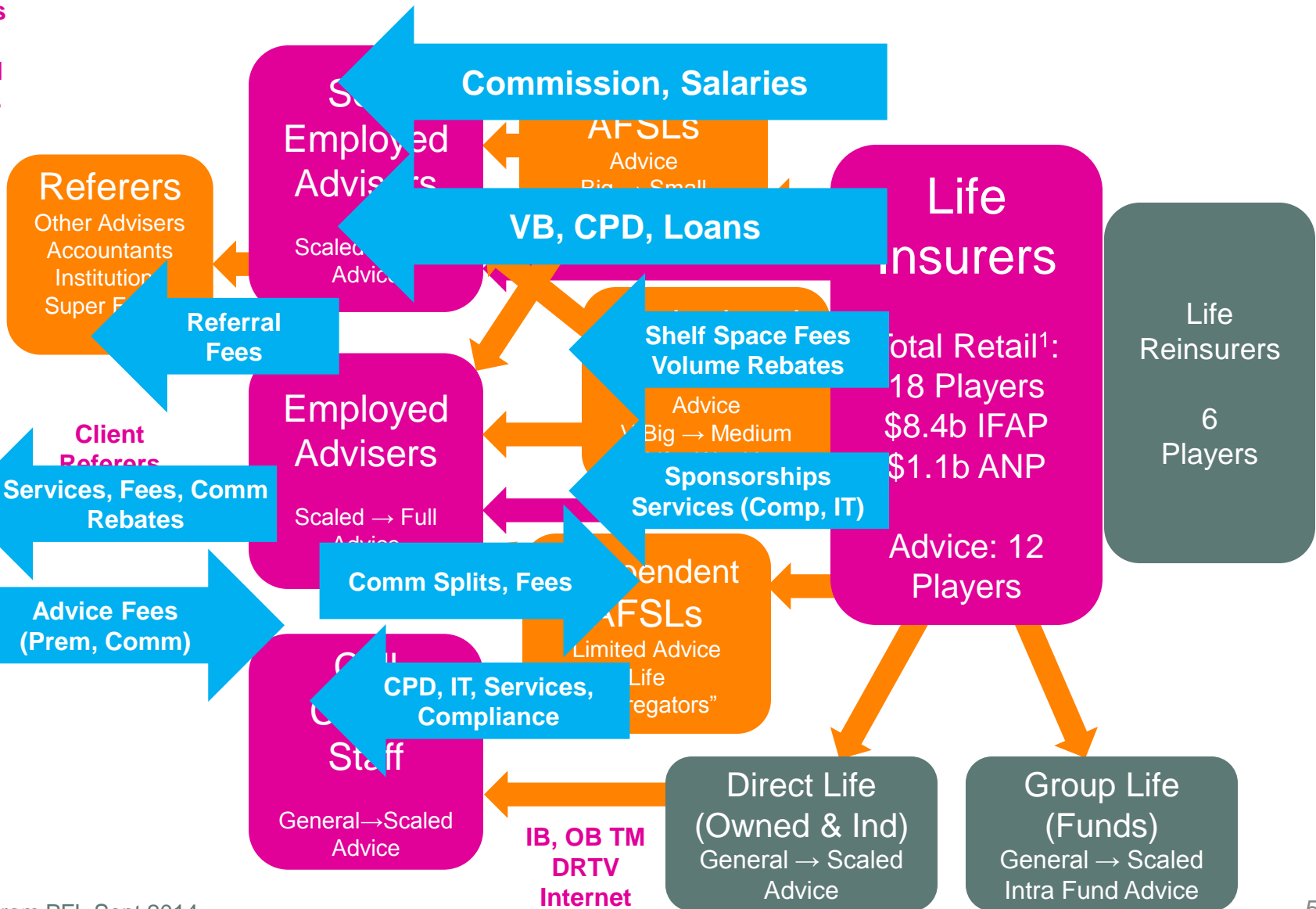
Uninsured  
Prospects  
Clients  
Buyers



