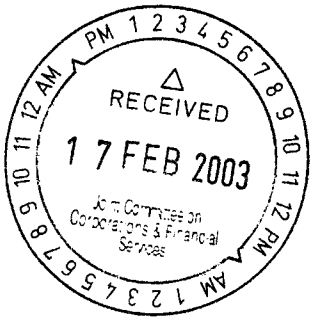

SUBMISSION

TO

PARLIAMENTARY JOINT COMMITTEE

ON

CORPORATIONS & FINANCIAL SERVICES

W.A. Brown

February 2003

17 February 2003

The Secretary
Parliamentary Joint Committee on Corporations
& Financial Services
The Senate
Parliament House
CANBERRA ACT 2600

Dear Kathleen,

I understand your committee will shortly be conducting an enquiry into the issue of whether or not advisers should be required to disclose commissions on life risk insurance products.

My submission on this matter is attached and I would be happy to attend a committee hearing and talk to my submission.

Briefly, my background is as follows.

- I am a life insurance adviser of 15 years continuous experience.
- I have advised as a tied agent for one year, a multi-agent for 10 years, and a registered life broker for 4 years.
- I hold an ASIC registration as a life insurance broker.
- I hold a current PS146 certificate.
- I do not hold a Proper Authority which would entitle me to provide securities advice (a so-called "financial planner").
- I hold life brokerage agreements with 12 Australian-registered life offices. I intend to apply for an FSR licence in late 2003.
- I have obtained qualifications for every life insurance training course offered by my professional association, the Association of Financial Advisers. I am an Accredited Fellow of that Association.
- I have some 950 clients in a predominantly risk-based client base.
- I provide ongoing program reviews to my clients. **This program is threatened by the anti-hawking provisions of FSR.**
- I employ one full-time support staff member and operate from leased commercial premises.
- I publish a bi-annual newsletter for all clients.
- **I currently have at least eight ongoing income protection claims which require constant monitoring and intervention.**
- **I receive no remuneration from either clients or insurers to compensate me for the time I spend on claims.** Four of these claims are long-term and **may require supervision and monitoring for 20 years.**
- My business is not owned (wholly or partially), or controlled, by any life office or fund manager.

Yours faithfully,

BILL BROWN, FALA

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EXECUTIVE SUMMARY

The arguments contained in this submission are, of necessity, complex and detailed.

I would prefer the Members of the Committee were made aware of the reasons behind my recommendations. Reluctantly, I have decided to provide the following summary.

- Commission disclosure on Life Risk products is *complex, difficult to explain* to the consumer, and ultimately *misleading* to the consumer.

- Unlike investment products, the amount of commission paid on a life risk product can never affect the end benefit. A widow will still receive the same insurance benefit, and the insured will still receive the same income protection benefit, *notwithstanding the amount of commission paid.*

- The purchasing consumer consistently tells life risk advisers that they are *NOT interested* in how much commission is paid, or may be paid, to the adviser on the sale of life risk products. Consumers already know commission is paid on life risk sales, and they also know there will never be any fees charged for associated services they may require in the future.

- Life offices will take advantage of the perceived (by them) inability of life risk advisers to justify up-front commissions to introduce LEVEL COMMISSIONS. Level commissions are, in my view, anti-consumer.

- If the legislators were serious, they would take the obvious course of action – require *standard commissions* across all companies and product ranges.

- If Disclosure of Risk Commission is to stay, then the Disclosure Rules must also apply to LICENSEES, who retain 15-25% of the commission notionally paid to the adviser on life risk products.

- The change of the basis of advice to "reasonable" under FSR will ensure that advisers must use research programs in their recommendation process, and provide explanations as to why one product is better than another. This alone will largely reduce the limited amount of advisers who, it could be argued, are influenced by commission alone.

- ASIC should be required to recognize that *life risk advisers* are an important and integral part of the financial services industry, and require different policy imperatives to those of financial planners, who primarily sell investment products.

PROPOSED DISCLOSURE OF LIFE RISK COMMISSIONS

The purpose of this submission is to present an argument that the proposed requirement for the disclosure on life risk commissions will be unnecessary as well as misleading and confusing for the purchasers of life risk insurance products.

PART A - A BRIEF HISTORY & BACKGROUND

The old adage that life insurance is not bought, but sold, remains as true today as it was 150 years ago.

Likewise the business model used by life offices to pay for the acquisition of new business has rarely changed – a commission payable to a non-employed or associated person, based on a percentage of the premium paid remains the only choice.

