Fit for process

Risk advice post-QAR

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The only constant is change

- The only constant in the provision of risk advice is change
- This change has focused primarily on regulation, remuneration, and professional standards
- Compliance is driving the risk advice process, driving the cost to serve up
- In the first half of 2023, only 6,373 financial advisers wrote a risk policy, with fewer than 500 responsible for 50% of all new business

Australia is underinsured

- At the same time risk new business is decreasing, the need for risk advice is accelerating
- Deliotte's 'Mind the Gap' indicated that Australians could have claimed 25 billion
  more in the last year if not for underinsurance (need to provide source)
- It is estimated Australians remain underinsured by up to 60-80% (need to provide source)
- Client's prefer seeking life insurance advice through a financial planner
  – advice can be all encompassing and independent of product

And then there was light…

- And then there was light, in the form of the Quality of Advice Review (QAR)
- The purpose of the QAR is to improve the accessibility and affordability of quality financial advice
- Much of the focus has been in relation to the removal of regulatory red tape, including streamlining fee consent and the divisive Statement of Advice (SOA)
- The provision of advice should prioritise substance over form and focus on the outcome; the advice document should be fit for purpose

Fit for process

- The need for a fit for purpose risk advice document is needed and not up for debate
- What is up for debate are the inputs required in the advice process that form the basis of the advice; with the focus being on appropriate outcomes that are in the best interests of the consumer
- This presentation will focus on these inputs, producing a streamlined, compliant, repeatable risk process that we hope will rekindle your love for risk

Agenda

1. Risk identification & quantification
2. Risk tolerance & capacity to pay
3. Establishing goals and objectives
4. Goals prioritisation matrix
5. Risk transfer/retention & repeat
6. Outcome mapping

Risk identification

- Through an analysis of the client's unique circumstances, risk identification allows the client to understand their risk exposure
- Risk quantification takes this exposure, and expresses it in dollar terms

- There is no ASIC/Code approved approach, rather an industry driven needs calculator that varies practice to practice; common risk considered include:

Risk	Life	TPD	CI
Repay debt	✓	✓	✓
Income replacement	✓	✓	✓
Provision for tax	✓	✓	✗
Children's education	✓	✓	✗
Childcare expenses	✓	✓	✗
Home modifications	✓	✓	✗
Final expenses	✓	✗	✗

Risk quantification

Each identified needs to be quantified; your quantification method should ideally demonstrate how each number has been determined including research/data points

There are some quantum's however that will guided by a best estimate e.g. home modifications, provision for tax

Consideration needs to be given as to how the quanta interact with each other e.g. income replacement

Once you have your risk identification and quantification philosophy settled, you can create a simple calculation tool to run each clients numbers

Establishing goals and objectives

- Your advice needs to address the client's goals and objectives
- It is often the role of the financial adviser to uncover a goal or objective the client didn't know they had
- Where cost is an issue, these goals will need to be prioritised and/or dealt with by means other than insurance
- Risk tolerance will play an important role is addressing each risk e.g., it is more likely to claim on an IP policy than for Life, TPD and Trauma

Insurance appetite & affordability

RISK PROFILE

Risk comfortable

Unconcerned by risk to income – not seeking risk transfer solution.

Balanced

Pragmatic view of risk and necessity of income protection – seeks value.

Product solution provides necessary coverage and minimises present and future financial impact.

Conservative

Limited appetite for risk to income – seeks the most comprehensive solution.

Product solution provides maximum coverage and certainty, prepared to make financial concessions in present and future state.

SOLUTION CONSIDERATIONS

- Nil cost – no insurance
- High risk of income loss if unable to work

- Lower initial cost
- Minimised long term cost
- Reduced risk of premium increase

- High initial cost
- Greater long term cost
- Greater risk of premium increase

INCREASED PRODUCT GENEROSITY COMES AT GREATER COST AND WITH INCREASED UNCERTAINTY OF FUTURE COST

Which risk profile suits your client?