# Retail Insurance Market

Actual  
Customers

Uninsured  
Prospects  
Clients  
Buyers



- Many industry and proprietary studies over the years
  - E.g. FSC Metlife Apathy to Action, 2014
    - Understanding, spending priorities/expensive, “apathy”
  - Need to be careful: Stated v's revealed preferences & attitudes
    - Opinion: Many get this a bit wrong...complex...but also simple....
    - “Cost”, “Expensive”, “Trust”, “Need”, responses not always true...
  - Also, lots of solid theory: purchase paths, market constructs, etc
  - Opinion: Sort of right, sort of not

- Life insurance not unique.....lots of similar things

Doctor check-ups

Paint your house

Dental check-ups

Leaves out of gutter

Tax returns

Do your will

Home fire “escape plan”

Colonoscopies for CRC  
(or even FOBT!)

Stated excuse for these is often “time”, “cost” .....

- Small cost of incremental deferral (rational)
- Health & mortality
- Lack of bragging rights
- Behavioural science
- Behavioural finance

# Sold v's Bought Debate (Cont)

L.I.,  
Wills

- CRC, FOBT, Colonoscopies...just as an example
  - 1 in 12 Australians likely to develop CRC in their lifetime.
  - CRC is the second most common cause of cancer-related mortality
  - Historic studies consistently indicated <20% ever undergoing FOBT

Colorectal cancer screening in Australia: a community-level perspective, Medical Journal of Australia, 2012

- Also, not true people don't think about it...
  - Aus: 80% do life insurance searches online. Every 30 seconds!
- So...not unique....BUT...
  - In a sub-class: Those with weak daily "action" trigger points
    - In the class of those with a long, soft "rubber bands"...e.g. CRC
- Also in the class of those involving purchase complexity
  - How much do I need...and of what combination...
- The big issue.....need for positive "activator"...that is the "sell"

Funeral  
Life

Desired, Needed

Emotionally Deferrable

Figure 15: Lapse rates by remuneration arrangement for stepped premium policies

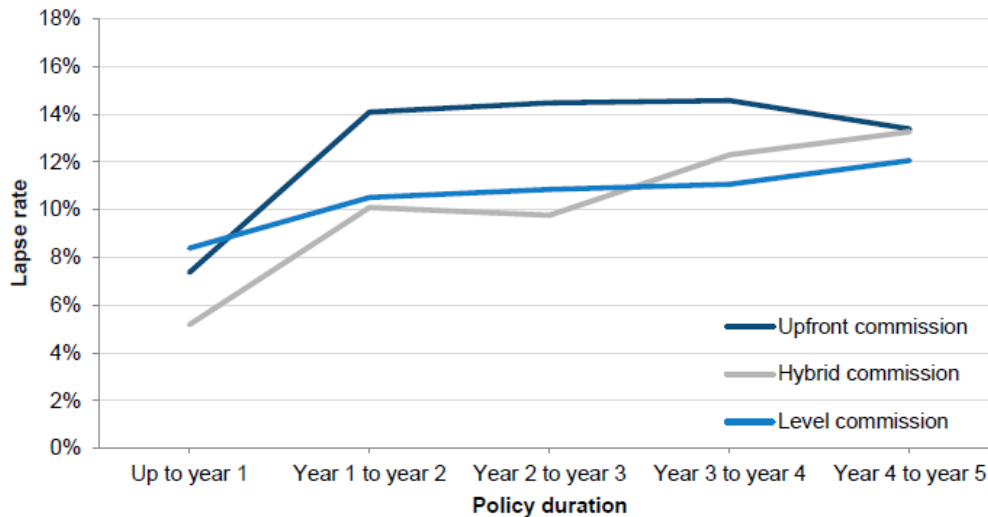
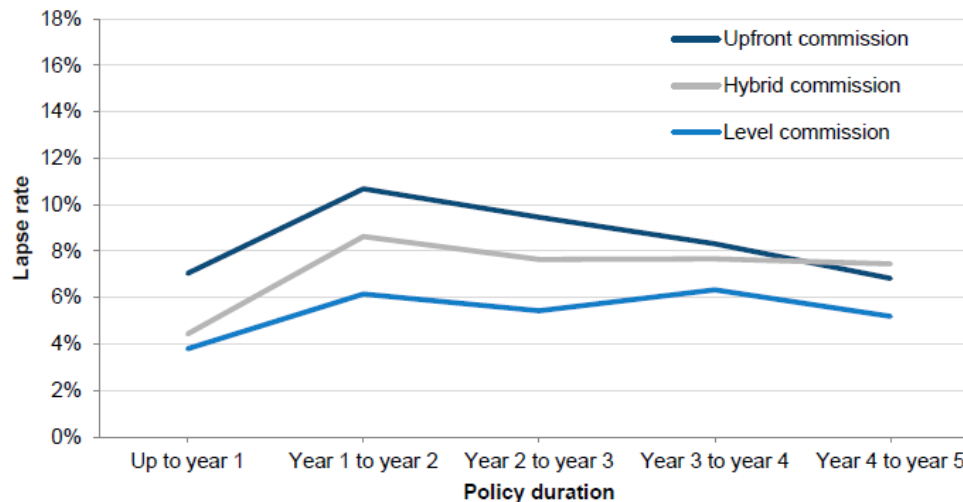


