

Income Protection Business

The Impact of the Tax Changes

Michael Porter

Head of Client Solutions

RGA Reinsurance Company of South Africa

mporter@rgare.com

+27 79 494 1016

September 9, 2014

Meet my friends



- Mr Geyser, a plumber
- Earns R40,000 pm
- Bought IP policy for R1,000 pm
- Taxable income reduced by R12,000
- MTR = 35% so pays R4,200 less tax



Fast forward to June 2016

- Mrs Geyser is becoming anxious
- Mr Geyser submits his tax return
- SARS refunds him R4,200 less than last year!



Meet my other friends



- Mr Volt, an electrician
- Earns R50,000 pm
- Bought IP policy for R50,000 pm
- Claim of R50,000 pm
- His insurer deducts R15,000 pm

Fast forward to March 2015

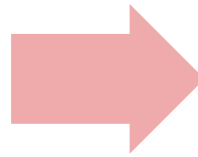
- The insurer stops deducting the R15,000!
- Mr Volt is so happy, says to his wife “no chance I’m going back to work!”
- Mrs Geyser is so happy too!



The tax change

Currently

- Premiums are tax-deductible
- Benefit are taxable



From March 2015

- Premiums are not tax-deductible
- Benefit are tax-free

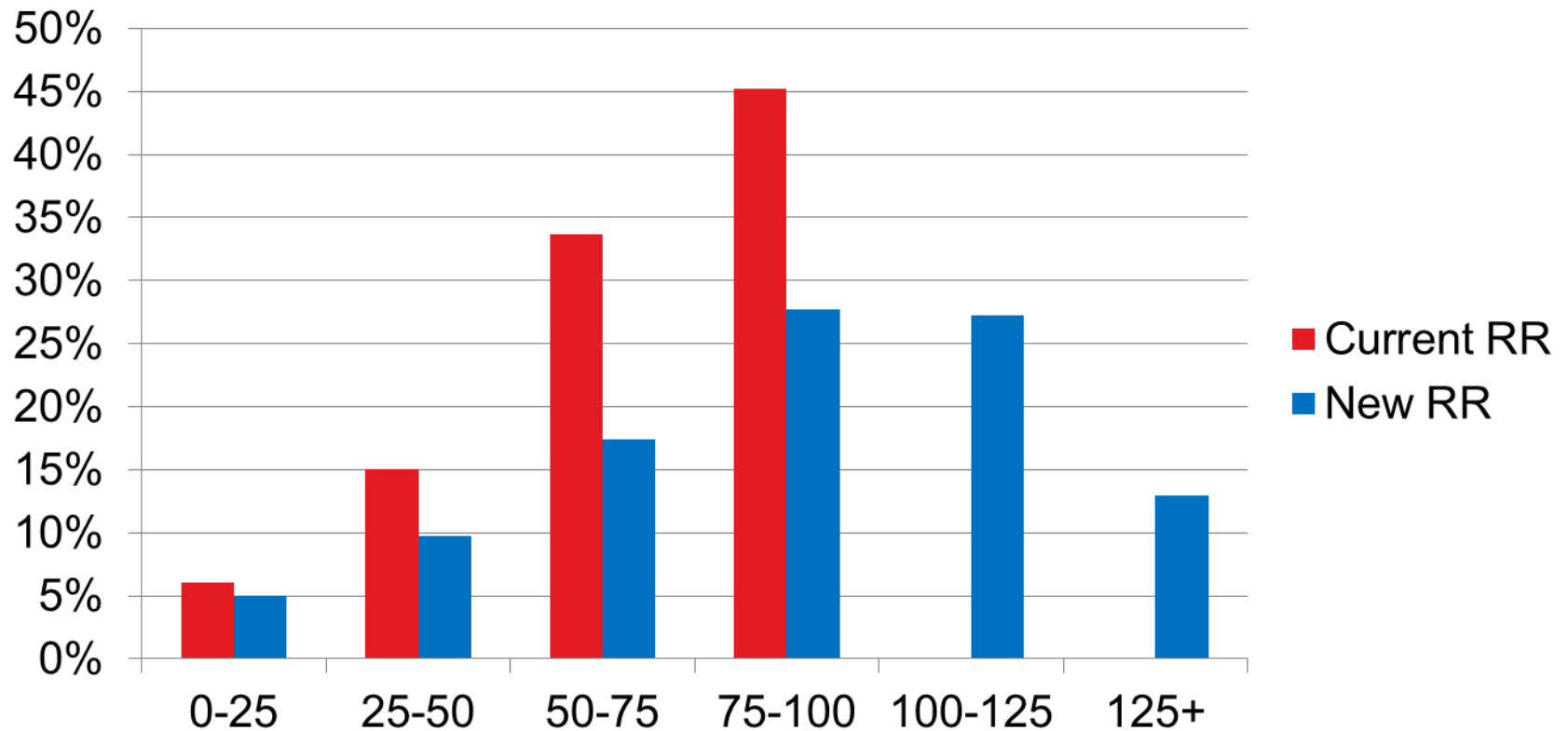
Replacement ratio

$$RR_{\text{current}} = \frac{\text{net of tax benefit}}{\text{net of tax salary}}$$

$$RR_{\text{new}} = \frac{\text{gross of tax benefit}}{\text{net of tax salary}}$$

