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Introduction

From 21st December 2012, it will no longer be possible for life insurers to use gender, or related factors, in calculating premiums or benefits for their products. Since the Test-Achats judgement was announced on 1st March 2011, life insurers have been very aware of this change and are likely to be well advanced in their plans for moving to gender neutral pricing across all of their retail product lines.

The Test-Achats judgement will have implications for all protection product lines, including Life Insurance, Serious Illness cover, and Income Protection cover. It will also have implications for annuity pricing and indeed for general and health insurance too.

Life insurance pricing

Typically, Life Insurers currently use 3 main rating factors for calculating life insurance premium rates – age, gender, and whether or not the individual smokes. For over 80% of customers, the premium rate will be calculated based on this information only. The health of the individual is only taken account of in a small minority of cases, with a loading to standard rates applied if the underwriter determines that the individual has a lower than average life expectancy. This may be due to the individual's medical history, occupation, family history of ill-health etc.

For smokers, the cost of life insurance can be more than double the cost for non-smokers. This reflects the fact that smoking shortens average life expectancy by up to 10 years.

For females, the cost of life insurance is typically 25-30% less than the cost for males. Throughout history, females have tended to live

longer than males, and, currently, females live on average about 5 years longer than males. The reasons for this are not completely clear – it has been speculated that this is due primarily to lifestyle and occupation factors, rather than genetic factors. For example, males tend to drink more alcohol than females and also tend to have poorer quality diets. Both of these factors will tend to result in females living longer. In addition, males tend to have much higher rates of suicide than females and are much more likely to die as a result of a road traffic accident.

However, there is also some evidence that females are genetically more likely to live longer. Females have higher life expectancy in all countries in the world, and longer female life expectancy is also found in most animal species. The gap between female and male life expectancy has been gradually declining in recent years, presumably as a result of female and male occupations, and lifestyles, becoming more similar.

Whatever the exact breakdown of the different factors which go into explaining the gap between female and male life expectancy, life insurers have found gender to be a very useful proxy for the various risk factors involved. From 21st December, this approach will no longer be possible.

Initially, it is likely that life insurers will simply calculate new premium rates based on the expected mix of males and females in their portfolio of business, using the existing separate premium rates which they have for males and females as a base. There will be some uncertainty about the mix of new business between males and females, and therefore insurers are likely to take a somewhat conservative view on business mix to begin with.

This will result in males paying a similar rate to current rates for life insurance, and females paying significantly more (30% to 50% more,

depending on age). So, for females needing life insurance cover, now is the time to buy!

Most life insurance in Ireland is written on either a joint life or dual life basis, and the total premium on a new joint or dual life policy after 21st December is likely to be similar to current premium rates.

Over time, it is possible that life insurers will look at introducing new rating factors (such as taking account of occupation or lifestyle) to a greater extent than is currently the case. Life insurers in Ireland are likely to watch developments in larger markets, such as the UK, before making any significant changes. They will also want to strike a balance between the costs of a more complex underwriting process (with additional rating factors) and the potential benefits of assessing risk more accurately on an individual basis.

Serious Illness pricing

The current rating approach for Serious Illness cover is similar to that used for Life Insurance i.e. the main rating factors used are age, sex, and smoker status. Again, smokers pay much more for their cover than non-smokers. While males are more likely to suffer from heart related serious illness and stroke, females are more likely to be diagnosed with cancer, particularly at younger ages. Overall, these factors balance each other out so that the price difference between males and females for serious illness cover is much smaller than for life insurance. The difference varies by age, and in some cases females pay more than males while in other cases males pay more.

Therefore, the impact of gender neutral pricing on serious illness pricing is likely to be small. The gender neutral rate will be calculated by insurers based on their expected mix of business, and is likely to be close to both the current male rate and the current female rate. Neither males nor females will see a major change to the cost of serious illness cover after 21st December.

Income Protection pricing

For Income Protection products, insurers use a somewhat more sophisticated pricing approach, taking account of occupation class in addition to the usual factors of age, sex and smoker status. Occupations which are office based typically pay a lot less than occupations involving significant manual work. For some occupations, insurers do not provide income protection cover because of the high risk of injury or disability.

All other rating factors being equal, females are currently charged 50-60% more for Income Protection cover compared to males. In setting a gender-neutral price, insurers will take account of the expected mix of business, in the same way as on other product lines. This is likely to result

in a rate which is closer to the current male rate than to the female rate, because insurers will not expect a major change to their mix of business. Therefore, females requiring income protection cover might be well advised to review their cover and the price they are paying for it, after the introduction of gender neutral rates.

Annuity pricing

Annuity pricing in Ireland currently uses a simple rating approach, taking account only of the sex and age of the client, with no allowance for smoker status or for the health of the individual. For the same reasons that females pay less for life insurance (i.e. they live longer), females pay more for annuities – typically about 5% more. When gender neutral pricing is introduced, males are likely to see a small reduction in the annuity they can purchase, while females will see a small increase.

The annuity market in Ireland is somewhat underdeveloped relative to the UK market: impaired life annuities are not widely available and we have yet to see any insurers offering better annuity rates for smokers (this is common in the UK). The introduction of gender-neutral pricing may drive Insurers to develop their annuity products, and to offer more innovative solutions for clients.

Impact on existing business

Life insurance contracts are typically written on a long-term basis. The Test-Achats judgement does not impact the premium rates which Life insurers can charge on existing contracts, even where gender has been taken account of in calculating those rates. This means that clients with existing contracts need not worry that their premium rates could be increased as a result of the introduction of gender neutral pricing. However, life insurers need to be aware that any changes made to an existing policy, which are not part of the original terms and conditions, may result in a need to apply gender neutral pricing to the policy.

Conclusion

Gender-neutral pricing is the most significant change to the pricing of life insurance products in Ireland which we have seen in the last 10 years. The impact of gender-neutral pricing will vary depending on the product line, and insurers are likely to take a prudent view on calculating gender-neutral rates until the market settles down. Over time, life insurers may look to develop more sophisticated pricing approaches and the introduction of gender-neutral pricing may be a spur for greater product innovation.