

Submission to
The Royal Commission into Misconduct
in
The Banking, Superannuation and Financial Services Industry
Life Risk Insurance Underwriting and Claims Professionalism
and Product Design and Development

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I have spent over 40 years working within the Life Risk Insurance Industry from an Underwriting and Claims background. My later roles were managerial including the role of Managing Director of a major Life Reinsurer in Australia for over 10 years. I retired from the corporate environment at the end of 2011 and have been providing occasional consulting services since. In my last 20 years in the industry, I work in managerial roles as a technical specialist on underwriting and claims practices and product development areas.

This submission focuses on points of regulatory change requested in Question 1 of Module 6.

1. The current regulatory regime needs to change in the following areas:
 - 1.1. Life Underwriting and Claims Personnel Professionalism - All Life Underwriting and Claims assessment personnel with authority to accept or deny underwriting risks and claims should be professional trained, qualified and formally licensed under ASIC oversight.
 - 1.2. Product Design and Development – A strict regulatory approval process for all Life Risk Insurance products, benefits and exclusions should be installed.
 - 1.3. Banning Certain Products - All Life Risk Insurance products with a Loss Ratio of less than 50% should be banned.

1.1 Life Underwriting and Claims Personnel Professionalism

- a) There is a critical issue regarding the professionalism of claims and underwriting handling in the Life Insurance Industry - this is an issue of knowledge, skills, training and qualifications of the Underwriting and Claims assessment personnel who are making the important decisions of accepting and denying Life Risk Insurance applications and claims. Currently there is no requirement for these personnel to be qualified in any way. This is totally incongruous with the importance of the implications of their decisions on consumers and is totally unacceptable having regard to the significant number of issues reported around underwriting and claims handling and decisions. These personnel are mainly taught 'on-the-job' and most of the training that they might undergo is via individual insurer's in-house training courses.
- b) The Life Insurance Industry is chronically short of high quality underwriting and claims assessors and as a result, 'poaching' of assessors across the industry is rife. When poaching assessors, the new employer has no independent way to determine knowledge and skill levels that the poached assessor may possess. This shortage of assessors and the lack of a requirement for independent verification of an assessor's knowledge does not generate an environment that encourages assessors to undertake voluntary external skills training. It in

fact, does the opposite – semi-skilled assessors with the ‘gift of the gab’ or those who are good self-promoters are able to achieve senior roles without the necessary knowledge and skills to appropriately manage the responsibilities of their senior roles.

- c) The Life Insurance Code of Practice has a requirement that underwriting personnel (under paragraph 5.15) and claims personnel (under paragraph 8.20) *will be appropriately skilled and trained. They will not make underwriting/claim decisions on our behalf until they have demonstrated technical competency and an understanding of all relevant law, the requirements of the Code and relevant FSC Standards and Guidance.* This assessment of an individual’s knowledge and skills levels is an insurer’s determination under the Code. The level/degree of authority granted to these assessors is also an internal insurer decision usually based on years of service in the industry– for example, it is not uncommon for an assessor to be classified as a ‘Senior’ assessor after only 2 years of experience.
- d) The Australasian Life Underwriting and Claims Association (ALUCA), which is the association representing Life Underwriting and Claims personnel, has a Competency Framework which provides a description of the knowledge, skills and experience that they believe are the minimum requirements for their members to professionally perform their various roles. This ALUCA Competency Framework is at a very high level and is only ‘guidance’ for its members. ALUCA does not provide any independent measurement or scrutiny of a member’s skill levels, knowledge or performance. There is no regulatory requirement placed on Insurers to accept or use this framework even as a minimum requirement of knowledge and skills for compliance with the Life Insurance Code of Practices or as a guide for their in-house training courses. ALUCA does have a number of classifications of membership, such as Member, Affiliate, Associate, Associate Fellow and Fellow. There is a basic points and years of experience system to achieve these classifications. The undertaking of the requirements for higher ALUCA classifications is not mandatory for members. ALUCA Membership is widespread within the industry but is not compulsory for underwriting and claims assessors and while ALUCA has over 1500 members, relatively few members undertake any of the external courses required for higher ALUCA membership classifications.
- e) ALUCA has a Code of Conduct which goes some way to support the impartiality and professionalism of assessors and is mandatory for all members of the Association. Insurers are under no obligation for their decision-making underwriting and claims assessors to be members of ALUCA.
- f) For over 30 years and until very recently, Life Insurers appear to have not put a high priority on the training of their assessor and not particularly interested in spending money on assessor training, especially external training. The Australia and New Zealand Institute of Insurance and Finance (ANZIIF) is the preeminent specialist training institute for the insurance technical personnel of the industry in Australia, New Zealand and SE Asia. The Life Insurance industry’s failure to use their range of technical life risk insurance courses over the years has resulted in ANZIIF reducing the number courses they offer in the life insurance area, especially in the higher skill levels of underwriting and claims education– this is a shame!. Now some insurers have turned to developing their own in-house assessor training courses. It is more than likely that much of these in-house training courses focus is on process rather than on the technical knowledge required for appropriate underwriting and claims decisions. This in-house approach to training avoids the exposure of any lack of knowledge to external testing and scrutiny. These in-house training pathways also tend to support poor and inappropriate corporate cultures, performance and behaviours, where they exist, without bringing any of the benefits and impartiality of the discipline of professional external training courses and skills testing.
- g) Underwriting and claims assessors are responsible for major decisions affecting the lives and lifestyles of the industry’s consumers. It is time that it is mandatory that these assessors are professionally qualified and that their knowledge and skills are independently assessed and