Figure 16: Lapse rates by remuneration arrangement for level premium policies



- ASIC Report (inferences):
  - Comm model → lapses
  - Responsibility → Yr 2 churn
  - Level v's step
  - Recent ↑ lapses → rebroking
- Other considerations
  - Annual premiums – year 1
  - Year 2 sticker shock
  - Current free choices
  - Rational behaviours
  - Post GFC (non-advice)
- Correl ≠ C&A
- Be clear on dimensions
- Be clear on C&A



## Retail Life Insurance Products Sold By Advisers

The views of an actuary  
working as an adviser

Feb 2015

# My 5 key points

## 1. After 10 years, only 50% of our business is sold using hybrid commissions

- Our profit margin is less than 10%. Moving to everything on hybrid would cause us to lose money for several years. We have not managed to increase our use of hybrid by more than 10% in any one year.

## 2. We are losing more clients to accountants and financial planners (when clients are on hybrid commission)

- They encourage our clients to assign them as their broker after the first year. We do the hard upfront work and they get the higher trail commission ! Not a major risk with upfront commissions.

## 3. Most of our advisers have no tertiary education

- Nearly 75% of Australians have no bachelors degree equivalent. Our advisers are great at what they do, but they would not have become insurance advisers if they could get tertiary academic qualifications. Academics are not the best at selling life insurance Medical terminology education courses are more relevant

## 4. It is harder to sell life insurance than other forms of insurance

- Our life insurance business is 10 years old and has 13 advisers. Our general insurance business is only 3 years old and has only 2 advisers. Yet we now sell as many general insurance policies per annum as life insurance policies. General insurance and health insurance is bought, yet life insurance has to be sold.

## 5. Advisers play an important role in convincing clients to keep paying for their life insurance premiums

- 130 of our clients failed to pay their premium in January. We worked extensively with each and get most to renew their cover. What would the DAC write off be if we were not there ?



**EXPERIEN**  
INSURANCE SERVICES



# Actual commission rates are not as high as you think !

	Upfront	Hybrid
Headline rate quoted by press	115%	80%
Remove GST	-11%	-8%
Remove components of premium on which commission is not paid eg stamp duty, frequency loadings, policy fee etc	-15%	-8%
Net commission	89%	64%

***Referral fees , clawbacks and client rebates will reduce these even further***

# There are very high costs incurred in selling life insurance

- It is expensive to fund a life insurance adviser !

Professional indemnity insurance	\$5k per annum
Assistant salary	\$50k + per annum
Dealerships fees	\$15k per adviser per annum
Software costs (eg X Plan)	\$10k per annum
Experienced adviser salary	\$100k per annum base + bonus
Rent	\$10k per annum
IT costs	\$3k per annum
Marketing	\$10k + per annum
Training, travel, phone, workers compensation, compliance training, accounting, payroll tax	\$5k +++

> \$200k per annum +

- This is without allowing for :
  - Difficulty, time and recruitment cost in finding someone
  - Key person risk
  - Operational risks
  - High compliance costs eg ongoing training