Life offices over the years have attempted alternative business distribution models – all have failed. Direct marketing response rates remain static at 1%, and all attempts at employing salaried sales forces to generate new life risk business have failed - most recently with AMP.

Basis of Commission on Life Risk

Commission on life risk business is normally paid on an up-front basis, calculated as a percentage of the first year's risk premium, net of policy fees and stamp duty. If the policy continues in force, an ongoing renewal commission is paid of up to 10%, based on the new net annual premium, as revised. Level commission options are sometimes offered, but traditionally have remained un-attractive to all but the most established business. In an industry where adviser numbers are rapidly decreasing, an introduction of compulsory level commission would result in less volumes of new business.

Under the commission for new business system, the adviser bears all the risk. New clients are constantly needed, but are hard to find. The adviser will probably interview 10 prospects to make 2 sales, with premiums from as little as $200 p.a., but the commission associated with the sale would be lost if the client cancels the policy within the responsibility period.

It is, by any standard, a feudal system, it's not perfect, but it is proven.

Commission on Life Investment Premiums

Some years ago commission disclosure on life ***investment products*** *was made* ***compulsory***. This was a significant benefit to consumers, because it showed the investor how much the investment, and the end benefit, would be reduced by the impact of commission paid to the adviser. (However the *fund manager* still is not required to specifically state their earnings from the sale.) Disclosure of investment commission was needed – because it directly affected the client's end benefit.

Most importantly, the disclosure required was simple and meaningful.

Fees v. Commission

ACA and other bodies constantly advocate fee-for-service as an alternative to commission, usually using the accountant model as an example of how advisers should operate. Accountants of course practice in a *compulsory environment* – everyone has to do a Tax Return annually but *few people are compelled to purchase life insurance.* Accountants charge fees for everything they do for and on behalf of the client, whether or not the client benefits, and the fees, which can range from reasonable to excessive, are normally based on the length of time taken to perform the task and the degree of complexity involved in the task.

However, if a client leaves an accounting practice in the first one or two years, fees are still payable by the client for work done (whether successful or not) and only fees payable for future work are foregone. (The insurance adviser, on the other hand, may suffer a claw-back of commission.)

As accountants themselves have discovered, merely referring a client to an insurance adviser (in-house or external) does not necessarily result in a sale, as insurance will still have to be *sold.* Their limited experience is that much time will be wasted for little resulting insurance business, and accountants have also discovered that if they charge a fee for insurance advice while rebating commissions (but never the production bonuses) the accountant's business loses money because the cost of the wages to the insurance adviser, together with cost of back office services, exceeds the fee income that can be reasonably charged.

Furthermore, should an insurance claim arise, accountants have realized it is not morally justifiable to charge a client a fee for *administering the claim* and representing the client in any claims dispute. This is, of course, opposite to the situation where an accountant charges a client for work done in association with a *Tax Audit.*

Then there is the issue of what is a fair hourly rate for an insurance adviser. Consumer groups often argue that the adviser should charge an hourly rate, but somehow think it should be less than that charged by accountants. *However the adviser still carries a risk if he charges a fee and rebates commission because the life office can still claw back commission if the policy lapses.*

Salaried Advisers v. Commission Based Advisers

Australian banks conduct a business model where bank-owned life offices run seamlessly alongside the lending institution – in the minds of the public and consumers they are one entity, and the banks make only token efforts to disabuse the customer of this impression, as it heightens a feeling of comfort and security.

Banks employ so-called "**salaried**" advisers to sell life risk products to customers who have recently taken out loans or made investments etc.

For many years, bank staff, in their conversations with consumers, have insinuated that because their advisers are paid salaries, and not commissions, that in some way the client was better off. A few years ago, ASIC obtained an enforceable undertaking from a major bank preventing them from describing their financial planners as salaried when in fact the salary was substantiated on a quarterly basis by notional commission based on sales of life risk products and, primarily, investment products.

The proposed commission disclosure rules on life risk products will cause problems for commission based advisers running small businesses when they are in direct competition with a bank adviser. The proposed insured will on one hand believe they are meeting someone from a bank who they believe is not performance orientated, while the self-employed adviser will be forced to disclose commission in gross terms without allowances for the cost of his services and running his business.

An additional complication is that we now have two banks who recently purchased life offices and now sell those life office risk products in their bank offices. That same product, with an identical premium, will have two differing levels of commission disclosed, depending on the status of the adviser.

Such a situation could result in the demise of locally-based advisers, particularly in country towns, and the high standard of service such advisers provide. Bank advisers are not permitted to form ongoing relationships with their customers, and provide no ongoing service and cannot be involved in claims disputes. All service queries and claims matters are referred to nameless people in call centers, who have little training and lack product knowledge.