measured against the full range of required knowledge and skills of their roles. The formal licensing of assessors who are to be granted authority to make decisions on underwriting risks and claims is a minimum to improve professionalism, fairness and impartiality of these decisions. ASIC should oversee this licensing and the required standards to support increased professionalism.

1.2. Product Design and Development

- a) Over the years, the product design and review function within Life Insurers has been more about 'winning space on the sales supermarket shelf', such as Approved Product Lists (APL's), than about improving coverages or covering new and emerging needs of the consumer. For over 30 years, the Life Insurance industry has struggled with the very basic question of "Who is their customer? – Is it the insured/consumer or the sales adviser/broker/distribution chain?" Many insurers acted as if their customer was the distribution chain by accepting the argument that more sales and more business would provide a lower cost base per policy for better value to the customer – 'the bigger the better'.
- b) This argument is clearly spurious. In many areas of product development, Insurers bowed to the distribution chain by adding more events and benefits to their products to satisfy simplistic 'tick-a-box' product comparators. The major role of product developers has been to find new events or benefits which other insurers don't have – "We have 21 benefits and our competitors only have 20 so sell our product or change your clients to our better product."
- c) An example of this is from the 1990's when Critical Illness/Trauma (CI) cover was introduced: The one 'Paraplegia' Event which covered the loss of use of any two limbs was changed to four events; 'Paraplegia', 'Quadriplegia', 'Hemiplegia' and 'Diplegia'. Other examples of this type of inappropriate product development are the CI events, such as MS, Benign Brain Tumour, Meningitis, Head Trauma, Parkinson's Disease, Encephalitis and Meningococcal Disease. Many insurers' version of these specific disease CI Events have a similar degree of impairment requirement and these specific disease events are already covered under their Loss of Independent Existence type event. This single event covers all causes of similar impairment measured by criteria such as an Inability to Perform Activities of Daily Living, Impairment of Whole Person Function or similar. These additional events added no extra coverage or benefit to the consumer and can, therefore, be added at no additional cost. This allowed a marketing spiel of "we have more benefits than our competitors for the same price". This type of thinking has continued throughout the 2000's. The initial 4 or 5 major CI events continue to account for about 85% to 90% of all CI claims while CI events available in the industry have now spiralled upwards to reached around 50 events.
- d) A similar approach to product development has now spread to all types of death and disability products with the addition of numerous add-on benefits. This is the same across all distribution methodologies.
- e) As a result of this unconstrained product development, Life Risk Insurance coverages have become so complicated and confusing that it is almost impossible for even a trained life insurance expert to fully understand these contracts. In many instances this unconstrained product development has not resulted in significantly improved coverage for consumers and only served to confuse consumers. The Life Risk Insurance products are now exceedingly complex and disclosure documents are too long for consumer comprehension. When a number of insurers' individual contract differences are to be considered, it is impossible for the consumers to fully understand or compared products. Product Disclosure Statements now commonly exceed over 100 pages. The average consumer ~~cannot~~ cannot be expected to understand the medical terms, the legal nuances and the complexity of these

modern insurance contracts. Those consumers who struggle with even simple contract wordings and financial concepts are wide open to manipulation and exploitation.