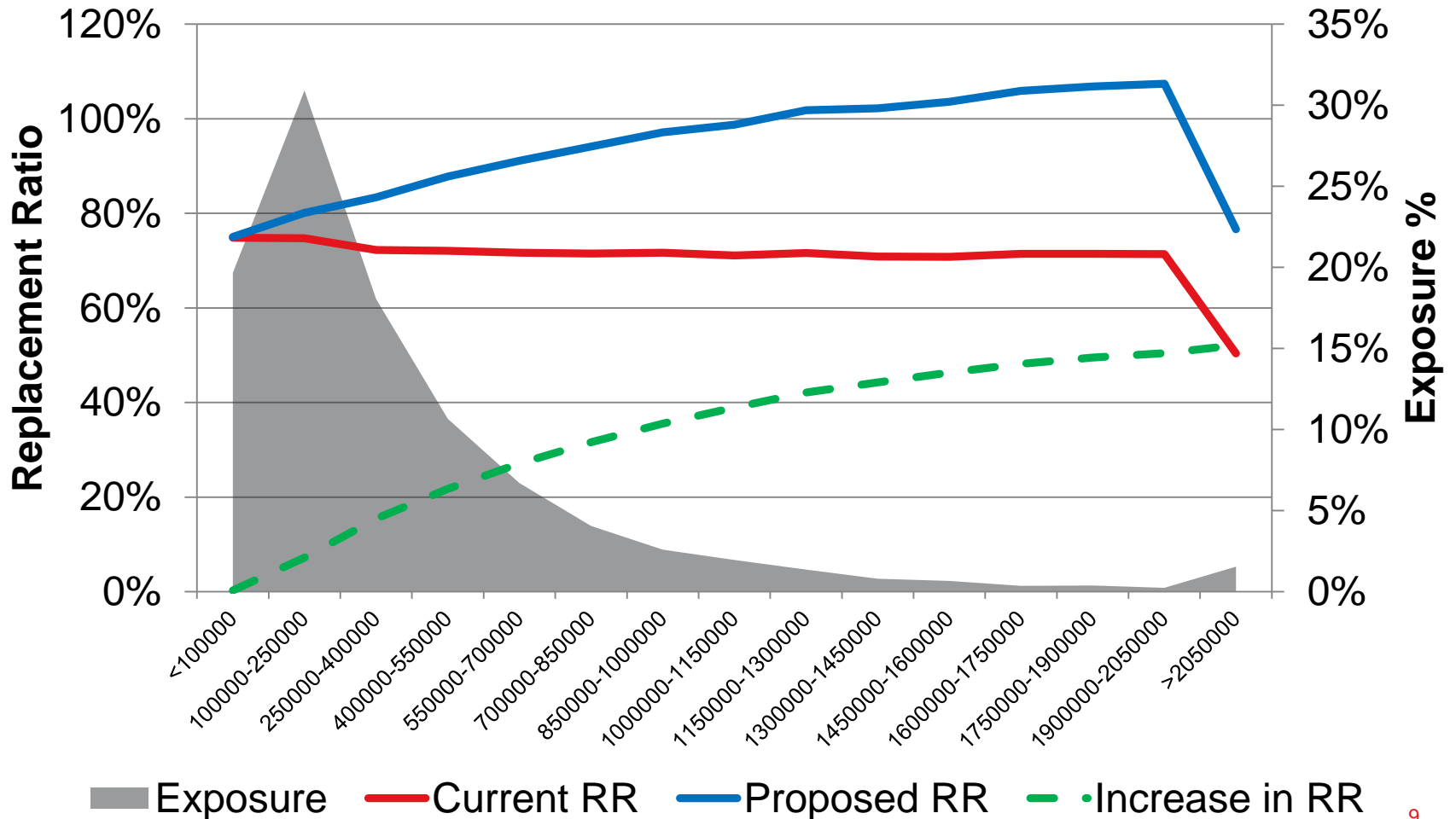
Increase in replacement ratio

Individual business



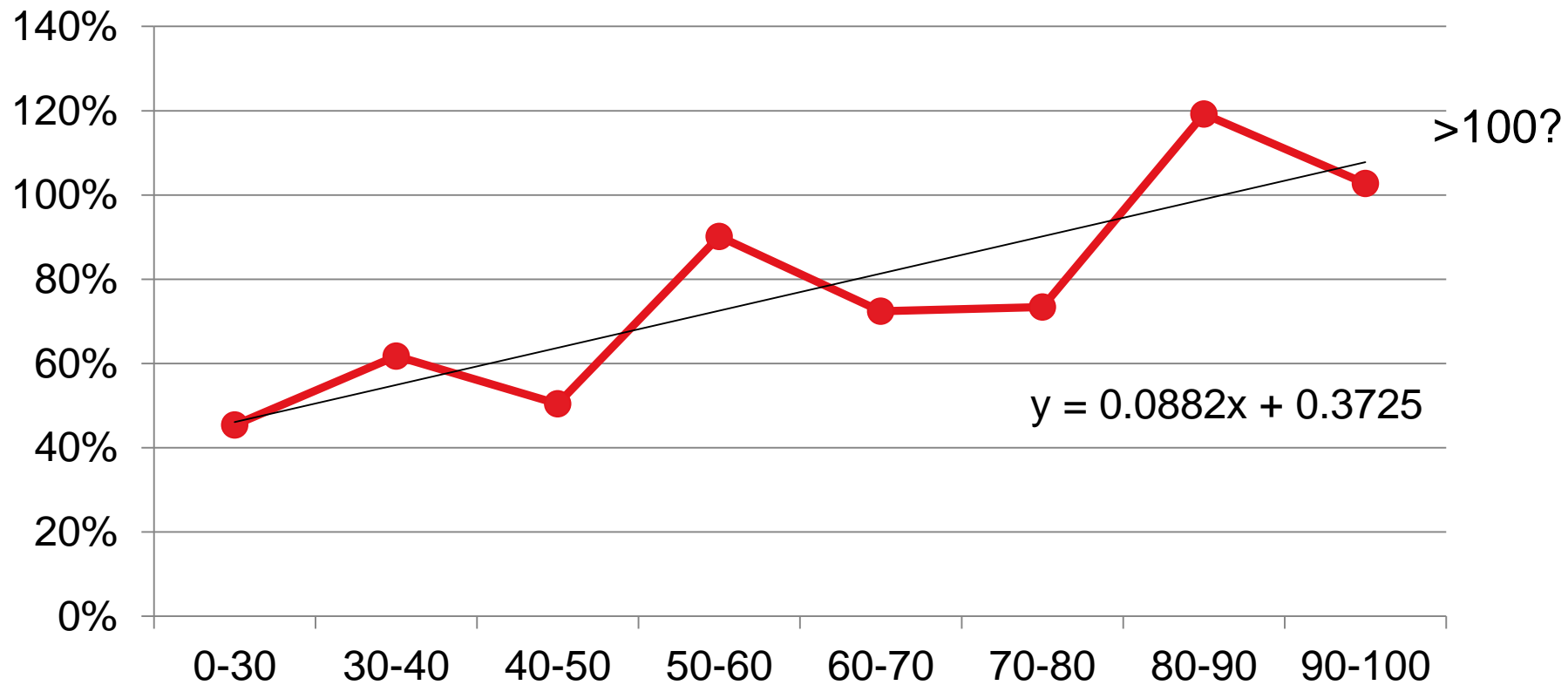
Increase in replacement ratio

