Implications of the Test Achats verdict for UK Insurers and Pension Schemes

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Dave Grimshaw
Partner, Barnett Waddingham LLP

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Agenda

- 2004 EU gender directive
- The “Test-Achats” case, the Advocate General’s Opinion & the ECJ judgment
- What happens next
- Implications for insurers
- Implications for pensions

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Current EU Directive (2004/113/EC)

- Aims to combat discrimination based on gender in access to, and the supply of, goods and services
- Unisex rates required but Member State opt out allowed (unless already using unisex rates)
- Applies to new insurance contracts concluded after 21 December 2007 where these are private, voluntary and separate from the employment relationship
- Pregnancy and maternity related costs cannot be reflected in premiums or benefits
- 5 year review (originally) due at end of 2010 with Member State review of opt-out to follow by 21/12/2012
- Implemented differently across Europe

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EU Directive: The Opt-out clause

- Article 5(2) allows Member States to permit differences related to sex in respect of insurance premiums and benefits:
  - Where gender is a determining factor in the assessment of risk based on relevant and accurate actuarial and statistical data then proportionate differences in individual premiums or benefits are allowed
  - Data must be compiled, published and regularly updated

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EU Directive: Not a "Single Market"

- All 26 countries availed of the opt-out clause:
  - 13 for all types of insurance (incl. UK)
  - Others selectively, e.g. Belgium allows for Life/annuities only
- Different requirements for what data is published and who by
- Different interpretations of relationship between pricing and data
- Different application:
  - Consumer Protection – applies to policies sold to domestic residents, e.g. UK
  - Prudential supervision – applies to domestic insurers, e.g. Belgium

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UK implementation of EU directive

- Implemented March 2008
- Gender allowed as a rating factor for all types of insurance
- Data - individual company level or pooled
- Pricing - proportionate to the data, but says that other factors affect the premium rates
- UK legislation applies to insurance sold to UK residents (whether by UK or overseas insurers) but does not apply to UK insurers selling overseas to non UK residents.

Data to be published: mortality

3.2 Publication may be by way of a table or chart illustrating the ratio of male to female mortality for insured risks in the United Kingdom or an appropriate region. The published data must illustrate recent differences in mortality by gender and by age. It may be based on graduated data using single year age points or raw data by age ranges not exceeding five years up to age 75 and 10 year age ranges thereafter

3.3 The published data may aggregate different forms of annuity and life assurances. It should be reviewed and, if necessary, updated at intervals not exceeding four years

The Actuarial Profession
making financial sense of the future

Gender differentials

Gender as a factor in the assessment of insurance risks.

When underwriting insurance policies, insurance companies base their premiums on a wide variety of factors that may affect the claims cost they observe among their customers. One factor is gender.

From 6 April 2008, the Sex Discrimination (Amendment of Legislation) Regulations specify certain conditions under which insurance companies are allowed to differentiate premiums based on gender. One condition is that the use of gender as a factor in the assessment of risk for individual policies is based on relevant and accurate statistical data. A second condition is that this data must be compiled, published and regularly updated in accordance with guidance issued by HM Treasury (**Latest guidance, March 2008**).

Data in respect of the following types of insurance can be found by clicking on the links below:

- **Life assurance and annuities**
- **Critical illness insurance**
- **Income protection insurance**

This data is supplied by the Continuous Mortality Investigation, which carries out research into mortality and morbidity experience on behalf of the UK Actuarial Profession. This includes people covered by long term insurance policies issued by life insurance companies in the United Kingdom.

These investigations cover all the main types of life assurance, annuitant, pensioner, critical illness and income protection insurance contracts offered by the market. The base data is supplied by life

Related content

- An executive's handbool for understanding and ris managing unit linked guarantees.
- Risk and capital assessment and

Introduction

When underwriting insurance policies, insurance companies base their premiums on a wide variety of factors that may affect the claims cost they observe among their customers. One factor is gender.

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This bulletin illustrates differences in mortality rates between men and women for life assurance and annuities written in the UK.

Data

The table below shows the ratio of male to female mortality rates based on CMI data for 2003-2006. This data is explained in the subsequent notes:

Age band	Ratio of male to female mortality rate	Age band	Ratio of male to female mortality rate
26-30	248%	56-60	145%
31-35	215%	61-65	163%
36-40	156%	66-70	165%
41-45	137%	71-75	154%
46-50	128%	76-80	142%
51-55	139%	81-85	137%

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The “Test-Achats” case

- Belgium adopted the Opt out for life insurance/annuities only
- Action brought in June 2008 by Test-Achats in the Belgian Constitutional Court that law is incompatible with the principle of equal treatment for men and women embedded in constitution
- Court decided that validity of Article 5(2) of Directive 2004/113 needed to be referred to the Court of Justice of EU

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The Advocate General's Opinion

- Founding principles override the EU directive
- Opt out is against EU principle of equal treatment
- 3 year transition period
- Impacts all future insurance premiums (and benefits?) after 3 years, i.e. existing as well as new business

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The Advocate General's Opinion