# And it is difficult to make a sale !

- Most people are **not pro-active** with their life insurance
- **No compulsion** like health insurance, super and some general insurances
- Finding people to discuss insurance with is hard. Convincing them to proceed is harder !
  - 20% of people that are spoken to agree to receive a proposal
  - 60% of these submit an application
  - 80% of these progress with application after underwriting process
  - **So, a good adviser will need to speak to 20 people to make just 2 sales a week !**
- **Lots of time per client !**

Initial client visit to conduct fact find	2 hours +
Prepare a high quality SOA	3 hours +
Presentation of SOA and completion of application	2 hours +
Arrange and follow up medical tests	3 hours +
Annual reviews	5 hours +
Claims	Days

# 「The commissions don't cover the」 「costs.....」

- Costs per annum = \$200k+
  - Sales per week = 2 (48 weeks in the year)
  - Average premium per sale = \$2,500 pa
  - Sales of slightly more than \$200k per annum in premiums
  - Income is approx \$160k in first year
  - Costs are \$200k + in first year
  - Net loss of \$40k + on upfront commissions
- Needs to be higher. An average adviser will not be ok*
- Needs to be higher. Can only work with wealthy clients*
- Need capital and a long term view*

Average time between initial client meeting and receiving commission can be > 3 months

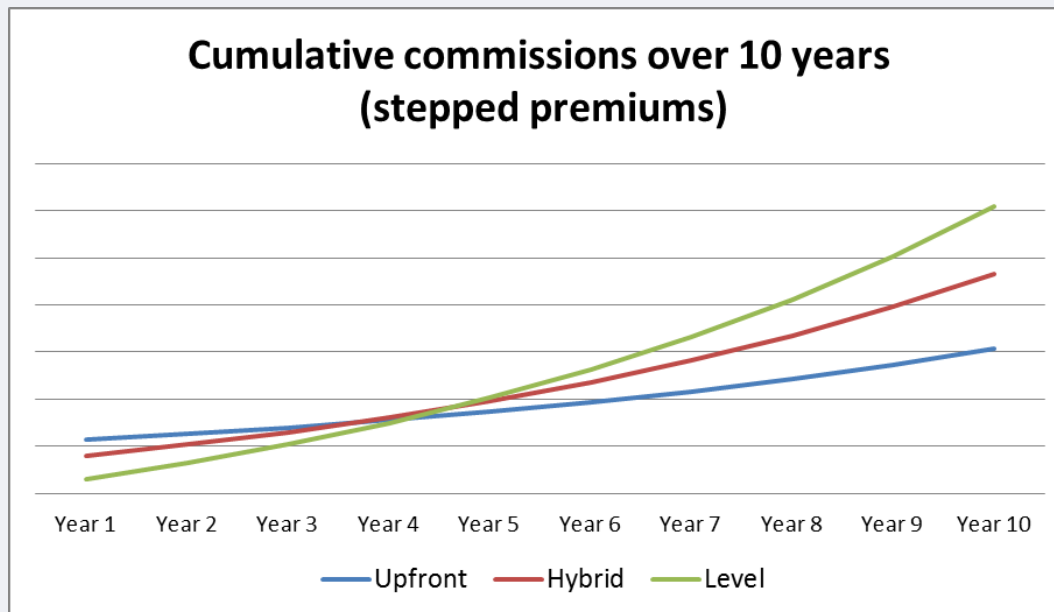
# Theft of trail commission is a big concern

- We often advise clients to use level premiums and we take hybrid commission
- Creates a feeding frenzy for financial planners and accountants to steal the client and take our trail commission with one simple form being filled out
- [Yourshare.com.au](http://Yourshare.com.au) will refund half our trail commission to clients if you assign them as the broker – but they will not perform any work for you



**EXPERIEN**  
INSURANCE SERVICES

# Hybrid and level commissions can be materially more expensive for insurers



Level 98%  
Hybrid 51%

*Assumes same policy/no lapse*

Will insurers assume a fall in lapse rates if upfront commissions are abolished ?

Will hybrid and level commission rates fall or will customer prices rise ?

Surely the goal from these changes can only be to reduce prices for clients ?