Group business



Actual claims / Expected claims (rebased)

Individual business

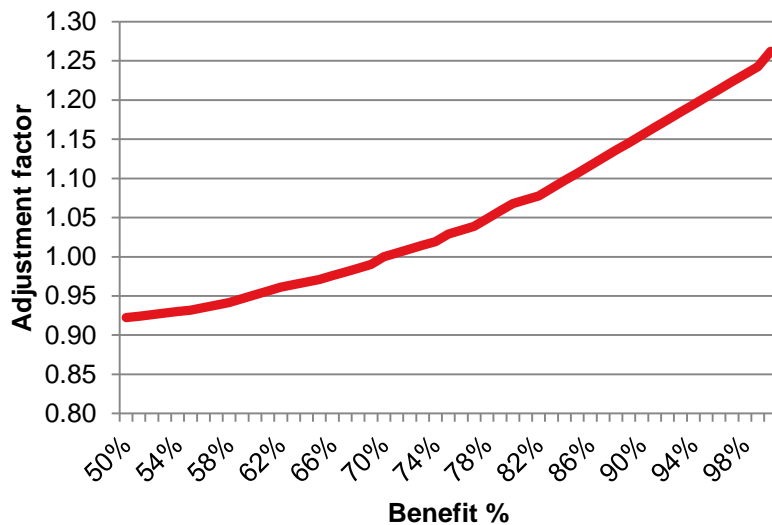