“Client, know thyself”

- Position the Client on the Risk Tolerance Spectrum according to the Client’s perceptions, and not your perceptions
- Positioning Tool has been developed: Series of risk attitude questions with a score allocation for each answer
- We are not pigeonholing the Client. The tool is a stimulus encouraging the Client to consider their position on the Risk Tolerance Spectrum
- Ensure the Clients consider the cost of risk transfer in their positioning deliberations
- Proper positioning on the Risk Tolerance Spectrum empowers the Client to make appropriate risk transfer/retention decisions
- Each Client’s perceptions are unique. Positioning and transfer retention decisions will vary from client to client

Establishing client goals & objectives

Step 1
Articulate goals using a blue sky approach

Step 2
Adjust goals by the Client's risk attitude

Step 3
Complete the goals matrix

Step 4
Resolve any tension between competing needs

Step 5
Ensure that the Client understands the outcome

Articulation (Step 1)

Resolution process (Steps 2–4)

Confirmation (Step 5)

"....a process of not just identifying needs but prioritising those needs to ensure that any tension between competing needs is resolved through discussions with the client"

"The Best Interest Duty does not demand that specific recommendations are made to meet every possible client need"

*direct quotes from AFCA determination 747581

Goals matrix example

Goal	Description	How can I achieve my goal?	What happens on my death or disability?	Priority ranking	Comment
Debt on primary residence	Discharge my mortgage by age 60 or on death or disability. I cannot leave my family without a home on my death	Ensure that I have sufficient superannuation savings to discharge debt	Use my superannuation death benefit to discharge mortgage debt. Use insurance to supplement any shortfall.	1	Important for the family to have a roof over their heads
Child maintenance costs	Provide for my children until age 18, the estimated time of entry into the work force or entry into tertiary education	Use my after tax income to maintain our existing life style	Use my superannuation death benefit to discharge mortgage debt. Use insurance to supplement any shortfall.	3	
Education funding	Provide for the secondary education of my children in Catholic Schools until they reach age 18	Use my after-tax income to fund my children's education	Use insurance to fund ongoing education. Worst case scenario, the children can go to state schools.	2	

Risk identification

Meet David

David is a 50 year old non-smoker and works as an accountant for a large mining house.

David is married to Irene and they have two children aged 15 and 10 respectively.

David's two children attend Catholic Schools and David and his wife want to ensure that the children complete their education in the Catholic system if David suffers premature death or disability.

Salary
$180,000 plus SGC
$18,900 per annum

Mortgage Amount
$500,000

Superannuation balance
$400,000

Other insurances
Income Protection
$4,500 per month.
Aged 65 benefit

Use the risk matrix to identify and quantify the risks confronting David

David risk matrix(1)

Identified Risk	Financial Exposure	Risk Transfer Strategy			Risk Retention	Risk Retention Strategy
		Life	TPD	CI		
Debt on primary residence	$500,000	$500,000	$500,000	$0	$500,000 for trauma	
Child maintenance costs	$192,042	$0	$192,042	$0	$192,042	
Education funding	$152,737	$152,737	$152,737	$0	$152,737 for trauma	
Cash flow replacement	$692,272	$0	$692,272	$0	$692,272 for life and trauma	
Total	**$1,537,051**	**$652,737**	**$1,537,051**	**$0**		

David risk matrix(2)

Identified Risk	Financial Exposure	Risk Transfer Strategy			Risk Retention	Risk Retention Strategy
		Life	TPD	CI		
Total B/F	**$1,537,051**	**$652,737**	**$1,537,051**	**$0**		
Home modification/ medical	$200,000	$0	$200,000	$200,000	$0	
Final expenses	$20,000	$20,000	$0	$0	$0	
Total	$1,757,051	$672,737	$1,737,051	$200,000		
Superannuation	($400,000)	($400,000)	$0	$0	$0	
Existing insurance						
Other assets						
Income protection adjustment	($577,043)		($577,043)			
Total	**$780,008**	**$272,737**	**$1,160,008**	**$200,000**		

Risk retention discussion

- Vital to consider strategies for all retained risks. There needs to be informed consent for all risk retention
- Recording risk retention strategies on the risk matrix are essential

Discussion of David's risk retention choices:

- Debt in the case of trauma risk
- Child maintenance for debt, TPD and trauma risk
- Cash flow replacement for life and trauma risks

