ASIC

Australian Securities & Investments Commission

REPORT 454

Funeral insurance: A snapshot

October 2015

About this report

This report is for providers of funeral insurance products, consumers of these products and other interested parties (e.g. consumer agencies and advocacy groups).

It gives a snapshot of the funeral insurance market in Australia in 2013 and 2014, describing common features of policies and providing data about sales, claims and cancellations to better understand the benefits and risks associated with these products.

It also includes recommendations for improving the features of funeral insurance products to potentially address issues raised in this report.

About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

Consultation papers: seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

Regulatory guides: give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

Information sheets: provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

Reports: describe ASIC compliance or relief activity or the results of a research project.

Disclaimer

This report does not constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act and other applicable laws apply to you, as it is your responsibility to determine your obligations.

Examples in this report are purely for illustration; they are not exhaustive and are not intended to impose or imply particular rules or requirements.

Contents

Executive summary

Funeral insurance in Australia

1 Funeral insurance is sold to consumers to cover the cost of funerals. Funeral insurance is a form of life insurance and, in common with other types of life insurance, the premiums are ongoing and often stepped—that is, they increase as the consumer ages. Even so-called 'fixed' premiums will increase (along with the benefit payable) under 'inflation protection' measures (usually by 5% annually).

2 Significant issues of concern with the design and sale of funeral insurance have been identified in Australia in recent years. For example:

(a) In its 2013 annual report, the Australian Prudential Regulatory Authority (APRA) reported that it was closely monitoring the prudential implications of developments in directly marketed life insurance products,[1] noting that:

> insurers need to fully understand the reputational risks they face from customers subject to substantial premium increases as they age and who may pay more in premiums than they receive in benefits.[2]

(b) In 2013, a coalition of consumer and older-Australian advocacy groups released a strategy paper on funeral insurance in response to concerns raised with the cost and value of funeral insurance, and the ways in which it is marketed and promoted, including to particular communities such as the elderly and Indigenous consumers.

(c) In 2012, the Australian Securities and Investments Commission (ASIC) published findings from research into consumer awareness of different ways to pay for a funeral.[3] This research found that participants rarely shopped around for the funeral product that best suited them and did not understand the full range of options available to save and pay for a funeral.

3 This report provides an overview of the funeral insurance market in Australia, based on data collected in 2013 and 2014. It describes common features of policies and provides data about sales, claims and cancellations to better understand the benefits and risks associated with these products.

4 It also includes recommendations for improving the features of funeral insurance products to potentially address issues raised in this report and elsewhere.

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[1] Life insurance products are increasingly directly marketed through websites, call centres and advertising, rather than through a financial adviser, financial planner or other intermediary.
[2] APRA, *Annual report 2013*, p. 34.
[3] ASIC, Report 292 *Paying for funerals: How consumers decide to meet the costs* (REP 292).

5 During and since the period of our review, some insurers have introduced more flexible features into their funeral insurance products: see paragraphs 13–14.

Our review

6 At the start of our review, ASIC obtained data from nine of the 12 insurers who were providing direct funeral insurance products to consumers at the time.[4] These nine insurers were selected because they offered funeral insurance products to consumers of all ages.[5] They included the insurers with the largest share of the funeral insurance market for the 2013 and 2014 financial years. We collected data about active policies, sales of new policies, claims and cancellations for these financial years.

7 We also obtained case studies of consumer experiences with funeral insurance from financial counselling agencies and other consumer advocacy groups.

8 We acknowledge the cooperation of participating insurers and consumer agencies that provided data and information for this report.

9 For details of methodology and data analysis, see the appendix to this report.

Key findings and recommendations

10 Table 1 sets out the key findings and recommendations of our review. These findings are also summarised in an infographic: see Figure 1.

11 The recommendations, especially as they relate to product design, are made in the context of ASIC's current powers. ASIC does not have a product intervention power. While we can and do take action regarding misleading conduct, if conduct is not misleading ASIC does not have powers to prevent funeral insurance products creating situations where consumers may:

(a) pay more in insurance premiums over a long period than the benefit that will be available under the policy; or

(b) have to cancel a policy due to unaffordable premiums, despite having paid premiums over a long period (and potentially in excess of the benefit available under the policy).

12 Our focus has been on ensuring that consumers are not being misled by advertising or disclosure, and on providing financial education resources to help consumers make informed financial decisions.

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[4] At the date of publication of this report, there were 14 insurers offering direct funeral insurance products.

[5] For most of these products, applicants must be at least 18 years old. However, children can be added to the policy. Three of the nine insurers also had a product for over-50s only and provided ASIC with data on that product as well as their all-ages products.

Table 1: Key findings and recommendations

Area	Findings	Recommendations
Premiums and product design	*Increasing premiums* On the whole, premiums rose steeply for persons over 50, as most consumers held stepped premiums that increase with age. For consumers aged 80–84, the average annual premium was four times as much as for consumers aged 50–54. In particular, the use of stepped premiums (which increase with age) may place a burden on aging consumers at a time when their income is more likely to be fixed or decreasing. Even so-called 'fixed' premiums will often increase (along with the benefit payable) under 'inflation protection' measures (usually by 5% annually). In a small number of cases, consumers had paid more in total premiums than they would receive as a benefit under the policy. This was an inherent risk in the pricing and feature settings of many policies we reviewed. The current structure of many policies leaves open the possibility of consumers paying more in premiums than the policy is worth.	**Recommendation 1** We recommend that insurers: • review the design, pricing and features of their funeral insurance products; • provide an upfront estimate of the total cost of the policy based on the options offered (e.g. stepped or level premiums; with or without consumer price index or automatic sum increases; if the consumer lives to 70, 80 or 90); and • if the total amount of premiums payable under a policy has the potential to exceed the benefit amount, clearly and prominently disclose this to consumers as an identified risk.
Cancellations and how products are sold	*Policy cancellations* There was a high rate of policy cancellations, with nearly 55% of cancellations occurring during the first year of the policy. Of the cancellations, 65% were actively initiated by the customer, while the rest (35%) were cancelled by the insurer for non-payment of premiums. Most insurers identified the cost of premiums as the most common reason for cancellation. The high rate of cancellations potentially points to problems not only with cost, but also with how some funeral insurance is being designed, marketed and sold. It may suggest that many consumers do not understand important features of the product until after they have signed up. Significant numbers of consumers may also lose the value of premiums paid before the policy is cancelled. *Age profile of persons insured* While over half (51.2%) of consumers with funeral insurance were aged 50–74, funeral insurance sold to Indigenous consumers had a much younger age profile (50% were aged under 20). A higher proportion of Indigenous consumers also had their policies cancelled for non-payment of premiums.	**Recommendation 2** We recommend that insurers: • do more to ensure that consumers understand key features of a funeral insurance product when it is sold to them (whether over the phone, in person or online), especially when selling to vulnerable groups like Indigenous consumers; and • provide a longer 'grace period' than the 28 days required by law before a policy is cancelled for non-payment, particularly for policies that have been in place for a long period of time.