Consistent with group business practice in other markets

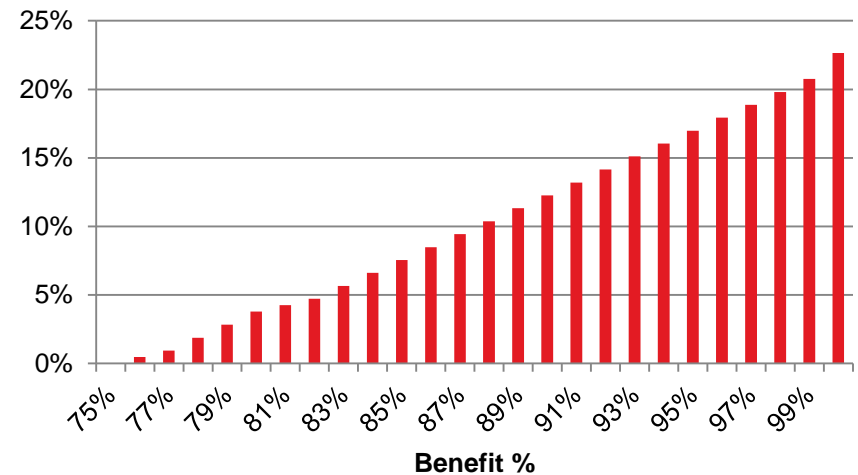
- Australia
 - Rule of thumb: 1% for every 1% additive increase