And we only have to read the recent ACA survey of financial planners to know that bank advisers lead the pack in poor quality advice.

<u>Increasing Service Demands on Advisers</u>

There are two new factors which are currently impacting on current and the future profitability of a life risk business

- Increased involvement in underwriting
- Increased involvement in claims

Around 90% of life offices now require proposals for income protection insurance for self-employed people to be accompanied by financial evidence and confirming accountant's statements. This requirement has added additional workloads for the life risk adviser because he, and the client, are now dependent on an accountant to support a proposal. *The adviser receives no commission until the policy is issued, and the completion process may take months, and be further hindered by delays in obtaining medical reports.*

Claims Handling

Recent industry experience is that insurers are attempting to control costs by delaying or denying income protection claims and this is particularly noticeable where a life office is for sale or being prepared for a public float. Life risk advisers who are currently agents are generally contractually prevented from representing clients in income protection and other claims disputes. On the other hand, life brokers/dealers, who legally represent the client, can legally intervene in claims and are expected by the consumer to do so.

After 2004, all advisers as brokers representatives will be able to intervene in claims on client's behalf. However, if the intervention starts to take up time (and it is more so) the brokers/dealers and their representatives have a stark choice – charge a fee to someone in financial difficulties, or do the work for nothing. Claims involvement can go on for months, or even years and is emotionally draining on both client and adviser.

This is a difficult and complex ethical question because it involves seeking fees from a client at the hour of need. Every adviser who sells an income protection product knows full well that only a small percentage of policies sold will ever involve a claim of any sort but an experienced adviser also knows that some of those claims will take a considerable and disproportionate amount of time to resolve.

PART B

PROPOSED DISCLOSURE REGIME

Introduction

ASIC has issued guidelines on the FSR requirements for disclosure of commissions on the sale of life risk products.

ASIC, when pressed to provide detail of what disclosure actually means, intones the following

> "Generally we consider **any benefit** (including a commission received) ..... might reasonably be expected to be capable of influencing the providing entity in providing that advice".

Clearly, the underlying assumption here is that life risk advisers will always opt for the product which pays the higher commission and benefits.

This attitude fails to note the increasing professionalism and sophistication of life risk advisers in today's market place. (The same cannot be said of Financial Planners as evidenced by the recent survey.) While it is true that there is the odd dinosaur who would fit this description, these people will be out of the industry soon (primarily because of age) and if they stay, their training requirements and the requirements of using a research program provided by their new licensee to justify their sales recommendations under FSR will eliminate them more efficiently than commission disclosure.

Legislators and regulators should also note that there still are life offices who offer higher then what is considered "standard" commissions – *but the spotlight seems to have gone past the life offices and now focuses on those who choose to take those commission options.*

An observer, innocent to the complexities of the minds of legislators and regulators, may wonder why the obvious has not been implemented – *a standardized rate for life risk commissions across all companies.* Then only the premiums will be different.

The Realities of Commission Disclosure

ASIC, when asked to explain exactly how commission (life risk) disclosure would work in an interview situation resorts to their usual response – "we don't give advice, you should seek legal advice". Once again this position favours the "big end of town" who can afford expensive "top six" lawyers to obtain an opinion on what the legislation means.

As it stands, it appears that the following must be disclosed.

- **How much first year commission is paid in dollar terms.** This involves explaining that some companies pay commission on stamp duty and/or policy fees and others don't, as well as what is "net annualized premium" on which commission is based. Two companies pay commission on the monthly premium (which includes a model loading) which further distorts the comparison.

- **What is the dollar term value of production bonuses paid over and above the agreed commission rate.** This varies from producer to producer and from life office to life office, and may (yet again) be varied by the life office in a production year as an incentive to encourage greater use of that company's products. *Many bonuses are constantly reviewed on an historic twelve-month rolling basis.* At best, the adviser may not know his production bonus rate (if any) at the time of sale, and may inadvertently mislead the consumer, and attract penalties.

- **Dollar value of so-called soft options.** The mind boggles – does this include the logo-branded pens and notepads handed out at seminars; the transport/accommodation packages paid to successful producers to attend conferences and tell their stories. Both ASIC and Treasury have declined to disclose their meaning of the word "**influence**".

  Life Brokers have never received free trips, but *agents still do.* After 2004, agents will belong to the past, and licensees will not have the dollars to splash around on such rewards. Does this mean I have to disclose in dollar terms and value of the Chinese lunch I received from the Business Development Manager who visited me last month and whose company product I may recommend but only if it meets the client's needs?