**EXPERIEN**  
INSURANCE SERVICES

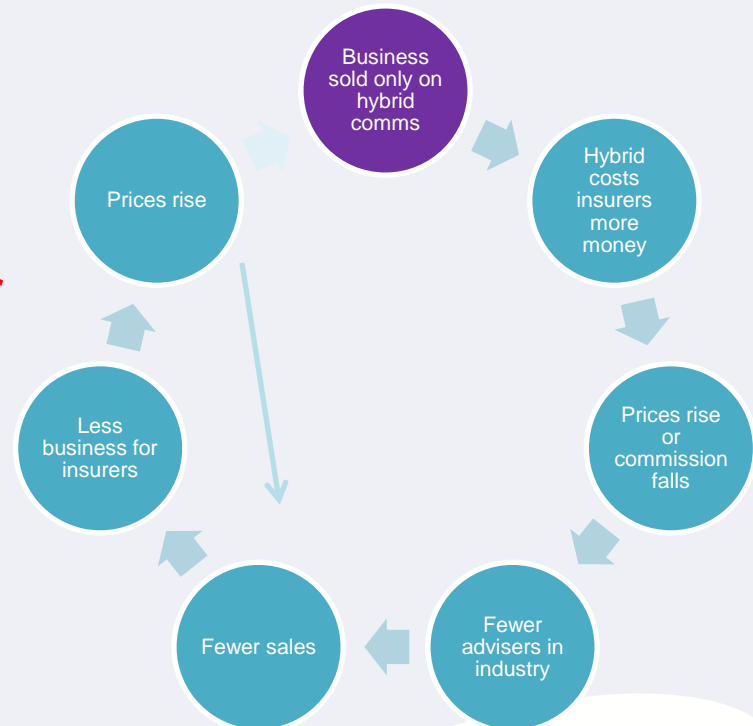
# What outcome are we trying to achieve ?

## Lower customer prices scenario



## Abolish upfront structure and lower hybrid commission rate scenario

or



**EXPERIEN**  
INSURANCE SERVICES

Financial Services Reform raised education and compliance standards in 2001...but tertiary qualifications may now be required.....

***FSR was good.....but don't now try get academics to sell insurance !***

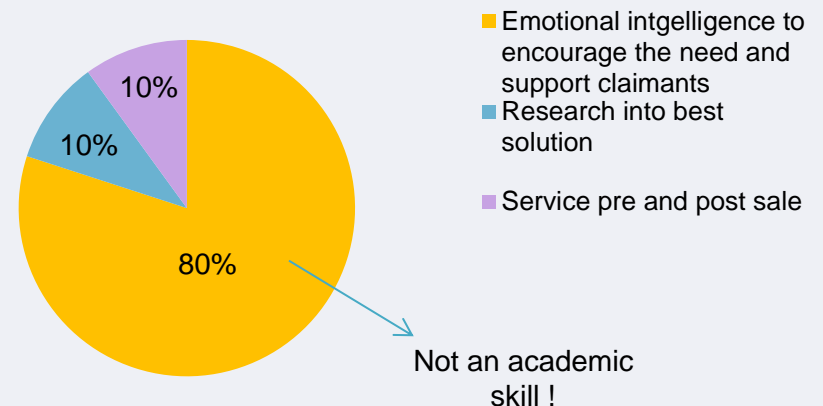
Never used to have :

- PS146
- FSG
- SOA
- PDS
- Licensing/ARs
- Audits



Profession	Annual independent audit ?
Insurance adviser	Yes
Lawyer	No/sometimes ?
Accountant	No/sometimes ?
Actuary	No/sometimes ?

**Relative importance of skills to sell life insurance**



**EXPERIEN**  
INSURANCE SERVICES



A photograph of a family at a beach. In the foreground, a young child with blonde hair, wearing a blue bucket hat and a white t-shirt, is smiling and holding a piece of bread. In the background, a family of four is sitting on the sand under a large yellow and red striped beach umbrella. The ocean is visible in the distance under a blue sky with light clouds.