- Purpose of Directive is to combat discrimination
- Gender discrimination only permissible if it can be established with certainty that differences between men and women necessitate such differences:
  - Opt out does not focus on clear biological facts; many other factors impact risk e.g. economic, social, individual habits
  - Use of gender as a substitute criterion for other distinguishing features is unacceptable
- Gender is something person has no influence over
- No party submitted that the introduction of unisex rates would seriously endanger private insurance systems

The ECJ judgment – 1 March 2011

- Conclusion consistent with the Advocate General:
  - *"Equality between men and women is a fundamental principle"*
- But a significant focus on the lack of a time-limit for the opt-out clause:
  - *"There is a risk that EU law may permit the derogation from the equal treatment of men and women, provided for in Article 5(2) of Directive 2004/113, to persist indefinitely."*
  - *"such a provision, which enables the Member States in question to maintain without temporal limitation an exemption from the rule of unisex premiums and benefits, works against the achievement of the objective of equal treatment ... and is incompatible with Articles 21 and 23 of the Charter."*
  - *"That provision must therefore be considered to be invalid upon the expiry of an appropriate transitional period."*
  - ***"Article 5(2) of Council Directive 2004/113/EC ... is invalid with effect from 21 December 2012."***

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The ECJ judgment: What we know

- Must use unisex pricing for new policies from 21 Dec 2012

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The ECJ judgment: What we don't know

- Process for implementation
- Ability to collect gender
- Application to policies sold before 21 Dec 2007?
- Application to policies sold 21 Dec 2007 to 21 Dec 2012?
- Scope of unisex pricing for new policies:
  - By product (Group?)
  - By jurisdiction
- Will legislation restrict product design/use of proxies/target marketing
- Does decision impact on underwriting of diseases that impact genders differently
- ... and lots more!

What happens next?

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What are the gender differentials?

Type of business	Differential
Motor Insurance	Females lower at all ages except 80+
PMI	Females 60% higher at ages 35-50 but lower at retirement ages
Mortality	Male 20%-25% higher than Female
Critical Illness	• Male / Female very similar at younger ages • Male higher than Female from age 45
Income Protection	• Female 50%-80% higher than Male • Except Holloway societies!

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How important is gender?

Approximate scale of key rating factors for Term Assurance

Rating factor	Relative importance
Disability (medical underwriting)	> 16 x
Age (60 v 30)	10 x
Smoking status (Smoker v Non-smoker)	2 x
Gender (Male v Female)	1.3 x

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New Term Assurance Business: considerations

- Joint Life and Critical Illness largely unaffected!
- Equalise Single Life premiums (example on next slide)
- Product Design/Target Marketing to seek a disproportionate mix (unless prohibited?)
- Find proxies (shoe size?) to (indirectly) keep gender in pricing
- Underwriting – gender-specific diseases
- Can we still collect gender?

New Term Assurance Business:

Equalising premiums

- Equalise premiums based on previous mix
  - Male premium £8.06; Female £6.71 (age 35, term 25, SA £150,000)
  - Previous mix 60% male, 40% female
  - Equalised premium = £7.52
- But...
  - Allow for any skew in our mix v market...
  - ...and consider how varies, e.g. by sum assured...
  - ...and how demand will differ with unisex pricing...
  - ...and include a margin for uncertainty...
  - ...and include costs for implementation...
- and premium may not be too far away from £8.06!!

The Transition Period

- New Business from 21 Dec 2012 .... but when will we know the new legislation?
- Substantial systems impact
  - Lower if can collect gender in application process
- Early or late adopter?
- Prioritisation of changes by product
- Need to allow for retrospection (if applicable)
- Need to allow for antiselection
- IFAs may target one gender (“Buy now while stocks last”)
- Dec 2012 review clause?
- Test future targeting strategies?

Existing Business

- How far will retrospection apply?
- Can reduce premium for one gender – but can we increase for the other gender?
- How to equalise premiums?
  - Dependent on actual business mix?
  - To what level of granularity?
- Joint Life business may be affected
- Major impact on profitability of in force blocks with high quota reinsurance, if reinsurer not obliged to alter rates
- May be forced to review Underwriting decisions
- IT
- Communications/Complaints

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Implications for pensions

- Direct Impact
- Possible Indirect Implications

Direct Impact – DC annuity purchase

- Current Annuity pricing:
  - Current rates @ 65 for a level annuity, £100,000 Fund
  - Male £6,000 p.a.
  - Female £5,500 p.a.
  - Expect to pay male for 24 years, female for 21 years
- Future Annuity pricing:
  - Look at current gender mix
  - Add margin for uncertainty
  - Consider future gender mix – affluent males may defer/not purchase
  - Rates could end up close to current female rates?

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Direct Impact

- DC:
  - Future Annuity purchase by individuals will be unisex
  - May be benefit in purchasing annuities for males before 21/12/2012
  - Trust-based advantage over contract-based for males?
  - Disincentive to pension savings for Males?

- DB:
  - Few if any direct implications

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Indirect implications – DB schemes

- Unisex transfer values
- Bulk annuity purchase
- Actuarial factors
  - Cash commutation factors
  - Early or late retirement factors
- Selective annuity purchase
- Legal challenges due to equality drift?

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Please Note...

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I am an actuary – not a lawyer

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ANY QUESTIONS?