13 We note that more insurers have begun offering improved features in new funeral insurance products introduced during, and since, the period of our review, including flat or level premiums for the life of the policy and capped premiums (where premiums cease to be payable once the benefit amount is reached).

14 It will take some time to see the impact of new policy features, particularly as consumers with existing funeral insurance policies will retain their existing product unless they decide to switch and lose the benefit of premiums already paid. We intend to monitor the impact of innovations in the market, including on the currently very high cancellation rates. We will also continue to monitor advertising and sales of funeral insurance to ensure that consumers are not misled about the benefits and risks of these products.

15 In the meantime, we recommend that consumers concerned about how to pay for their funeral consider all the options available. Apart from funeral insurance, other options include funeral bonds, pre-paid funerals, superannuation (including life insurance within superannuation) and term deposits. Some of the pros and cons of each option are discussed on our MoneySmart website.[6]

[6] See 'Paying for your funeral' at www.moneysmart.gov.au.

Figure 1: Funeral insurance: A snapshot

What we did for this report

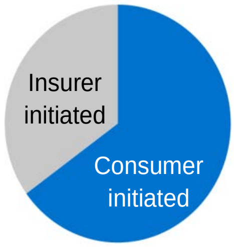
We obtained data from nine insurers who offer funeral insurance to Australian consumers via direct channels including TV, print and radio advertisements.

The data included sales of policies, premiums, claims and cancellations for the 2013 and 2014 financial years. We also obtained case studies about consumer experience of funeral insurance from financial counsellors and other consumer advocates.

HIGH RATE OF CANCELLATIONS

80%

In 2014 the number of cancellations was 80% of the number of polices sold. **The main reason was cost.**



65% of cancellations were initiated by consumers

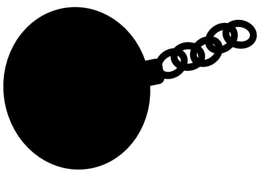
35% were initiated by insurers for non-payment of premiums

Consumers who cancel their policies **lose the value of premiums** paid to date.

STEEP INCREASES IN PREMIUMS

The average premium for 80–84 year olds was **four times the average** premium for 50–54 year olds.

With stepped premiums **consumers risk becoming trapped** in an unaffordable product at a time when their income is likely to be fixed or falling.



A Funeral insurance in Australia

Key points

Funeral insurance in Australia is a type of life insurance that is sold directly to consumers rather than through a financial adviser.

Regulators and consumer organisations have identified significant issues of concern with the product design and sale of funeral insurance.

ASIC is responsible for the conduct and disclosure obligations of the issuers of funeral insurance, including the obligation to provide services efficiently, honestly and fairly.

We have taken action in recent years on misleading advertising of funeral insurance and have produced research and information about alternative ways consumers can pay for their funeral, including superannuation, term deposits, funeral bonds and pre-paid funeral plans.

How funeral insurance works

16 The funeral insurance products we reviewed for this report are 'direct' life insurance products. This means they are sold directly to consumers (e.g. through advertising and call centres), rather than through a financial adviser, financial planner or other intermediary. The sum insured is typically much lower than for other life insurance products, as it is intended only to cover the cost of a funeral and burial or cremation, rather than providing for dependants.

17 Despite the low sum insured, the cost of most funeral insurance coverage is relatively high, due in part to features like guaranteed acceptance (no health or medical checks) and an absence of full underwriting.

18 Funeral insurance products in Australia typically have the following features:

(a) The premium payable depends on the age (and sometimes gender) of the applicant and the sum insured.

(b) Applicants are not usually subject to health or medical checks.

(c) There are often restrictions on when benefits are payable in the first 12 to 24 months of a policy (e.g. usually benefits are payable during this period for accidental death only).

(d) Premiums usually increase as the insured person ages, although in some policies premiums cease after the person reaches a specified age (e.g. 90).

(e) The sum insured also usually automatically increases in line with the consumer price index or a fixed amount (e.g. 5%). The insured person can sometimes opt out of automatic sum insured increases.

(f) Premiums are not refundable if the insured person stops making payments or cancels the policy.

19 While the above features are common or typical, there is variation among insurers' offerings and consumers considering funeral insurance need to scrutinise carefully the specific features of a given product. For more details about new product features in the market, see paragraphs 54–57.

Recent scrutiny of funeral insurance

20 In 2013, a coalition of 11 consumer and older-Australian advocacy groups released a strategy paper on funeral insurance in response to a number of concerns identified in their work with consumers.[7]

21 Among the 13 recommendations made were recommendations that funeral insurers should:

(a) offer fixed premiums for the duration of a policy, so that consumers are not paying escalating premiums at a time in their lives when their capacity to pay is likely to be declining;

(b) provide consumers with an estimated total cost of the policy, based on publicly available longevity data, so that they can better assess the suitability of the product for them;

(c) offer capped insurance products, so that consumers do not pay more in premiums than they will be entitled to claim for;

(d) extend policy arrears periods, so that consumers who miss payments do not have their insurance cancelled after 28 days but are offered more flexible arrangements, including the chance to repay arrears over time to retain their cover and be eligible to claim; and

(e) improve compliance with prohibitions on mis-selling and deceptive conduct, especially for funeral products that target Indigenous consumers.

22 The Combined Pensioners & Superannuants Association of NSW (CPSA) has expressed concern about the claims made in advertising by some insurers about the affordability and 'peace of mind' offered by funeral insurance products.[8]

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[7] Consumer Action Law Centre (CALC), *Time to end the funeral insurance rip-off: A consumer strategy for a fairer deal*, August 2013. The 11 agencies contributing to this report were: CALC, Choice, The Council on the Aging, Financial Counselling Australia, Consumer Credit Legal Service (WA), Insurance Law Service, Footscray Community Legal Service, National Information Centre on Retirement Investments, National Seniors Australia, the Combined Pensioners & Superannuants Association of NSW (CPSA) and Financial and Consumer Rights Council.
[8] CPSA, *The $140,000 funeral: Pitfalls of funeral insurance*, March 2011.

23 The CPSA report analysed two funeral insurance products, together with life expectancy data, to highlight issues—including the following:

(a) A policy holder will pay more in premiums than both the cost of a funeral and the benefit paid under the policy before they reach their average life expectancy.