- f) During my corporate life, I argued against standardisation of insurance definitions in the erroneous belief that it would stifle innovation and competition. In many instances insurers have misrepresented product innovation as an advantage for consumers whereas it has been more about the insurer maintaining or attracting advisers and other sales distributors to sell their products. It is time to stop this unconstrained product development.
- g) There is a need to introduce a formal regulatory product approval process to return benefits to a sustainable, simpler and more comprehensible design which better support the needs of the consumers. The 'approval' of insurance products would also provide consumers with comfort that an external impartial body has reviewed the reasonableness these contracts. In the USA, each of the individual States' Insurance Departments or Divisions must approve every coverage before it can be sold in their state. This approval process can be a costly administrative process if an insurer wants to sell their product across all the 52 US states. Some insurers don't write certain products in some states due to this process and its costs. Australia's centralised federal regulatory insurance framework would make approval of products simpler and less costly than the US regime.
- h) This approval process could be under the standard cover regime in Division 1 of Part V of the Insurance Contracts Act and other regulatory regime. The concept of approved, standard or prescribed cover across all Life Risk Insurance has very significant merit - not only for key terms but actual events covered, definitions, exclusions and benefits provided.

1.3. Banning Certain Products

- a) Most Life Risk Insurance products do serve a valid consumer need at reasonable cost, subject to the issues mentioned above. However in some instances, the cost of the actual risks covered is grossly disproportionate to the administration and sales costs. For example, in the past, some products have had a Loss Ratio of less than 20%. This means that less than 20% of premiums paid are returned to consumers as claim benefits and more than 80% of a consumer's premiums are paid to entities (or individuals) for the administration of the product or within the sales and distribution chain.
- b) All Life Risk Insurance products with low Loss Ratios should not be allowed to be sold and it is very hard to argue that a product is a benefit to consumers if less than 50% of their premiums are returned in claim benefits. It is not unreasonable to place a minimum Loss Ratio limit of 50% on all insurance products.
- c) What is an appropriate minimum Loss Ratio? Insurance is a product of a sharing of financial risks across all insureds/customers within an insurance pool. Not all customers will claim a benefit during the lifetime of their coverage. Some customers will suffer an insured event and receive a benefit in excess of their premiums paid. Others who are fortunate to not suffer an insured event will only receive the peace of mind that their financial stability was protected. Can you put a financial value on this 'peace of mind'?
- d) All Life Risk Insurance products should have a minimum Loss Ratio and if the Loss Ratio on an existing block of business reduces below this minimum, premiums should be required to be reduced. It is clear that a Group Product which has the advantage of mass simplified administration should have a higher minimum Loss Ratio, maybe 90%. While an individually underwritten and administered Retail Product might have a minimum Loss Ratio of maybe 80%. Other products and sub-products would have other appropriate minima.
- e) Some pedants in the industry will argue that Loss Ratios are simplistic or they are not appropriate or are problematical for Life Risk Insurance. These views may have some

technical credence for actuaries. The average consumer/insured, however, has little or no idea of what is the actual pure risk cost of a particular insurance cover. A transparent Loss Ratio is an appropriate and easy to understand indicator of 'value for money' for the consumers – "How much of my premium payments will go to claim benefits and how much will be taken by the Insurer for administration and sales costs?" There are complications in the calculation of Loss Ratios, so there would need to be a standardised methodology across the industry for each product and these methodologies would need security regulation by APRA.

- f) Fully transparent Loss Ratios of all Life Risk Insurance products, clearly disclosed to the consumer, provide an understandable and comparable figure of the cost and value of coverage for the consumer. If these Loss Ratios were provided to the consumer prior to the sale and on, at least, each annual policy anniversary, the consumer could appropriately assess the value of their coverage. If mandatory approved, standard or prescribed coverages and transparency of Loss Ratios are introduced, competition within the industry will drive insurers to compete on the efficiency and effectiveness of their administration and quality of their customer service delivery. This would seem to be a good thing>

If the Commission would like additional information or clarification of any comments in this submission, please contact me.

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28th October 2018