Such a disclosure requirement is complex, time consuming, misleading and of little value to the consumer in their primary objective of receiving advice on life risk products to allow them to make an informed choice.

Developments as a Result of New Disclosure Requirements

With the announcement of the requirement to disclose risk commission, some life offices have been busy.

Let us pick out just one company, which pays a life risk commission at 95% of the net annual premium on an up-front basis is now offering an alternative commission structure, which if nothing else, will complicate an already complex explanation, as outlined above.

The commission alternatives for income protection sales would look like this:

	1st Year	*2nd Year*	*3rd & Ongoing Year*
Up-front Comm.	95%	5%	5%
Level Comm.	66%	27.5%	27.5%

Clearly the adviser who chooses the up-front commission option will be at a serious disadvantage ***in the eyes of a consumer*** *who subsequently seeks a second opinion and visits another adviser who recommends the identical product but, knowing he is in competition, chooses the Level Commission option to gain an advantage.*

Only an extremely complex explanation to the consumer of how the level commission pays more after three years can save the adviser who opts for up-front commission option because of his business model. **More than likely the sale will be lost, probably to both advisers**, and another dependent will be burdened on the tax payer.

This confusion is not "the market at work", it's market lunacy. In addition, level commission distorts the adviser market because it favours the adviser with the longer established and sustainable business and if level commission were universal, such a change would prevent new small business advisers from entering the life risk market. This will result in even fewer new entrants to what is, because of age, a rapidly decreasing adviser force.

It is noted that of those few **financial planners** who sell life risk products, most opt to use small life offices who pay level commission only. The obvious conclusion must be that the planners find it easier to disclose, but it is doubtful if the ongoing revenue is stated.

Level commission is, in effect, anti-consumer. This is because the adviser, who should review the suitability of the product every one or two years, is now biased to keep the policy in place for at least three years, until he receives commission equivalent to the up-front option. The client will not know this, and will be disadvantaged in that he may not be advised of better, if not cheaper, products on the adviser's recommended list.

The end game of this madness is that small business advisers will desert the industry and consumers will be forced to deal with the large institution-owned adviser companies, and the big end of town wins again.

Why Not "Licensee" Disclosure

Attachment 'C' shows the calculation of first year commission (FYC) on the sale of an income protection benefit.

The spreadsheet also shows that between 15 and 25% of the commission paid by the life office will remain in the hands of the licensee responsible for the adviser, who incidentally, will not usually be physically co-located with the licensee but

conducting his own small business in a separate location, if not another part of the state.

ASIC seems to have decided licensees are not part of the life risk disclosure regime. (This is very curious given that the **adviser does not hold agreements** with the life office – the **licensee** does.) This lack of compulsion on licensees to disclose life risk commission is however consistent with the Investment Disclosure rules where the CIB discloses the total entry fee, the commission that may be paid to the adviser, but NEVER discloses what is **kept by the fund manager** out of the total entry fee.

As a result of the agreements which will be entered into between licensees and risk advisers under FSR, ALL commissions are first paid to *the licensee*, who then deducts the agreed 15-25% and *forwards the remainder to the adviser*, who holds the client file and the customer relationship, **but not the legal right to the client ownership**.

Under the ASIC model, the adviser is responsible for disclosing commission he does not receive.

Secondly, the adviser will never be made aware by the licensee (or the life office) of the secret production bonuses and profit share allowances paid to a large licensee by a grateful life office.

Thirdly, the adviser will never be made aware of other incentives paid to his licensee if the business of his licensee is owned (partially or wholly) or otherwise controlled by a life office to encourage the licensee to promote that particular life office products over those of other life offices the licensee is able to offer.

How can an adviser be required to disclose what he does not know?

PART C – WHY COMMISSION IS NOT AN ISSUE WITH MY CLIENTS

Advising Methodology Model for Life Risk products

For the last fourteen years, I have used a particular methodology to provide advice to clients wishing to purchase Income Protection, Trauma and Term Life products – refer Attachment A.

The methodology requires firstly a complete analysis of the client's situation and their needs which, as you know, is now a requirement formally codified under FSR, but I would argue that most competent life risk insurance advisers who run their own businesses have been utilizing this procedure all their practitioner years.