(b) If the policy holder lives into their 90s, the cost of the funeral may not be covered by the benefit paid.

(c) Premiums can reach and exceed 10% of a single person's aged pension.

24 The Insurance Law Service of the Financial Rights Legal Centre (FRLC) (formerly the Consumer Credit Legal Centre (NSW)) has published a pamphlet, *Why you DON'T need funeral insurance*, based on their experience with consumers who have had difficulties with funeral insurance, especially being unable to afford rising premiums over time. The pamphlet encourages consumers to carefully consider whether funeral insurance is the best-value method of paying for their funeral and highlights other options such as pre-paid funerals, funeral bonds, savings accounts, superannuation and life insurance within superannuation. The FRLC also includes funeral insurance on its 'Financial Hazards Hotlist'.

Regulatory framework and ASIC's role

25 ASIC has regulatory responsibility for the conduct and disclosure obligations of issuers of funeral insurance and funeral bonds. This includes the obligations to provide services efficiently, honestly and fairly and to comply with financial services laws. APRA has prudential responsibility for life insurance companies and friendly societies. Pre-paid funeral plans, often offered through funeral directors, are regulated by state and territory consumer affairs agencies.

26 ASIC is also responsible for the licensing of life insurers who issue funeral insurance and funeral bonds. However, providers of the following products only are exempt from the requirement to hold an Australian financial services (AFS) licence:

(a) *Funeral benefit:* This covers the cost of funeral and burial or cremation services (e.g. a pre-paid funeral plan provided by a funeral director).[9]

(b) *Funeral expenses only:* This policy provides a benefit for the sole purpose of meeting expenses of, and incidental to, a funeral and burial or cremation (e.g. the payout will not exceed these substantiated expenses).[10]

[9] See s761A and 765A(1)(w) of the *Corporations Act 2001* (Corporations Act), s5(2)(a) and 12BAA(8)(o) of the *Australian Securities and Investments Commission Act 2001* (ASIC Act) and s11(3)(e)(i) of the *Life Insurance Act 1995* (Life Insurance Act).
[10] See s765A(1)(y) of the Corporations Act, reg 7.1.07D of the Corporations Regulations 2001 and s11(3)(e)(ii) of the Life Insurance Act.

27 Two insurers we reviewed offered policies for funeral expenses only, but most policies provided a lump sum payment on the death of the insured person. Those policies that provide for funeral expenses only are regulated by ASIC under the consumer protection provisions of the *Australian Securities and Investments Commission Act 2001* (ASIC Act), but are not covered by the financial services licensing and conduct regime of the *Corporations Act 2001* (Corporations Act). Most policies we reviewed for this report were regulated under both the ASIC Act and Corporations Act.

Limitations in ASIC's powers

28 ASIC does not have a product intervention power. While we can and do take action regarding misleading conduct, if conduct is not misleading ASIC does not have powers to prevent funeral insurance products creating situations where consumers may:

(a) pay more in insurance premiums over a long period than the benefit that will be available under the policy; or

(b) have to cancel a policy due to unaffordable premiums, despite having paid premiums over a long period (and potentially in excess of the benefit available under the policy).

29 Our focus has been on ensuring that consumers are not being misled by advertising or disclosure, and on providing financial education resources to assist consumers make informed financial decisions.

Our work on funeral insurance

30 In 2011–12, ASIC's Consumer Advisory Panel commissioned independent research to better understand consumer experiences with funeral benefit products.

31 This research resulted in the publication of Report 292 *Paying for funerals: How consumers decide to meet the costs* (REP 292), which explored consumer decision making, product understanding and experience with three types of product: pre-paid funeral plans, funeral bonds and funeral insurance.

Case study 1: Understanding funeral benefit products

In our consumer research, funeral insurance was highlighted as having the highest profile among funeral benefit products.

However, our research also found that many people did not understand some of the key features of funeral insurance, such as increasing premiums, total cost of the insurance compared with the real cost of a funeral, and what will happen if they miss payments.

In addition, people were not aware of alternative ways to meet funeral costs, such as pre-paying by instalments or buying funeral bonds.

Based on these findings, we have taken specific action on funeral insurance: see Table 2.

Table 2: ASIC action on funeral insurance

Area of concern	Outcomes
Advertising	An insurer made changes to the way it promoted funeral insurance after we raised concerns there was a risk consumers may be misled about premium increases and qualifications regarding price.[11] Another insurer agreed to withdraw existing funeral insurance advertising after ASIC raised concerns that premium increases and stepped premiums were not adequately disclosed or explained.[12]
Indigenous consumers[13]	A booklet, *Paying for funerals*, is available on our MoneySmart website. It discusses different ways of paying for funerals and is tailored specifically to Aboriginal and Torres Strait Islander communities.
Over 55s	A booklet, *Paying for your funeral*, is available on our MoneySmart website. It is tailored more generally to the over-55 age group who might be thinking about how to pay for their funeral.
Alternatives to funeral insurance	Our MoneySmart website outlines the pros and cons of different options available to consumers as an alternative to funeral insurance, including the following: • *Superannuation:* This is payable to your dependants or estate. Any life insurance held with superannuation is also payable at this time. • *Savings accounts and term deposits:* These products can help you keep money aside to pay for your funeral. • *Government payments:* You may be eligible for a payment from Centrelink or Veterans' Affairs towards funeral costs. • *Pre-paid funerals:* You can pay in advance for your funeral, which fixes the cost in today's dollars. • *Funeral bonds:* This is a type of investment product that can help you save for funeral expenses.

[11] See Media Release (13-152MR) *ASIC acts to improve consumer understanding of funeral insurance* (26 June 2013).
[12] See Media Release (14-007MR) *ASIC continues to focus on funeral insurance* (20 January 2014).
[13] In 2004, we also obtained Federal Court orders under anti-hawking laws restraining an insurer from selling funeral insurance door-to-door to Indigenous consumers: see Media Release (04-094MR) *ASIC acts to stop illegal door-to-door selling to indigenous communities* (1 April 2004).

B Key findings

Key points

On the whole, premiums rose steeply for persons over 50, as most consumers held stepped premiums that increase with age. For consumers aged 80–84, the average annual premium was four times as much as for consumers aged 50–54.

There was a high rate of policy cancellations, with nearly 55% of cancellations occurring during the first year of the policy. Of the cancellations, 65% were actively initiated by the customer, while the rest (35%) were cancelled by the insurer for non-payment of premiums. Most insurers identified the cost of premiums as the most common reason for cancellation.

