Pricing Insurance Advice

Elixir Consulting has recently released the second edition of its Adviser Pricing Models Research, which considers the pricing models being used by advice practices. Elixir MD, Sue Viskovic, shares some results and key findings as they relate to pricing risk advice…

Many advisers breathed a sigh of relief when they learned that insurance commissions were largely being left in place after the Future of Financial Advice (FoFA) reforms. Other than for group life policies for members of a superannuation entity, or policies held within a default super fund, commissions remain a legitimate source of revenue for advisers that provide a very valuable service for clients seeking personal insurance – and reassurance.

Whilst they remain a legitimate source of income, many advisers do not believe commissions alone represent an adequate source of income for the often complex advice processes they complete for their clients. Opinions vary greatly on this topic. Some believe that clients who do not pay their adviser separately to their insurance premiums do not place enough value on their advice, and this reflects on their cooperation with the adviser to implement much-needed recommendations. Others seek a remuneration method that will pay them for their time to advise and assist clients who ultimately don't get cover enforced. Opponents of this thinking believe that the commissions earned from larger premiums subsidise the advice provided to the unfortunate few who don't get cover.

Perhaps the most valuable part of the insurance advice process is the support provided by most advisers at time of claim. Some argue that the small ongoing revenue they generate from all of their clients is sufficient to fund the support required by the few who actually make a claim. Others pre-position a claim fee with their clients, knowing that if they ever do need to claim, they would be more than happy to pay their adviser a 'success fee' to assist them through the process.

So what is the best solution to pricing risk advice? The answer is the same as that for pricing any other financial advice – there is no single solution that will suit every client and advice business in the country. One of the key findings in our research is that insurance advice is perhaps the most challenging area to price effectively. We extracted specific detail about pricing risk insurance from the 433 businesses that participated in our research. The majority of advisers used a combination of fees and commissions, and the choice of commission option also varied between the group.

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Interestingly, I recently delivered a workshop with a group of very experienced risk insurance advisers – these practitioners were in the top echelon of their field. Despite the fact that none of them charged fees for their advice – they all received commissions only – there were some very interesting opinions on the future of commissions for risk insurance. Whilst many expressed doubt that people would pay for advice separately to their insurance premiums, I was surprised that there was a general feeling around the room that commissions had a relatively short shelf-life. Whilst they had effectively 'dodged the FoFA bullet', many in the room felt that it was inevitable that insurance commissions would be phased out at some point in the future. The main reason that most had not yet started to charge fees was that they didn't know how. There was great interest when we shared some of the findings from the research.

Findings

Participants in this research adopted a range of different approaches to pricing insurance. When writing insurance as a standalone piece of advice the methods of charging for engagement fees included:

- Taking only the insurance commission and not charging an additional fee
- Charging a fee in addition to receiving the insurance commission
- Determining a fee, taking the insurance commission, and rebating any of the commission that exceeds the pre-determined fee
- Charging a fee and writing the policy with the commission rebated, resulting in a lower premium for the client
- Charging a fee to the client regardless of whether the insurance goes ahead (some will only charge a fee if the insurance does not go ahead)

The options used for pricing were similar, regardless of whether insurance advice was provided as part of a comprehensive financial plan that also included advice on investments, or for standalone insurance advice.

Engagement fees

We asked participants what they charged as an engagement fee for comprehensive advice that excluded insurance. We found that whilst some businesses charged higher fees in addition to receiving insurance commission, the average engagement fee charged across the group was 2.3% lower if insurance advice was included, and commissions were also accepted.

This was an interesting finding, given that there is a significant amount of work involved in providing advice on insurance, and then implementing that advice. In many cases the amount of work completed by the adviser to get the insurance in place has little correlation with the premium, and therefore commission, that is attached to the cover.

When writing insurance advice on a stand-alone basis, the average fees charged in addition to receiving commissions did not vary significantly across the four different options. This was remarkable considering that the amount of commission advisers would earn in addition to the fees would be significantly different across the four options.

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One of the interesting things we found about the level of engagement fees charged by advisers for risk advice was how low the average fees were when commission was not also received.

It was important to us that this research report was a true indicator of advisers around Australia, so we ensured that less than 5% of the participants had been coached by an Elixir consultant. In this instance, had we included the pricing models used by many of our clients, it is likely that our clients may have lifted the averages considerably.