After the needs analysis stage, the next step is to examine the contracts available to the adviser and, by a process of elimination, de-select those contracts that do not meet the stated needs and objectives of the client or contain particularly targeted restrictions. *In this example, you will note that only two company's products emerge as a solution.*

This is a complex and detailed process, equal in complexity to any process an adviser might do to prepare a plan for investment of monies. At the end of the process however, it is always the client's choice, based on information and advice provided by an appropriately trained adviser. If the client acts contrary to the adviser's recommendations, file notes, including the Customer Advice Record, will record the process.

The methodology set out in Attachments A, B and C relies on detailed knowledge of the various definitions and clauses in Income Protection contracts and requires the use of an appropriate and independent research product program. It also assumes a comprehensive knowledge by the adviser of *all income protection products per se* and not just knowledge of those contracts the adviser is able to sell, *because replacement of existing contracts may be recommended.*

I began using this method when I became a multi-agent in early 1989 after completing the Disability Income course offered by the then Australian Lifewriters Association (now the AFA). The course was completely updated in the early 90's and I took the opportunity to re-do the course (now the **Income Protection** course) at that time as well as to make myself available to moderate two such courses held in Canberra. *Please note – the Diploma of Financial Planning Unit on Life Insurance as offered by the Financial Planning Association does not provide this level of knowledge.*

In this method, premium is rarely an issue – once a client can compare premiums across the market and then compares the advantages of a particular contract over another, the choice is no longer commodity-based, as would be the case with a (say) simple Term Life (Death only) sale.

If premium is not an issue for the client, then neither is commission because all clients understand commission is paid as a percentage of premium.

Using this procedure, refined over the years by the addition of a number of explanatory diagrams that I have developed, *I have had no more than 5 requests from clients to provide details of the commission I earn from the sale of the recommended product* in the 14 years that I have used this process – **commission is just not an issue for the client because the clients can see the differences in the contracts and the value of those differences to them and therefore perceives that "bias" does not exist.** (Please note that neither ASIC, Treasury or ACA have ever defined "bias" in this context.) *The client is also aware that the adviser is running a business and therefore needs to be remunerated appropriately for advice, ongoing service, and claims handling assistance,* all of which is explained at interview.

Attachment 'C' is a spreadsheet showing the actual commission paid to a **life broker** for an **income protection policy** at today's rates, with commission shown as being payable on an up-front first-year only basis. Some points to note

- Commission for income protection policies in the hand of the adviser ranges from 61% to 75% of the premium paid by the client
- This commission payable is usually based on an underlying assumption by the life office that the *policy will remain in force for ten years*, and that the adviser will be expected to service that client (offer services, policy maintenance) for that time
- Most agency agreements forbid agents becoming active in dealing with their clients' claims on the life office. (Agents after all, represent the life office.) Brokers on the other hand are legally able to represent clients in claims. Brokers representatives will receive no additional remuneration to handle claims
- The new disclosure rules do not require the broker/dealer to disclose to the client that the broker/dealer, to whom all commissions are paid, will deduct a fee of up to 25% (depending on the cost of Professional Indemnity insurance).

  The broker's representative/adviser is thus required to explain remuneration he does not receive.

- Average income protection premium in most risk advisory businesses would be approximately $900 p.a.
- **If the policy fails to remain in force for 1 or 2 years, all or part of the commission is claimed back by the life office.** The adviser receives no other remuneration.

ATTACHMENT 'A'

WHY COMMISSION IS IRRELEVANT

Client – Ms Sue Sample

Relevant Facts

- Client is a 36 n.b. female, smoker, Computer Professional with degree, married with one child – she generates $120,000 p.a. net of expenses
- She indicates she may go overseas to work for a year or more if IT contracts are on offer
- At any particular time, she may have readily accessible savings of approx. $5,000
- She may have another child in next two years. Her husband is on leave raising their first child
- She has been self-employed in her own company (sole director) for less than 2 years. She favours short-term work contracts because of the flexibility offered, and her current contract expires in two months
- Ms Sample agrees that she is highly motivated to work for both financial, professional and contractual reasons. She would prefer to work than be sick at home
- It is important to Ms Sample that she protects current and future lifestyle
- Ms Sample indicates that she has had a 2 month episode of reactive depression just on 2 years ago – she took anti-depressant medication for 2 months, and was off work for two weeks.
- She advises that her existing Life/Trauma cover is adequate, and therefore she only seeks advice on Income Protection, which she has been unable to obtain in the past.