While over half (51.2%) of consumers with funeral insurance were aged 50–74, funeral insurance sold to Indigenous consumers had a much younger age profile (50% were aged under 20). A higher proportion of Indigenous consumers also had their policies cancelled for non-payment of premiums.

Increasing premiums

32 At 30 June 2014, there were a total of 437,274 active funeral insurance policies covering 743,421 individual lives. In the 2014 financial year, the nine insurers wrote 90,063 new policies covering 156,143 lives. While a few insurers saw an increase in new funeral insurance business in 2014, there was an overall decline of around 20% in new policies compared with the 2013 financial year.

33 Most consumers held policies with stepped premiums, where premiums increase as the person ages. We found that average annual premiums quadrupled for consumers aged over 50, rising from $336 for those aged 50–54 to $1,344 for those aged 80–84.

34 Despite the overall decline in new policies between the 2013 and 2014 financial years, the nine insurers we reviewed received a total of nearly $315 million in premiums for 2014 financial year, an increase of about 9% on the previous year.

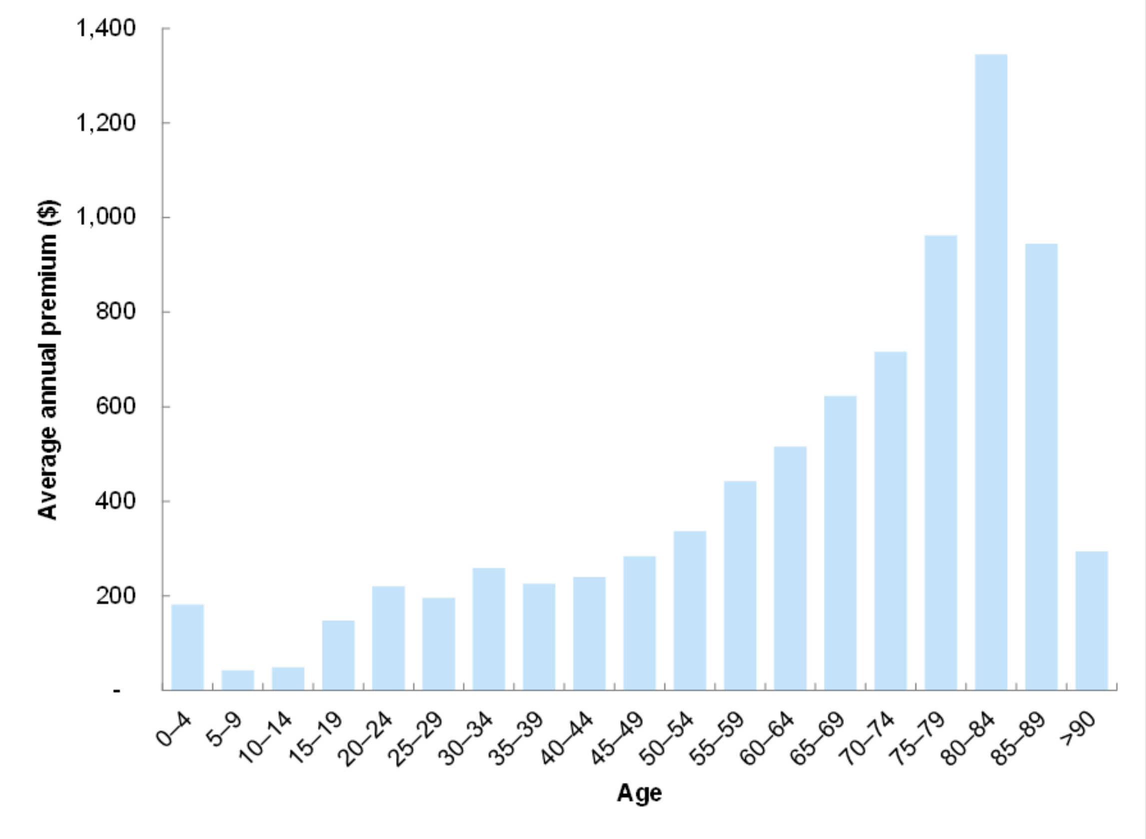
35 In the 2014 financial year, there were a total of 12,648 funeral insurance claims accepted by insurers. Over $103 million was paid out in claims (with an average payout of $8,143), a significant increase on the previous year ($61.6 million). The amount paid out by insurers was around 33% of the value of premiums collected over the same period (in the 2013 financial year, the value of claims paid was 20% of premiums collected).

Case study 2: Struggling to meet the cost of stepped premiums

A 70-year-old woman who lives in a regional town contacted her local pensioner advocacy agency as she was having difficulty maintaining her funeral insurance premium payments.

Due to the stepped nature of the premiums, she found she was now paying *per week* what she was originally paying *per month* for the same level of cover when she took out funeral insurance 12 years ago.

Figure 2: Average annual premium by age group



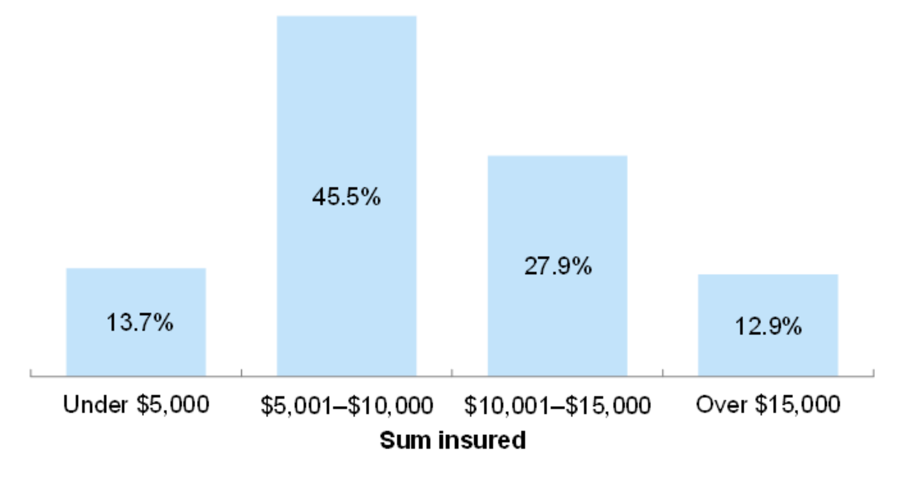
Source: Responses provided by insurers to ASIC. All persons insured as at 30 June 2013.

