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Guarding your income

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Peter Neilson says the spike in claims is a global problem.

A soft job market and increased layoffs are boosting claims against income protection insurance policies to such an extent, that premium hikes are now being predicted.

A similar pattern has also emerged for trauma protection insurance.

In the December quarter insurance claim statistics from the Financial Services Council, (FSC) the industry body for life insurers, show that for every $100 of income protection insurance, insurers paid out $11. For trauma insurance it was $15.

Both figures were much higher than claim levels 2 years' ago (see table), and insurance broker Tony Vidler said it had become clear that insurers had mispriced risk.

There has been a surge in the uptake of income protection policies, on which we collectively pay premiums of around $270 million a year but, Vidler said, there has been an even higher surge in claims.

"The claims experience for most insurers is that claims are far longer than they would have expected," he said.

FSC chief executive Peter Neilson said that had been happening all around the world, as people who successfully claimed monthly income payments were taking longer to return to work.

Neilson said claimants' average speed of returning to work seemed to be related to the state of the job market.

That had raised eyebrows among the giant international reinsurers, who had made it known that premiums would have to rise if the high levels of claims did not abate.

The story behind the higher than expected claims for trauma insurance, for which we also pay in the region of $270m in premiums each year, was one of policies that paid out too easily, Vidler said.

He believed fierce competition in the insurance market for brokers' business had led to trauma policy definitions being so broad that they pay out too frequently on health events that may feel serious, but are relatively minor.

In some cases it meant a minor heart attack or an early stage prostate cancer, both of which often triggered payouts, and could end up feeling like a lottery win to policyholders whose lives were only modestly interrupted and whose prognosis was for a long and happy life.

While that was not the feeling among trauma policyholders featured in Sunday Star-Times last week who had suffered heart attacks that did not trigger payments, the contracts were still, by international standards, fairly generous in terms of the benefits and the definitions, Vidler said.

He did acknowledge the unhappiness of policyholders, most of whom he felt had virtually zero chance of understanding the policy definitions of some conditions such as heart attacks.

At a recent conference of advisers, he asked around 100 "very well qualified" advisers to explain the meaning of two heart attack definitions from two policies currently on the market.

"Nobody could," he said. "You have to be a cardiologist to understand them correctly."

Vidler believes there are really only two options for the industry on the income protection and trauma policy claims' spikes: Raise prices and/or change policies so they pay out only on the more serious cases.

Neilson said policyholders had been hard hit by rises in premiums on their house and contents insurance following the Christchurch earthquakes, making the prospect of such price rises more unwelcome than at any time he could remember.

"There has never been as much resistance to price increases as there is in the current marketplace."

Vidler said insurers would not allow the current high claims to premium ratio to continue.