Particular Needs Revealed After Receiving Advice

- She must insure herself to the maximum benefit available – she and her partner have a mortgage and negatively geared investments with total debts of $500,000, and she is currently the sole earner in the family
- My recommendation will be for the maximum benefit of $7,500 per month, indexed to CPI, Waiting Period 30 days, Benefit period Age 65
- Ms Sample wants to be covered for disability arising from pregnancy, if at all possible
- She seeks a contract with no overseas travel or residence restrictions which would prevent payment of benefits while Disabled and living overseas, as she may take short term overseas contracts
- She seeks an Agreed Value policy, with the indexation of Monthly Benefit guaranteed in the contract. She will not accept an Indemnity contract
- Ms Sample now understands value of benefits payable in the Waiting Period. She indicates that she needs to be paid from Day 1 of Disability if she suffers a broken bone or is diagnosed with a critical illness

- As her duties do not require use of tools, machinery or vehicles (other than for commuting), she has accepted that she does not require an Accident Benefit in her policy (this will result in a premium saving)
- Upon receiving advice on the differences between a base level contract and a professional-level contract, she advises she prefers the professional level contract
- Ms Sample prefers an income protection policy which does not require her to be Totally Disabled for any fixed number of days in the 30 day Waiting Period, in order to receive Partial Disability benefits from Day 31
- Because of her previous experience seeking Income protection, Ms Sample will not accept "non-standard" exclusions on policy, and consequently the policy must cover all sicknesses
- Because of the small possibility of gaps between work contracts, she insists that her policy not be able to be cancelled by the insurer in the event of ceasing work before retirement age
- After viewing an explanatory diagram, she has indicated she prefers to be able to "lock in" good years of earnings for purposes of calculation of Partial Disability benefits. As a minimum requirement, she must be able to "lock in" earnings from the year immediately preceding Policy Start Date, which she indicates has been a good year, earnings wise
- She requires a policy which will reduce benefits payable (offsets clause) only where workers compensation benefits are received, and preferably with no offsets.

Basic Process of Selection of Income Protection Contracts

Attachment B lists those "professional" level income protection contracts which have been de-selected from the list of Income Protection contracts available from life offices for which the broker has agreements.

At the end of this first stage of contract selection, only the following Income Protection contract still meets **all the *contract criteria*** (only) as specified by the client.

Plan from Company 'D' **$3,022.54 p.a.**

Fine Tuning of the Contract Selection

At this stage, I would again ask the client for her views on certain additional key areas in order to further refine my recommendation given that the contract from Company 'I' has only failed on one contract criteria (disability from pregnancy) and is similar in all other **contract criteria,** for the following reasons:

(i) There is a subjective argument that the definition of stroke in the Company 'D' contract, which underpins the payment of a Critical Conditions benefit in the Waiting Period, is more restrictive than the stroke definition found in the Company 'I' contract

(ii) Company 'D' underwriting may impose a temporary "Proof of Earnings" clause on the policy because the client does not have sufficient experience as a self-employed contractor, in terms of their current underwriting

guidelines. Company 'D's underwriters will usually insist on an accountant's statement covering two years to prove income at proposal, while Company 'I' underwriters will not. Obtaining accountant's statements is a difficult and time-consuming process as accountants are under pressure from work associated with the GST and may resist presenting the information in a form favouring the insured, rather than merely providing a tax return. While the underwriters wait for the accountant, there will be no cover for sickness.

(iii) In pre-proposal (no names) discussions with the underwriters of Company 'D', it has been indicated that the recent episode of depression would, depending on doctors report, result in the application possibly receiving a loading (more premium), an exclusion or even a refusal. However the underwriters at Company 'I' have advised that, subject to medical report confirmation of the facts disclosed by Ms Sample, the depression issue would not attract a penalty

(iv) Company 'I's coverage of disability arising from pregnancy is much more restrictive than that found in the Company 'D' policy

(v) **Other than these underwriting and contractual issues, the contracts are similar in structure, level and range of benefits and quality of definitions.**

To further define the advice being provided, I would then seek input from the client if she had any concerns with matters (i) to (iv). If she did not object, and she was prepared to take a chance with Company 'D's underwriting regarding the episode of reactive depression, I would recommend the Company 'D' Plan because of the superior treatment of Disability arising from pregnancy.

However, if she was prepared to, on balance, overlook the more restrictive Company 'I' treatment of disability arising from pregnancy, in preference with a more certain outcome from Company 'I' on the depression issue, I would recommend the Company 'I' contract.

Effect of Requirement to Disclose Commission

If there is a requirement to disclose life risk commission, the client would be confronted by the following dilemma:

Company 'D's contract (Recommended)	
Premium	$2,694.69 p.a. – Tax deductible
First Year Commission to Representative	**$1,813.14**
Company 'I's contract (Highly recommended)	
Premium	$3,336.11 p.a. – Tax deductible
First Year Commission to Representative	**$2,218.08**

My professional advice to Ms Sample would be that the product of Company 'I' is, on balance, more suitable to her needs, based on a reasonable assessment of her situation, for the following reasons.