Average sum insured

36 Our research suggests that most funerals cost somewhere between $4,000 and $15,000.[14] For the policies we reviewed, the average sum insured was $8,859. For new policies, the average sum insured rose to $10,631. Almost half of insured persons were covered for an amount between $5,000 and $10,000: see Figure 3. Nearly 13% (or 92,532 people) were covered for an amount in excess of $15,000.

[14] MoneySmart, *Paying for funerals* (PDF, 1.45MB), June 2013.

Figure 3: Distribution of persons insured by sum insured



Source: Responses provided by insurers to ASIC. Active policies as at 30 June 2013.

37 Many funeral insurance policies offer fixed benefit amounts—for example, consumers can choose to be covered for $5,000, $10,000 or $15,000. However, most policies we looked at included automatic annual ‘cost of living’ increases in the sum insured (usually 5%) which means the benefit amount increases over time, along with the cost of the premium. Some policies allow consumers to opt out of such increases.

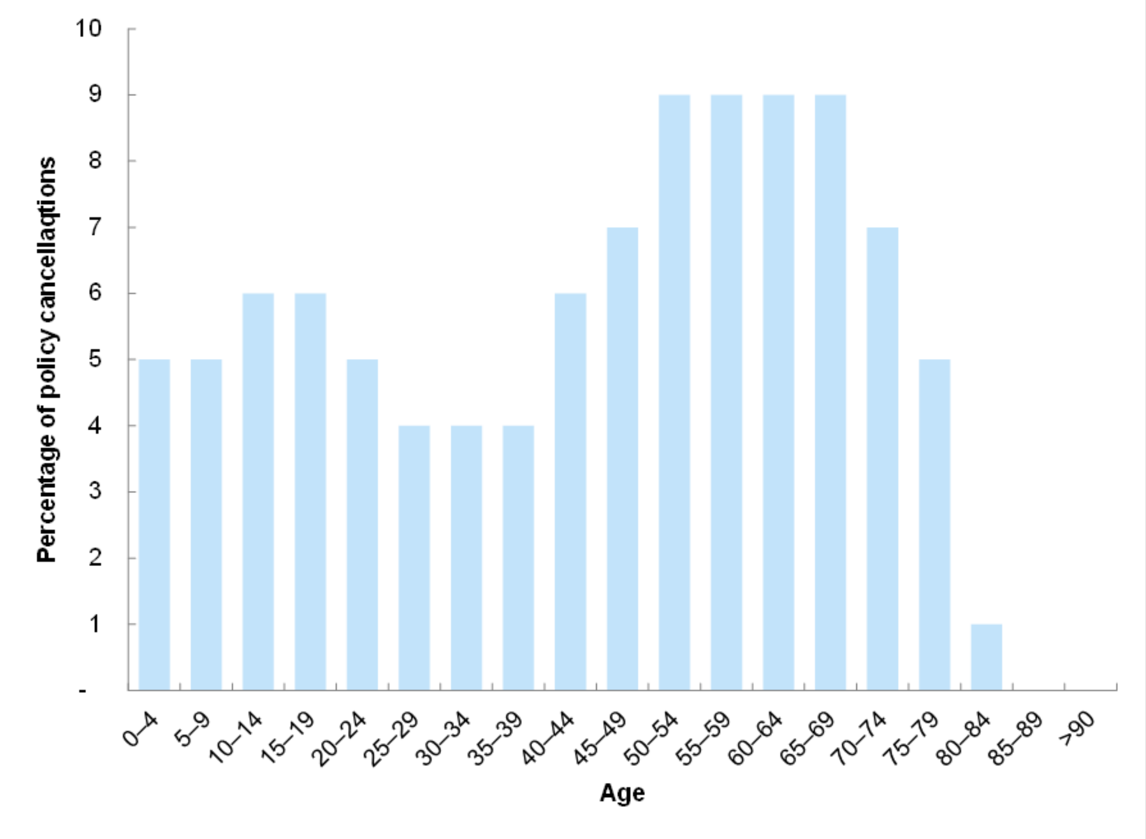
Policy cancellations

38 During the 2014 financial year, a total of 72,091 funeral insurance policies were cancelled, representing a lapse rate of 16.5% of total active policies. Notably, the rate of cancellations as a proportion of new policies was 80%. Nearly 65% of cancellations were initiated by consumers, while in the remainder of cases the insurer cancelled the policy due to non-payment of premiums.

39 Nearly two-thirds (65.2%) of active policies had been held for less than three years. Only 17.5% had been held for five years or longer, with just 4.7% held for longer than eight years.

40 About 16% of cancellations occurred during the cooling off period, while a further 39% occurred during the remainder of the first year of the policy. Therefore, about 55% of cancellations occurred during the first year of the policy. According to most insurers, the main reason why consumers are cancelling their policies is cost.

Figure 4: Policy cancellations by age group



Source: Responses provided by insurers to ASIC. 1 July 2012–30 June 2013.

Case study 3: Deciding whether to cancel insurance

Carli, a 58-year-old woman who lived in public housing with her teenage son, sought financial counselling due to a chronic inability to meet daily living expenses. She had been relying on emergency relief providers for grocery supplies for the past four months.

Carli had been paying for funeral insurance by direct debit throughout this period of acute financial difficulty. She had held the insurance policy for over six years and her premiums were approximately $24 per fortnight. She was on a disability support pension when she first purchased the policy and was unaware of alternative ways to pay for her funeral.

She was now in arrears on premium payments. However, she was reluctant to cancel the policy as she did not want to lose the cover she had paid for to date and her family was unable to afford the cost of a funeral.

