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Investment and Financial Services Association Cost of Underinsurance Project - Analysis of Life Insurance Needs

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1. Executive Summary

1.1. Background

The Investment and Financial Services Association (IFSA) has engaged Rice Walker Actuaries to carry out an investigation of the issues arising from the life insurance coverage patterns of Australian parents.

More details of our “brief” and the process that we followed are set out in Appendix E.

1.2. Investigations

Using ABS statistics on household expenditure, population census details and deaths, together with details of insurance coverage (from life insurance and superannuation sources) we have estimated:

- The life insurance needs of parents in Australia;
- The amount of underinsurance in this group; and
- The social security costs arising from the underinsurance.

1.3. Conclusions and Recommendations

Our conclusions and recommendations are as follows:

Financial Needs Analysis

The assessment of the needs of average full time workers of **couples** in their mid thirties **with young children** considered in this report indicate life insurance requirements for parents ranging from around **10 times to 13 times their taxable earnings**, depending on the level of their partner’s earnings. For part-time workers, the multiples of taxable earnings are much higher.

For full time workers in their mid forties **with older children**, the range of needs represented **6 to 9 times taxable earnings**.

Insurance “Gap”

For full time workers on average earnings, currently around \$50,000 per year, the range of needs for those with young children has been estimated as **\$500,000 to \$650,000**. This compares with average amounts insured for this group estimated to be of the order of \$70,000 for those with only superannuation cover or over \$400,000 for those with both superannuation and non-superannuation cover.

For those on average earnings with older children the range of needs has been estimated as **\$300,000 to \$450,000**. This compares with average amounts of life insurance for this group estimated to be \$20,000 to \$30,000 less than cover held by the younger persons’ above.

While the averages for amounts of cover in force include individuals without children, the underinsurance “gap” is sufficiently wide for it to be clear that many parents are underinsured.

A broad estimate of the amount of underinsurance for parents in Australia with dependent children is of the order of \$1,370 billion. For those with average levels of superannuation death cover only, the cover held represents less than 20% of average needs.

Social Security Impact

ABS statistics show the current annual rate of deaths of parents with children to be a little over 4,000 (see section 2.2).

In our analysis we have considered the additional social security payments arising from deaths of parents with limited insurance. The additional annual costs have been estimated on broad averages to be of the order of \$250 million.

However, this estimate does not take account of other costs/losses to government revenue such as:

- Provision of housing; and
- Loss of income tax revenue.

Options for Industry/Government

The options available to industry and Government to help to address the degree of underinsurance include:

- Promotion of insurance needs and calculators on the Government “Choice of Fund” websites and the supporting published material. If well-used, even by those changing jobs, this would encourage a better understanding of insurance needs within the community.
- Greater emphasis on insurance education and communications. The emphasis on investment education over the past 10 years has improved public understanding and appreciation of investments. The same opportunity is available for insurance possibly as both a Government and private enterprise initiative.
- Promotion of the additional security provided by insurance (superannuation or other) through material produced by the Department of Family and Community Services and Centrelink.
- Greater emphasis on insurance from mortgage providers at the time that mortgages are taken out or updated.
- Promotion of the financial advantages for the average person of increasing their insurance cover within their superannuation funds (group rates plus tax and underwriting advantages).
- Some Government incentives.

Consumer Research

The needs side of our research has been based on people using their income to support their lifestyle.

The consumer research should consider the actual needs segmented by broad income levels and family structure to take account of issues such as:

- Future family education (school plus university);
- Allowance for improving lifestyle (upgrading mortgages etc);
- Details of other family arrangements such as care for parents and other family members which would be covered by a comprehensive insurance programme;
- The impact of the less stable family structure;
- The different needs and aspirations of the single parent families;
- Attitudes to insurance, both within superannuation and otherwise. This may provide important information on the most effective area of focus for education campaigns;
- The perceived source of expert advice and when it is sought (accountant, financial adviser, mortgage broker, etc);
- The appreciation of the modest level of social security income support compared with the actual cost of maintaining the family lifestyle; and
- The effect of the perceived high commission content in premiums on peoples' buying decisions.