- Possibility of an unfavourable underwriting decision from Company 'D'
- Company 'D' would likely impose a "temporary" Proof of Earnings Clause for the first year of the contract.

  (This clause is removable upon demonstration of earnings in a year's time, but, *if Ms Sample's health changes in the meantime*, (e.g. a reoccurrence of the depression), **the clause <u>will not</u> be removed, and may remain for the life of the contract.**)

- The definition of stroke in the contract from Company 'I' is, by any reasonable standard, less restrictive than that found in Company 'D's contract.

  (If Ms Sample suffered a stroke as defined in the policy, but was only actually Disabled for a short time she may not receive as much (presumptive) Monthly Benefit in total from Company 'D' as she would from Company 'I' under the provisions of the Critical Conditions Benefit.)

- I would argue that these above three reasons may cancel out the superiority of the provision of benefits if pregnancy results in disability in Company 'D's product, but the final decision is for the client, and would be appropriately notated.

If Ms Sample is influenced by the disclosure of the amount of commission I will receive, she could end up with the wrong contract for her particular needs.

ATTACHMENT 'B'

REASONS FOR DE-SELECTION OF CONTRACTS

The following policies are regarded as fully featured "professional" level Agreed Value income protection contracts and are normally considered suitable for IT contractors. "Indemnity" style contracts have not, and would not be considered, if "Agreed Value" contracts were available.

Company A

* Policy restricts payment of benefits outside Australia/N.Z.
* Policy does not automatically guarantee to pay indexation increases made to the original Monthly Benefit since policy inception
* Current underwriting practices would result in decline of application because of recent proximity of reactive depression
* Possibility of reduction of available Monthly Benefit at the underwriting stage because she is unable to prove income for last two financial years as self-employed person
* Policy can be cancelled after 12 months non-employment
* Claimants for Schedule Injuries and Crisis Benefits must be disabled for length of the Waiting Period
* Offsets clause excludes monies from every imaginable source
* Pre-Disability earnings restricted to 3 years before Disability, therefore does not "lock-in" earnings in year before Policy Start Date.
* Insured must be Totally Disabled for 14 days in the Waiting Period to be paid Partial Disability benefits from day 31.

Company B

* Disability as result of pregnancy not covered unless "complicated"
* Policy can be cancelled after 12 months non-employment
* Offset clause reduces benefits for monies received from sources other than Workers Compensation.
* Insured must be Totally Disabled in the Waiting Period for 14 consecutive days to be paid Partial Disability benefits from day 31

Company C

* Regardless of Benefit Period, policy **restricts benefits to 2 years maximum** if claimant suffers from chronic fatigue syndrome, fibromyalgia, alcohol or substance abuse or dependency, or any mental nervous or stress disorder
* Current underwriting practices would result in decline of application because of recent proximity of reactive depression
* Pre-Disability earnings restricted to 3 years before Disability, therefore does not "lock-in" earnings in year before Policy Start Date.
* Offset clause reduces benefits for monies received from sources other than Workers Compensation.

* Disability as result of pregnancy not covered unless "complicated"
* Insured must be Totally Disabled in the Waiting Period for 14 consecutive days to be paid Partial Disability benefits from day 31

Company D

Not De-selected (Meets All of Client's criteria)

Company E

* Disability as result of pregnancy not covered unless "complicated"
* Policy can be cancelled after 12 months non-employment
* Offset clause reduces benefits for monies received from sources other than Workers Compensation.
* Benefits payable in Waiting Period for Critical Conditions, while paid at twice the normal rate, are only paid if Disabled
* Pre-Disability earnings restricted to 3 years before Disability, therefore does not "lock-in" earnings in year before Policy Start Date.
* Insured must be Totally Disabled in the Waiting Period for 14 consecutive days to be paid Partial Disability benefits from day 31

Company F

* Current underwriting practices would result in decline of application because of recent proximity of reactive depression
* Possibility of reduction of available Monthly Benefit at the underwriting stage because she is unable to prove income for last two financial years as self-employed person. Full set of financial statements required with application.
* Policy can be cancelled after 12 months non-employment
* Policy specifically excludes the earnings of the year immediately prior to Policy Start Date for purposes of calculating Pre-Disability Income
* Offset clause reduces benefits for monies received from sources other than Workers Compensation.
* Insured must be Totally Disabled in Waiting Period for 7 out of any 12 days to be paid Partial Disability benefits from day 31