Age profile of persons insured

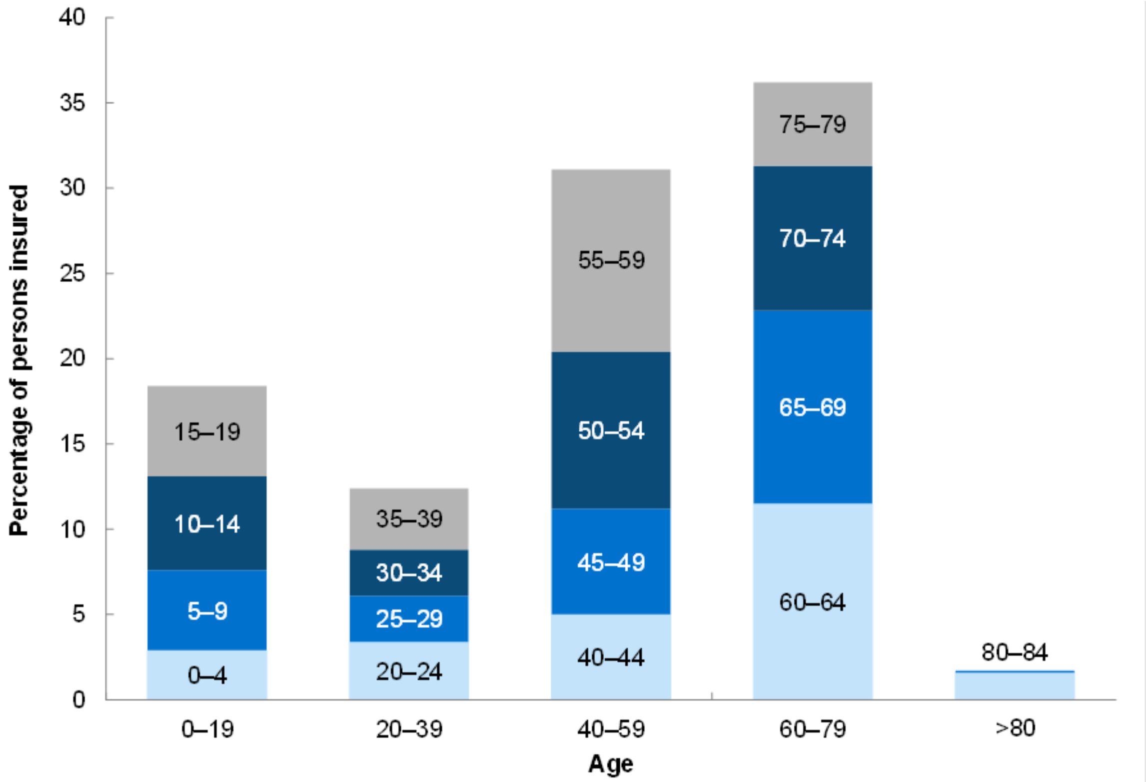
41 Over half (51.2%) of those covered by a funeral insurance policy were aged between 50–74 years of age. However, 18% of insured persons were aged between 0–19 years of age.

42 Variations in age profile between insurers appear to be largely due to the ways in which specific policies are designed and marketed—for example, some are targeted to the over-50s, some to Indigenous communities, and some offer free additional cover for children under 18 or a free first year of cover for all persons insured.

Indigenous consumers

43 While a few insurers had unusually high numbers of young persons insured due to offering free additional cover for children, there was only one insurer with significant numbers of persons insured under 30 for which premiums were being paid. This insurer's products were marketed to Indigenous consumers and their age profile of persons insured was anomalous compared with those of other insurers we reviewed. For this insurer, 50% of persons insured were aged under 20 and 33% were under 15. A higher proportion of Indigenous consumers also had their policies cancelled for non-payment of premiums.

Figure 5: Persons insured by age



Source: Responses provided by insurers to ASIC. Active policies as at 30 June 2013.

C Issues and recommendations

Key points

Steeply increasing premiums place a burden on aging consumers at a time when their income is more likely to be fixed or decreasing. Coupled with this is the risk of paying more in premiums that the policy is worth. Insurers should review the design, pricing and features of their funeral insurance products.

The high rate of cancellations in the first few years of a policy may reflect consumers' perception that funeral insurance is poor value. It may also reflect issues with the marketing and sale of funeral insurance. Insurers should do more to ensure that consumers understand key features of the product before they sign up.

Since we commenced our review, more insurers have begun to introduce improved product features, including level premiums for the life of the policy and premium payments that are capped at the sum insured. ASIC will continue to monitor funeral insurance, including the effect of product innovations on consumers.

Premiums and policy design

44 The existence of stepped premiums (i.e. premiums that increase as a customer ages) means that consumers may not understand the future cost commitment of funeral insurance when they first take out a policy. As the data for this report confirms, premiums rise steeply for consumers aged over 50, who represent more than half of those covered by a funeral insurance policy. Steeply increasing premiums place a burden on aging consumers at a time when their income is more likely to be fixed or decreasing. For 60% of couples over 65 and 76% of singles over 65, a government pension is their main source of income.[15]

45 Several insurers offer a choice between stepped and fixed (or level) premiums; however, most 'fixed' premiums will increase (along with the benefit payable) under 'inflation protection' measures (usually 5% annually). Only some insurers allow customers to opt out of these increases.

46 Additionally, fixed premiums generally start higher than stepped premiums, so when given a choice by insurers between the two, many consumers choose the 'cheaper now' option of a stepped premium, even if it may prove poorer value over time.[16] Behavioural economists call this 'present bias', where we tend to place more weight on immediate gains than future losses.

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[15] Australia Bureau of Statistics, *Household income and income distribution 2011–12*.
[16] REP 292 found that people who chose funeral insurance decided on how much premium they could afford right now: 'affordability was calculated in every case as "here and now" affordability' (p. 30).

47 Another risk arising from the structure of many funeral insurance products we reviewed is the potential for consumers to pay more in premiums over the life of the policy than they will receive as a benefit when they die. Our review found that this risk had materialised for some consumers.

48 Because of high lapse rates and the fact that many funeral insurance products were relatively new to the Australian market, the problem did not appear to be widespread. However, given the structure of most of the policies we reviewed, it is possible that the total amount of premiums paid over the life of the policy may exceed the benefit amount for an increasing number of consumers.

Recommendation 1: Premiums and policy design

We recommend that insurers:

- review the design, pricing and features of their funeral insurance products;
- provide an estimate of the total cost of the policy based on the options offered (e.g. stepped or level premiums; with or without consumer price index or automatic sum increases; if the consumer lives to 70, 80 or 90); and
- if the total amount of premiums paid under a policy has the potential to exceed the benefit amount, clearly and prominently disclose this to consumers as an identified risk.

Cancellations and how products are sold

49 The high rate of cancellations in the first few years of a policy, especially customer-initiated cancellations, may reflect consumers' perception that funeral insurance is poor value. This conclusion is supported by the fact that 'cost' was identified by most insurers in our review as the most common reason for cancellations. Consumers are also choosing to cancel in high numbers outside the cooling-off period, meaning they forgo any benefit from the premiums paid before they cancel their policy.

50 The high rate of cancellations also potentially points to problems with how some funeral insurance products are being marketed and sold, as it may suggest that consumers do not understand important features of the product they are purchasing until after they have signed up. Although not all insurers we reviewed use advertising to sell funeral insurance, television and radio advertising accounted for 60% of sales of funeral insurance during the period of our review.[17]

51 The power of funeral insurance advertising, especially on daytime television, was noted in our earlier report on funeral insurance (REP 292). It is therefore

[17] RiceWarner, *Direct life insurance 2014, research report*, p. 32.

important not only that such advertising does not mislead consumers, but also that consumers who contact insurers to express interest in purchasing funeral insurance as a result of television or radio advertisements are given adequate information about the product's key features at the time of sale.