We have assisted many advisers to analyse the average cost to engage a new client to the point that their insurance recommendations are put in place. Whilst it is often very difficult to estimate the amount of work involved for each client, we have found that most businesses find they need to generate in the vicinity of $2,000 to 2,500 to achieve even a modest amount of profit. The average showing in the research of $1,211 indicates that either a large number of the participants assist clients who get cover easily and efficiently, or they may not have adequately analysed what is involved in assisting clients that are more difficult to place. →

Engagement Fees for Insurance-only advice

	Insurance-only advice with commission rebated or refunded (43 participants)	Insurance-only advice with upfront insurance commission option (109 participants)	Insurance-only advice with hybrid insurance commission option (67 participants)	Insurance-only advice with level insurance commission option (25 participants)
Highest	$3,000	$3,300	$10,000	$2,750
Lowest	$200	$200	$100	$200
Average	$1,211	$906	$1,117	$1,143

Specialist vs generalist models

We separated the pricing techniques used by risk specialists, financial advisers, and financial advisers that were attached to accounting firms. None of the risk specialists in the research wrote insurance with the commission rebated, and only one took the commission and refunded it to the client – and only then when the insurance was written as part of a comprehensive financial plan (typically, a comprehensive plan for a risk insurance specialist would include estate planning and possibly super advice on small balances).

By far the most popular commission option for all three groups was the upfront commission option, although it was favoured by roughly half the financial planning businesses compared to around a third of the accounting/ financial planning firms.

The second most popular commission option for risk specialists was the hybrid option, with very few opting to take commission and rebate part of it to their clients. Writing premiums with the commission rebated was an option more popular among financial planners working within accounting firms than those in stand-alone financial planning businesses.

Financial planners working within accounting firms preferred the hybrid and level commission options equally, but more participants in specialist financial planning firms preferred the hybrid option to the level.

Why is insurance hard to price?

There are a number of reasons why insurance is so difficult to price:

- It is difficult to assess how much work will be required to get a policy in place. Advisers will usually track policies through the underwriting process until they are in force, and they often can't predict how long this will take or how much work is required until they complete the client's personal statement. For example, a seemingly healthy young person may have a medical condition that results in extra work for the adviser.
- Advisers can do a lot of work on a policy, only for the client to be declined by the insurer at the end of a long underwriting process. In a commission model, the adviser would receive nothing; in a fee model, the adviser is paid by a client who perceives they have received no value.
- Insurers will claw back commission if a client cancels the policy within a set period – usually twelve months.
- Some advisers say clients can get fed up with the underwriting process and may choose not to pursue it if they are not out of pocket should they stop the process. Advisers faced with this scenario often charge a fee, as they feel the client will be more committed to the underwriting process and less likely to drop out.
- Proponents of the value pricing model (linking a fee to the value a client receives) find it difficult to quantify the peace of mind delivered to the client, as well as the life-time value. Clients who need to claim on a policy receive infinitely more value from the risk advice than those who never make a claim.
- If a client needs to make a claim, most advisers will assist them through this process, and their services are valuable at what is usually an emotional time. Many a claim would not have been paid were it not for a vigilant adviser helping the client. There can be a significant amount of work involved for the adviser in a claim. Whilst some would argue that the ongoing commission is sufficient to cover this work, since only a percentage of an entire client base will ever make a claim, others argue that the ongoing commissions are only enough to cover reviewing their clients' insurance every year. For this reason, while some advisers offer a claims-assistance service to their clients at no extra charge and others include this in their annual retainer, a small percentage will charge the client an additional fee to be paid from the claim payout.

Conclusion

Despite the difficulties in pricing insurance, many advisers have gone a long way to creating a pricing model that works for their clients and their business. Of the 15 business models that are detailed in the report, two are specialist insurance advisers, and 12 of the remaining 13 provide insurance advice as part of their offering. The methods they have determined to price risk advice vary depending on their client base, philosophies, and pricing techniques for other advice they provide.

Yes, pricing insurance advice is challenging, but it certainly is possible. And for those doubting whether clients will pay separately for their insurance advice? The answer is clear – yes they absolutely will, provided that the value of that advice is articulated and delivered well.

Sue Viskovic is the Managing Director of Elixir Consulting, an independent practice management and business coaching organisation that specialises in the financial advice profession. For more information on the Pricing Models Research please visit www.elixirconsulting.com.au