Company G

* Offset clause reduces benefits for monies received from sources other than Workers Compensation. Unlike standard offset clauses, this company's offset does not apply to the larger of Monthly Benefit or Pre-Disability Income, but only Pre-Disability Income. Where client has experienced a number of years of declining income, this could be a serious advantage
* Offset clause reduces benefits for monies received from sources other than Workers Compensation.
* Disability as result of pregnancy not covered unless "complicated"
* Pre-Disability earnings restricted to 3 years before Disability, therefore does not "lock-in" earnings in year before Policy Start Date.
* Insured must be Totally Disabled in the Waiting Period for 14 consecutive days to be paid Partial Disability benefits from day 31

ATTACHMENT "C"

GROSS LIFE RISK BROKERAGE PAYABLE TO LIFE INSURANCE BROKERS & AUTHORISED REPRESENTATIVES

Commission Payable Based on Premiums Quoted in Life Research Report Dated 13 Feb 2003

Policy Parameters

Female, IT contractor(qualified), 35nb,smoker, Net Personal Exertion Earnings $120,000pa

Waiting Period - 30 days *Monthly Benefit - $7500(cpi)* *Benefit Period - Age 65*

Listed in Ascending Premium Order

Life Office	Base Insurance Premium	Stamp Duty	Policy Fee	**Total Client Premium**	**Commission Based On This Amount**	Brokerage Rate(%) Payable	Gross Comm Paid To Broker Firm	Broker Service Fee(%)	**Gross Comm Paid to Auth Rep**	Gross Auth Rep Comm as % of Prem
A	$1,842.75	$191.14	$68.60	**$2,102.49**	$1,842.75	95	$1,750.61	20	$1,400.49	**67**
B	$2,221.03	$230.61	$85.00	**$2,536.64**	$2,221.03	95.14	$2,113.09	20	$1,690.47	**67**
C	$2,381.17	$243.82	$57.00	**$2,681.99**	$2,438.17	91	$2,218.73	20	$1,774.99	**66**
D	$2,385.71	$244.98	$64.00	**$2,694.69**	$2,385.71	95	$2,266.42	20	$1,813.14	**67**
E	$2,397.45	$245.85	$61.02	**$2,704.32**	$2,458.47	91	$2,237.21	20	$1,789.77	**66**
F	$2,585.23	$264.15	$56.20	**$2,905.58**	$2,641.43	83.25	$2,198.99	20	$1,759.19	**61**
G	$2,745.90	$282.09	$75.00	**$3,102.99**	$2,820.90	100	$2,820.90	20	$2,256.72	**73**
H	$2,918.53	$298.19	$63.33	**$3,280.05**	$2,918.53	95	$2,772.60	20	$2,218.08	**68**
I	$2,982.84	$303.27	$50.00	**$3,336.11**	$3,032.84	103	$3,123.83	20	$2,499.06	**75**

Note

* **Broker Service Fee, under current proposal for disclosure, will not be required to be disclosed by Broker/Dealer, who has no relationship with the client.**
* Commission does not include GST
* Broker Service Fee, which will be payable by non-licencees, may vary (15% to 25 %) on an individual broker's rep basis.
* Commision is on standard Up-front basis - some companies may offer level commission
* Brokerage Agreement detirmines if commission is paid on Policy Fees
* A Renewal Commission may be paid while the policy remains in force, in a range of 4% to 10% of Annual Renewing Premium.
* **ALL COMMISSION RATES CAN BE VARIED BY THE INSURER ON 7 DAYS NOTICE**

Company H

* Policy does not automatically guarantee to pay indexation increases to original Monthly Benefit
* Disability as result of pregnancy not covered unless "complicated"
* Pre-Disability earnings restricted to 3 years before Disability, therefore does not "lock-in" earnings in year before Policy Start Date.
* Offset clause reduces benefits for monies received from sources other than Workers Compensation.
* Policy can be cancelled after 12 months non-employment
* Policy requires that, for benefits to be continued to be paid while overseas, insured must have a medical examination every 12 months in Australia (i.e. return to Australia) or if an overseas doctor, only if approved by Zurich
* Policy has no Critical Conditions Benefit payable
* Insured must be Totally Disabled in the Waiting Period for 14 consecutive days to be paid Partial Disability benefits from day 31

Company I

* Disability as result of pregnancy not covered unless "complicated"

Not De-selected (Meets majority of Client's criteria)