52 Despite our finding that most cancellations were customer-initiated, there remained a large percentage of consumers (35%) whose policies were cancelled by the insurer for non-payment of premiums. The proportion of cancellations for non-payment was higher still among Indigenous consumers.

53 As well as pointing to value and affordability issues, this finding appears to support calls by consumer groups for insurers to extend arrears periods. Most insurers use a standard arrears period of 28 days, after which a policy will be cancelled with no refund or benefit able to be realised by the consumer, no matter how long they have being paying premiums.

Recommendation 2: Cancellations and how products are sold

We recommend that insurers:

- do more to ensure that consumers understand key features of a funeral insurance policy when it is sold to them (whether over the phone, in person or online), especially when selling to vulnerable groups like Indigenous consumers; and
- provide a longer 'grace period' than the 28 days required by law before a policy is cancelled for non-payment, particularly for policies that have been in place for a long period of time.

New product features on the market

54 After increased scrutiny of funeral insurance by ASIC and consumer organisations, there has been a shift by some funeral insurers to incorporate policy features that attempt to address some of the specific concerns identified in this report and elsewhere. While these features may improve the value of some products, funeral insurance remains more expensive than some of the alternative ways of paying for a funeral for many consumers.

55 Recent product features introduced by individual insurers include:

(a) flat or level premiums that will not increase over the life of the policy;

(b) where the policy is cancelled for lapsed premium payments, a grace period of three months during which the policy can be reinstated;

(c) where the policy is cancelled for lapsed premium payments but the policy has been held for at least 10 years, the policy automatically converts to a 'paid up insurance' product where the benefit will be a percentage of the sum insured (e.g. 40% of $10,000) and no further premiums are payable;

(d) premiums that are discounted after a specified continuous period of coverage (e.g. every five years); and

(e) total premium payments that are capped at the sum insured, so that consumers will not pay more in premiums than the benefit amount.

56 We encourage all insurers who offer funeral insurance products to review their policy features to ensure they provide appropriate value for consumers. ASIC will continue to monitor funeral insurance, including the effect of product innovations on consumers.

57 We encourage consumers who are concerned about how to pay for their funeral to consider all the options available. Apart from funeral insurance, other options include funeral bonds, pre-paid funerals, superannuation (including life insurance within superannuation) and term deposits. For more information on the pros and cons of each option, see our MoneySmart website.[18]

[18] See 'Paying for your funeral' at www.moneysmart.gov.au.

Appendix: Methodology and data analysis

Insurers and products

58 At the start of our review, we asked for information from insurers who sold direct funeral insurance products in the Australian market at 30 June 2013. We obtained information from nine of the 12 insurers in the market. These insurers were selected because they offered funeral insurance products to consumers of all ages.[19] The nine insurers had a total of 42 different funeral insurance products under different brands, 12 of which were closed to new entrants.

59 Information we requested included the number of active policies, sales, claims and cancellations for the 2013 and 2014 financial years. For the 2013 financial year, we also obtained information about the cost of premiums, sum insured and the age profile of persons insured.

60 For some types of information requested, insurers with multiple funeral insurance products were asked to provide information only for the product with the most number of active policies. Not all insurers could provide all of the data requested.[20]

61 We also sought information from consumer groups and financial counselling agencies about cases they have seen of consumers experiencing issues with funeral insurance.

Policies and new sales

62 At 30 June 2014, there were a total of 437,274 active funeral insurance policies covering 743,421 persons insured. Active policies include both current products and those that are closed to new business. In 2014, the nine insurers we reviewed for this report wrote 90,063 new policies covering 156,143 persons.

63 Most insurers saw a slight increase in active policies and persons insured between 2013 and 2014. In most cases, this seems to be due to fewer consumers cancelling their policies in the 2014 financial year rather than to an increase in new business. While a few insurers saw an increase in new funeral insurance business in 2014, there was an overall decline of around 20% in new policies compared with the 2013 financial year.

[19] For most of these products, applicants must be at least 18 years old. However, children can be added to the policy. Three of the nine insurers also had a product for over-50s only and provided ASIC with data on that product as well as their all-ages products.
[20] All reasonable efforts were made by ASIC to check the data provided for errors and to seek clarification from insurers when possible errors were identified. However, in the absence of any independent publicly available figures, it was not possible to verify the data against other sources.

64 Two of the nine insurers accounted for 80% of active policies in 2013 and 73% of active policies in 2014. These same two insurers wrote 68% and 64% of all new policies in 2013 and 2014 respectively. The gap between active policies and new business may indicate increased competition in the market for funeral insurance over the past two years.

Premiums

65 The nine insurers received nearly $315 million in premiums for the 2014 financial year, an increase of about 9% on the previous year.

66 The average annual premium charged for the 2013 financial year was $448.30. However, there was a large variation in premiums charged among insurers. Some of this variation is attributable to the age profile of each insurer’s customer base, since average premiums mostly increased with age.

67 Average annual premiums rose steeply for consumers aged over 50, from $336 for those aged 50–54 to $1,344 for those aged 80–84. Some policies stop charging premiums when the insured reaches a specified age (e.g. 85 or 90).

68 We asked insurers about the number of consumers who had paid more in total premiums than the benefit amount under their policy. In many cases, the specific policy had not been on the market long enough for this risk to materialise. High cancellation rates also militated against this risk. However, for most of those funeral insurance products that had been on the market for more than approximately five years, there was a small proportion of consumers whose total amount of premiums paid had exceeded their benefit amount.

Claims

69 In the 2014 financial year, there were a total of 12,648 funeral insurance claims accepted by insurers. Only a very small number of claims were denied. However, in a further 1,809 cases premiums were refunded rather than a benefit paid, due to death being from natural causes (i.e. non-accidental) within the first 12 or 24 months of a policy. In such cases, most policies allow only for a refund of premiums paid to date.

70 Over $103 million was paid out in claims in the 2014 financial year (with an average payout of $8,143), a significant increase on the previous year ($61.6 million). Claims paid represented nearly one-third of the value of premiums collected over the same period (in the 2013 financial year, claims paid represented one-fifth of premiums collected). While two insurers had a

65% rate of claims paid as a proportion of premiums received, most insurers had a rate of claims paid to premiums received of between 20–30%.

Cancellations and policy duration

71 During the 2014 financial year, a total of 72,091 funeral insurance policies were cancelled, representing a lapse rate of 16.5% of total active policies. Notably, the rate of cancellations as a proportion of new policies was 80%.