Risk adjustment discussion

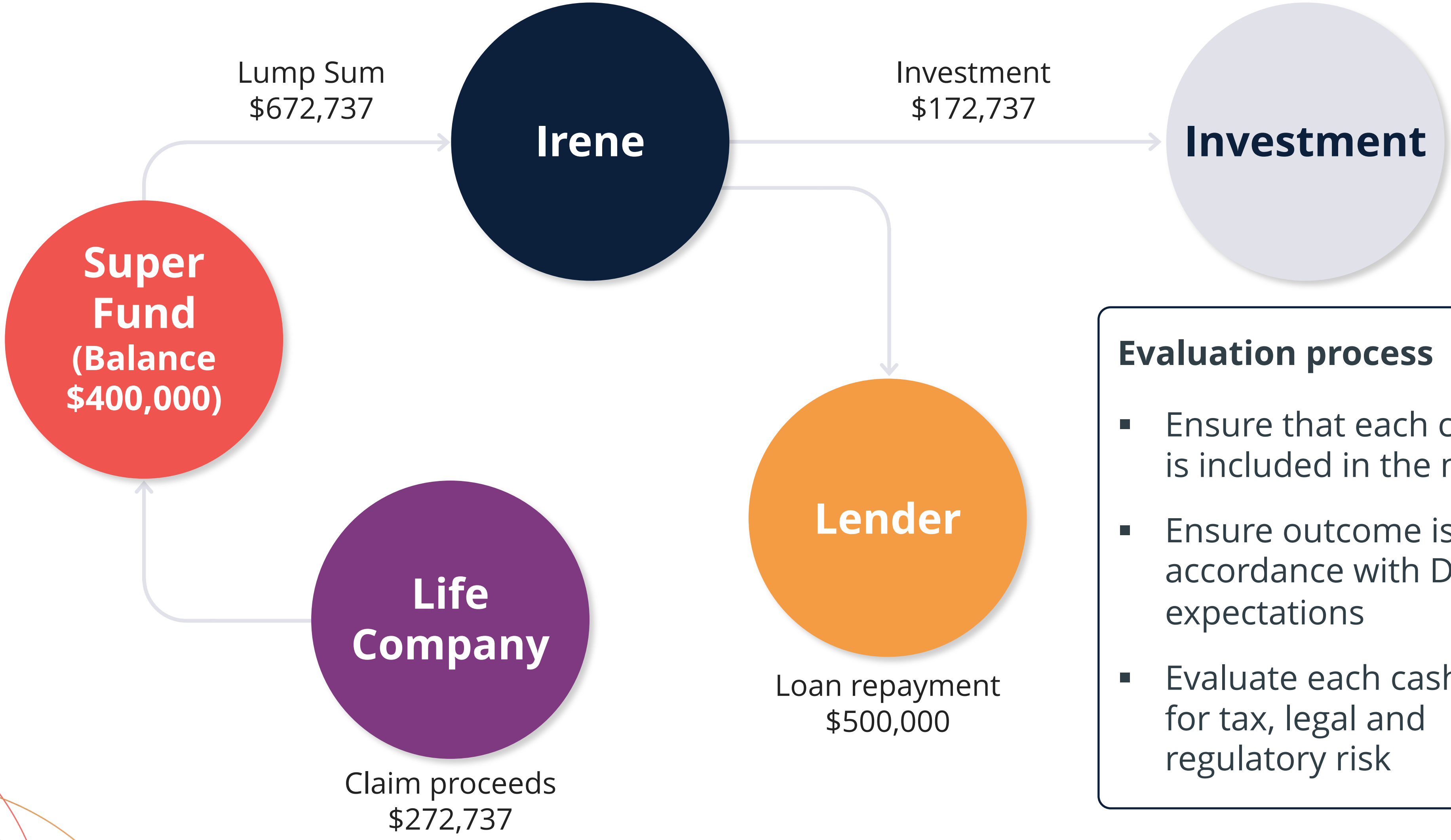
Adjustment for superannuation balances:

- Life Yes
- TPD: No
- Trauma?

Adjustment for income protection

- Life No
- TPD: Yes
- Trauma?

Mapping insurance outcomes for David



Evaluation process

- Ensure that each cash flow is included in the mapping
- Ensure outcome is in accordance with David's expectations
- Evaluate each cash flow for tax, legal and regulatory risk

Q&A

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