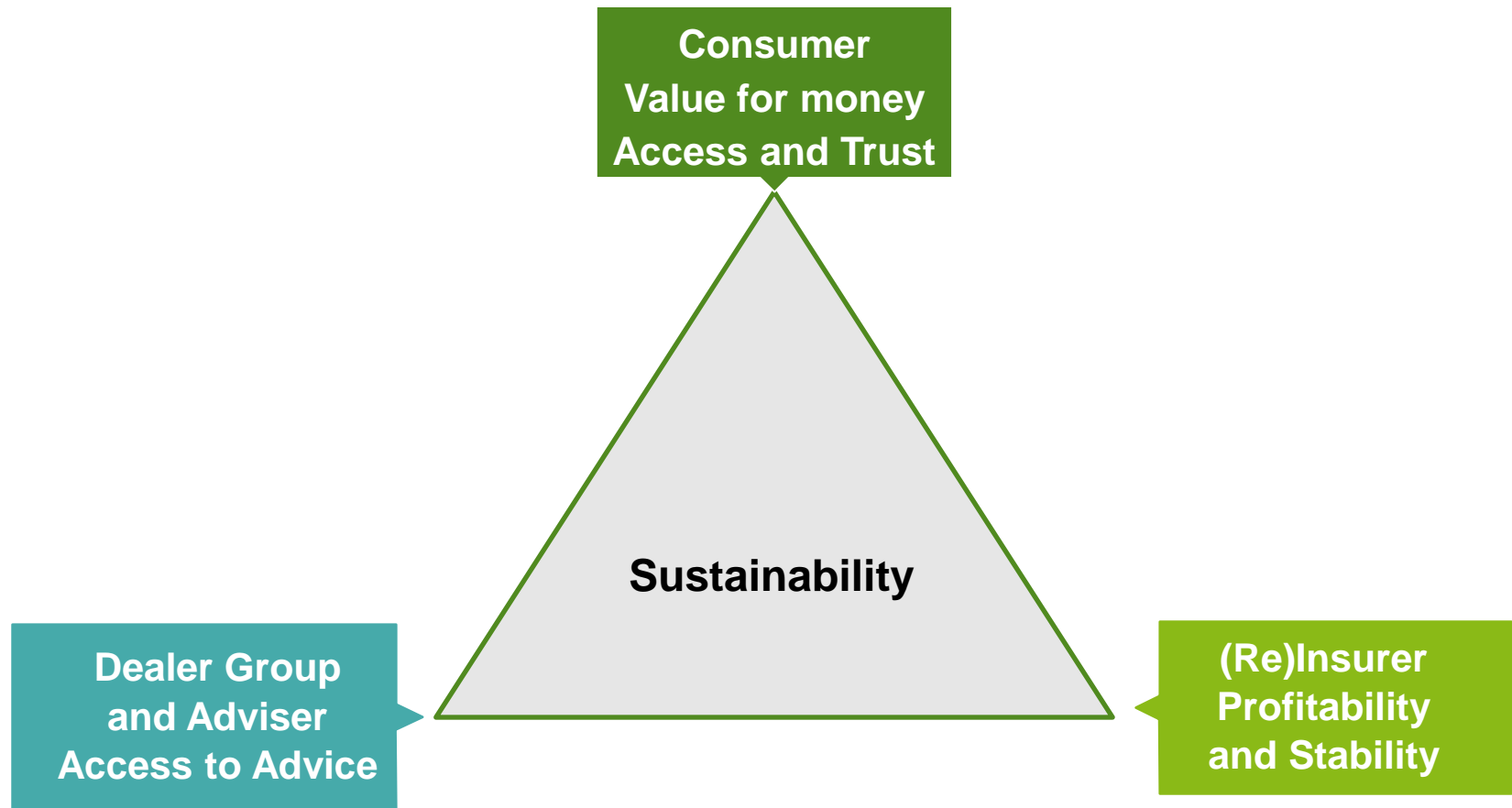
# The Risk Advice Economy of the Future

Actuaries Institute Insight session February 2015

**TAL**

# Striking a balance in the risk advice economy

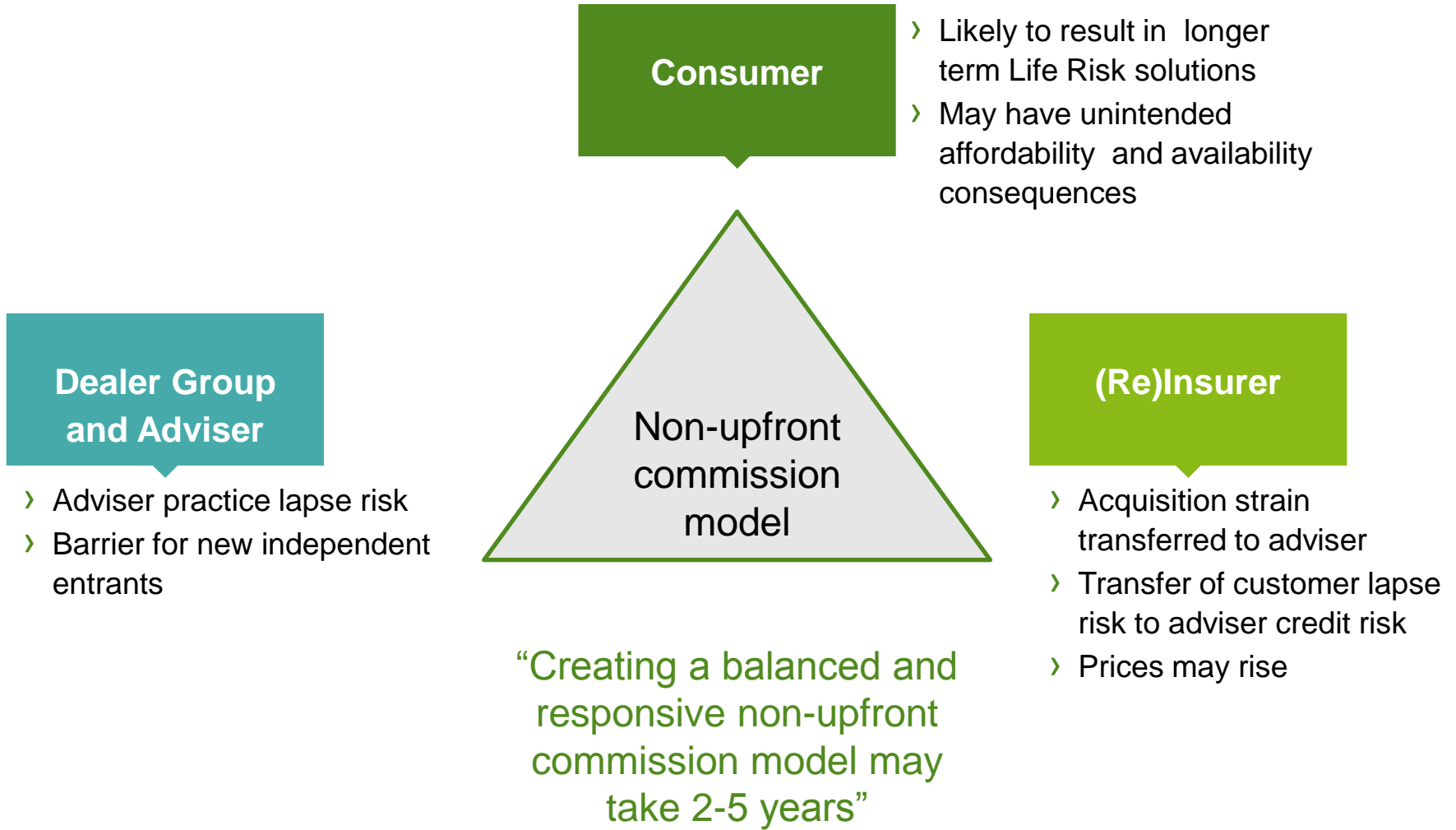
---



## Key Underlying Principles

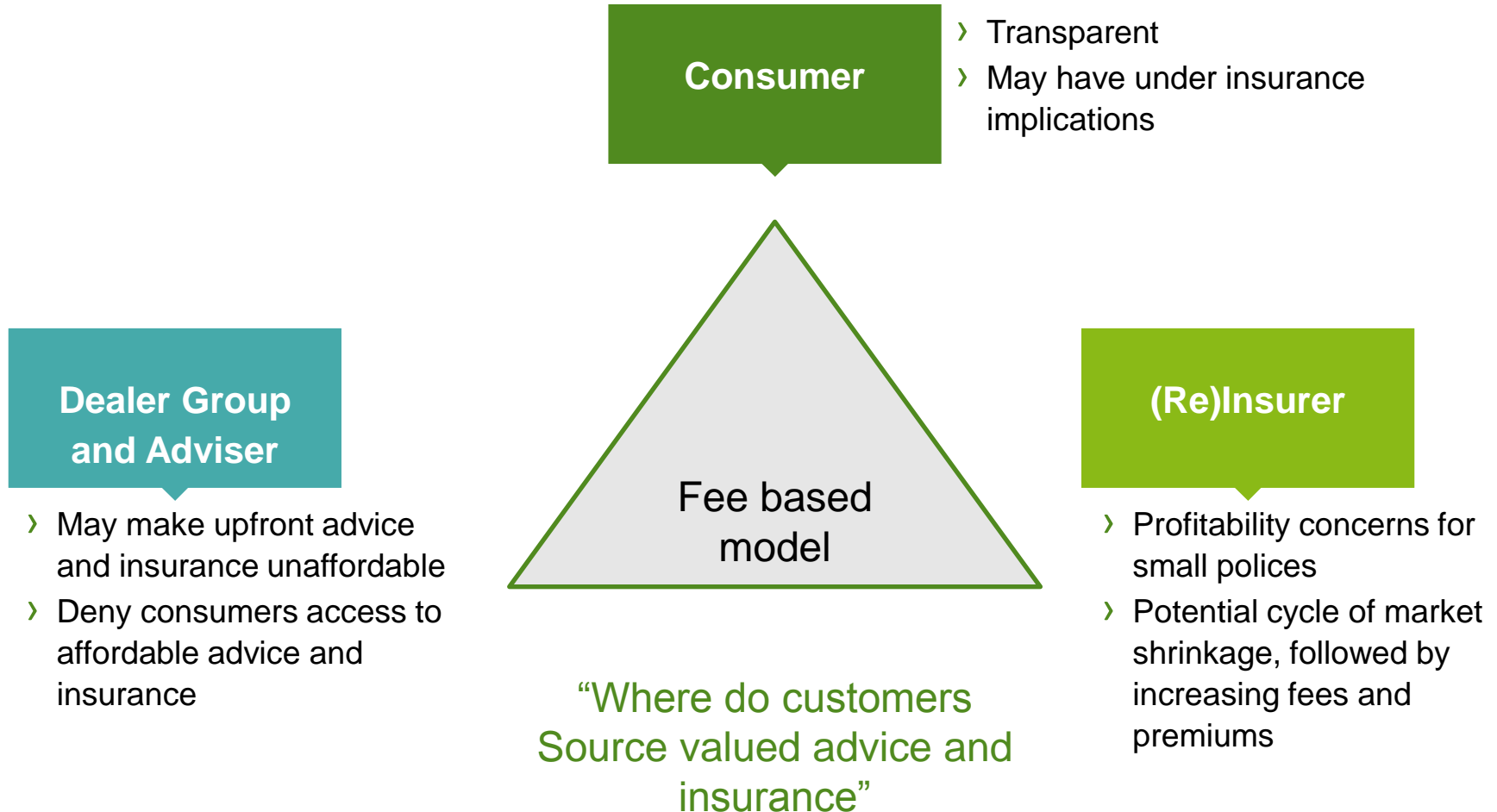
Equitably sharing the costs and risks of providing risk advice and insurance  
Creates the right level of stimulus for continuous improvement

# Impact of a non-upfront commission model



# Impact of a customer fee model

---



# The many futures of the risk advice economy

---

## Summarising the Economics

Breakeven year	Adviser	Insurer
Upfront	0	4.5
Hybrid	2	2
Level	4.5	1

**“The challenge is to create a balanced and responsive risk advice economy for any future”**

A photograph of a family at a beach. In the foreground, a young child with blonde hair, wearing a blue bucket hat and a white t-shirt, is smiling and holding a piece of bread. In the background, a man, a woman, and another child are sitting on the sand under a large yellow and red striped beach umbrella. The ocean and a blue sky with clouds are visible in the distance.

# The Risk Advice Economy of the Future

Actuaries Institute Insight session February 2015

**TAL**