72 Nearly 65% of cancellations in the 2014 financial year were initiated by consumers, while in the remainder of cases the insurer cancelled the policy due to non-payment of premiums.

73 About 16% of cancellations occurred during the cooling-off period. A further 39% occurred during the remainder of the first year of the policy. Therefore, about 55% of cancellations occurred during the first year of the policy.

74 The data on policies cancelled by age group shows approximately half of cancellations occurred in the 50–89 age bracket (see Figure 2), roughly commensurate with the proportion of policy-holders in the same age bracket. See our discussion of the age profile of insured persons at paragraphs 78–81.

75 Insurers were asked to give their view of the main reasons consumers had cancelled their policy. The *cost of premiums* was the most common reason insurers gave in response to this question. Other frequently cited reasons were that the consumer:

(a) had switched to a competitor;

(b) had switched to an alternative insurance product (e.g. life insurance); and

(c) no longer felt the need for the product (e.g. due to favourable change in financial circumstances).

76 Nearly two-thirds (65.2%) of active policies had been held for less than three years. Only 17.5% had been held for five years or longer, with just 4.7% held for longer than eight years.

77 We note that the data on policy duration applies only to those insurers' products with the largest number of active policies and therefore is based on a smaller sample than the cancellations data. We also note that several of the funeral insurance products on which the policy duration data is based had been on the market for less than five years.

Age profile of insured persons

78 There was a noticeable degree of variation in the age profile of persons insured for each insurer, with some insurers concentrated in the over-60 age bracket and others having a wider distribution by age. This variation seemed to be due to the tailoring and marketing of specific policies. For example, some products are targeted to the over-50s, some to Indigenous consumers, and some offer free additional cover for children under 18 or a free first year of cover for all persons insured.

79 Despite these variations, just over half (51.2%) of those covered by a funeral insurance policy were aged between 50–74 years of age. At the same time, around 18% of persons insured were aged between 0–19 years of age. This relatively high percentage of young persons insured seems to be mainly due to ‘family plans’ that allow dependants to be added to a policy, sometimes at no additional cost. Between ages 20–39, the percentage of persons insured dropped to 12%.

80 However, while offering free additional cover for children resulted in a few insurers having unusually high numbers of young persons insured, only one insurer had a significant number of persons under 30 for which premiums were being paid. This insurer’s products were marketed to Indigenous consumers and their age profile was anomalous compared with other insurers we reviewed. For this insurer, 50% of persons insured were aged under 20 and 33% were under 15.

81 With increasing life expectancy, the concern with younger people taking out funeral insurance is the risk that uncapped premium payments will over time outstrip the benefit amount. This risk was explored and modelled in some detail in the CPSA report, *The $140,000 funeral: Pitfalls of funeral insurance*.

Number of persons insured

82 Nearly 60% of active policies provided cover for a single person only and about 30% of active policies provided cover for two persons. About 5% of active policies covered five or more persons.

83 Those insurers who had a higher proportion of active policies with more than two persons covered tended to offer features such as discounts on premiums for additional persons covered or free cover for children up to age 18 when added to an adult’s policy.

Sum insured

84 Our research suggests that most funerals cost somewhere between $4,000 and $15,000.[21] For the policies we reviewed, we found that the average sum insured was $8,859. For new policies, the average sum insured rose to $10,631. Almost half of persons insured were covered for an amount between $5,000 and $10,000. Nearly 13% (or 92,532 people) were covered for an amount in excess of $15,000.

85 Many funeral insurance policies offer fixed benefit amounts—for example, consumers can choose to be covered for $5,000, $10,000 or $15,000. However, most policies we looked at included automatic annual 'cost of living' increases in the sum insured (usually 5%) which means the benefit amount increases over time, along with the cost of the premium. Some policies, but not all, allow consumers to opt-out of such increases.

86 Some policies included features such as double or triple payouts for accidental death. In the case of a triple payout, for example, a benefit of $15,000 becomes $45,000 if the insured's death is caused by an accident. A few policies confine this benefit to motor vehicle accidents.

87 With the exception of two insurers, payouts were for the full sum insured and could be used for any purpose. Two insurers made payouts for actual funeral and funeral-related expenses only.

[21] MoneySmart, *Paying for funerals* (PDF, 1.45MB), June 2013.

Key terms

Term	Meaning in this document
AFS licence	An Australian financial services licence under s913B of the Corporations Act that authorises a person who carries on a financial services business to provide financial services Note: This is a definition contained in s761A.
APRA	Australian Prudential Regulatory Authority
ASIC	Australian Securities and Investments Commission
ASIC Act	*Australian Securities and Investments Commission Act 2001*
CALC	Consumer Action Law Centre
Corporations Act	*Corporations Act 2001*, including regulations made for the purposes of that Act
CPSA	Combined Pensioners & Superannuants Association of NSW
direct life insurance	Insurance sold directly to consumers (e.g. through advertising or call centres), rather than through a financial adviser, financial planner or other intermediary
FRLC	Financial Rights Legal Centre
Life Insurance Act	*Life Insurance Act 1995*
premium	The amount of money charged by an insurer for coverage
REP 292 (for example)	An ASIC report (in this example numbered 292)
s761A (for example)	A section of the Corporations Act (in this example numbered 761A), unless otherwise specified

Related information

Headnotes

consumer protection, financial services licensing and conduct, funeral benefit, funeral expenses, funeral insurance, insured persons, policy cancellations, stepped premiums, sum insured

Legislation

ASIC Act, s12BAA, 5(2)

Corporations Act, s761A, 765A

Corporations Regulations 2001, reg 7.1.07D

Life Insurance Act, s11(3)

Regulatory guides

RG 234 *Advertising financial products and services (including credit): Good practice guidance*

Consultation papers and reports

REP 292 *Paying for funerals: How consumers decide to meet the costs*

Media and other releases

04-094MR *ASIC acts to stop illegal door-to-door selling to indigenous communities*

12-170MR *How will you pay for your funeral?*

13-152MR *ASIC acts to improve consumer understanding of funeral insurance*

14-007MR *ASIC continues to focus on funeral insurance*

Paying for funerals (Indigenous booklet)

Paying for your funeral (Over-55s booklet)

Other documents

APRA, *Annual report 2013*

Australia Bureau of Statistics, *Household income and income distribution 2011–12*

CALC, *Time to end the funeral insurance rip-off: A consumer strategy for a fairer deal*

CPSA, *The $140,000 funeral: Pitfalls of funeral insurance*

FRLC, *Why you DON'T need funeral insurance*

RiceWarner, *Direct life insurance 2014*, *research report*