- US

US Group Insurer

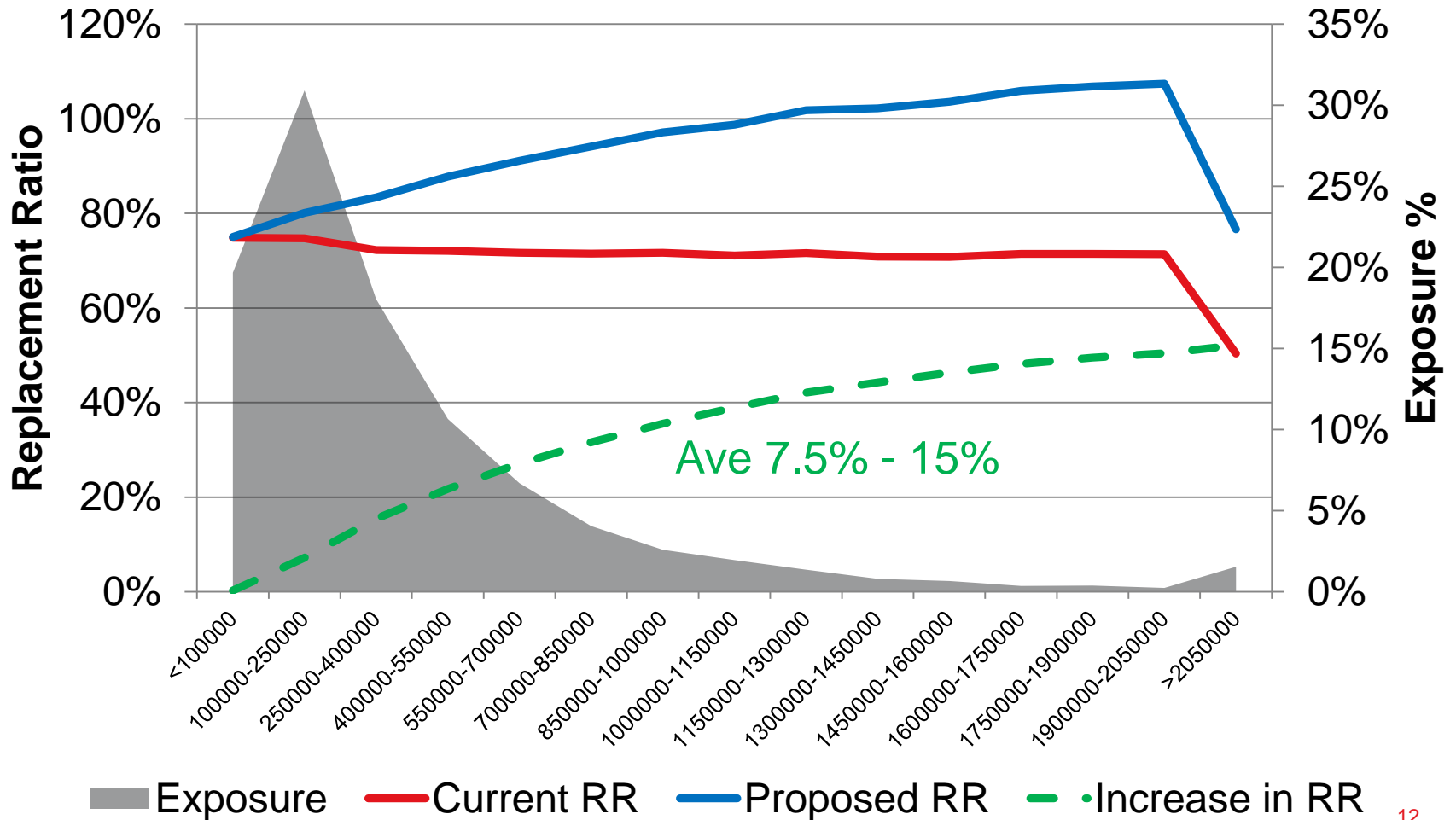


Relative increase in factor from 75%

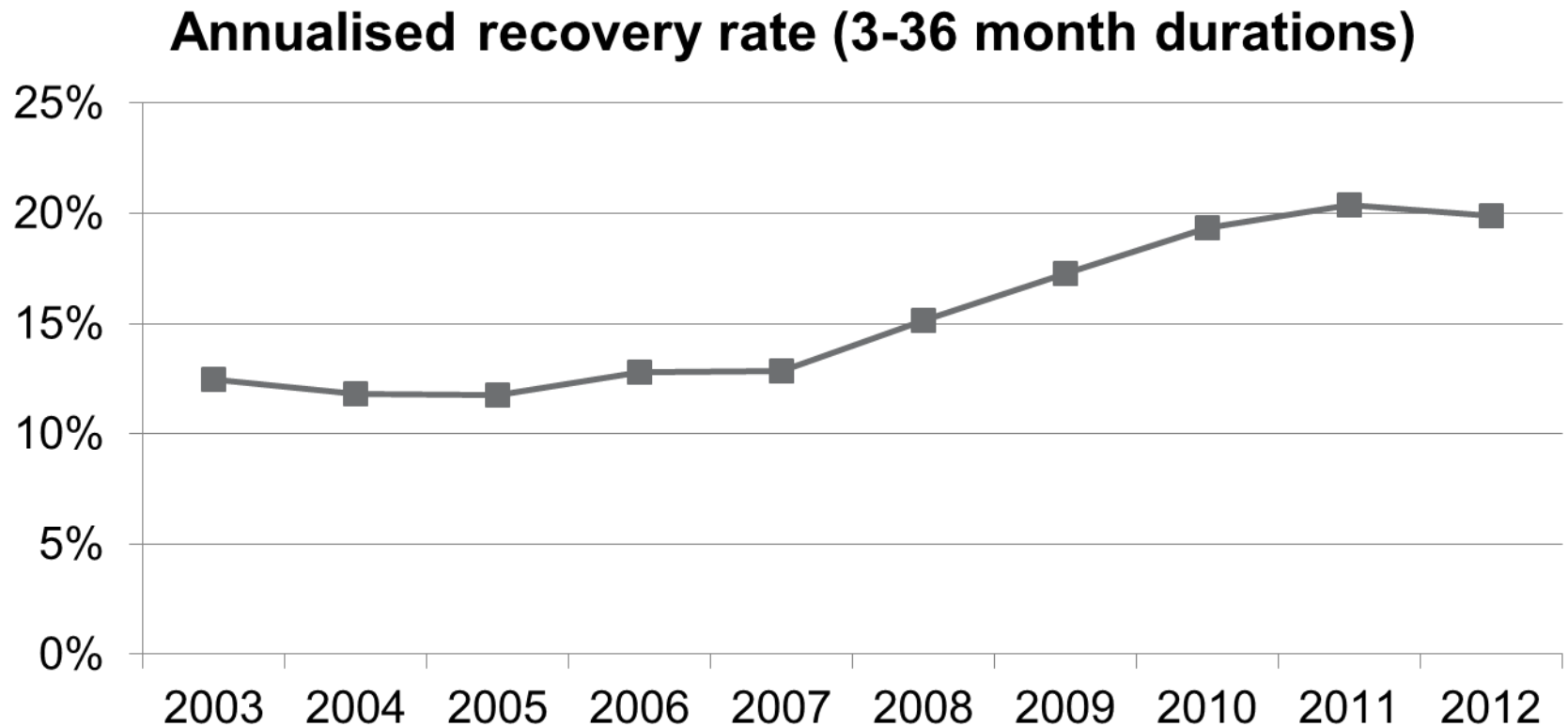


Potential cost

Group business



The impact of claims management



RGA

RGA

Response Options

Three aspects to consider

In-force claimants

In-force business

New business (and renewals)

In-force claimants

1. Do nothing
 - Increase reserves (lower terminations)

2. Proactively manage claimants back to work
 - As many as possible before 1 March 2015 – start now!
 - Focus on large covers where tax rate is high
 - Focus on the right claims causes
 - Guaranteed payment periods

3. Offer to commute income payments

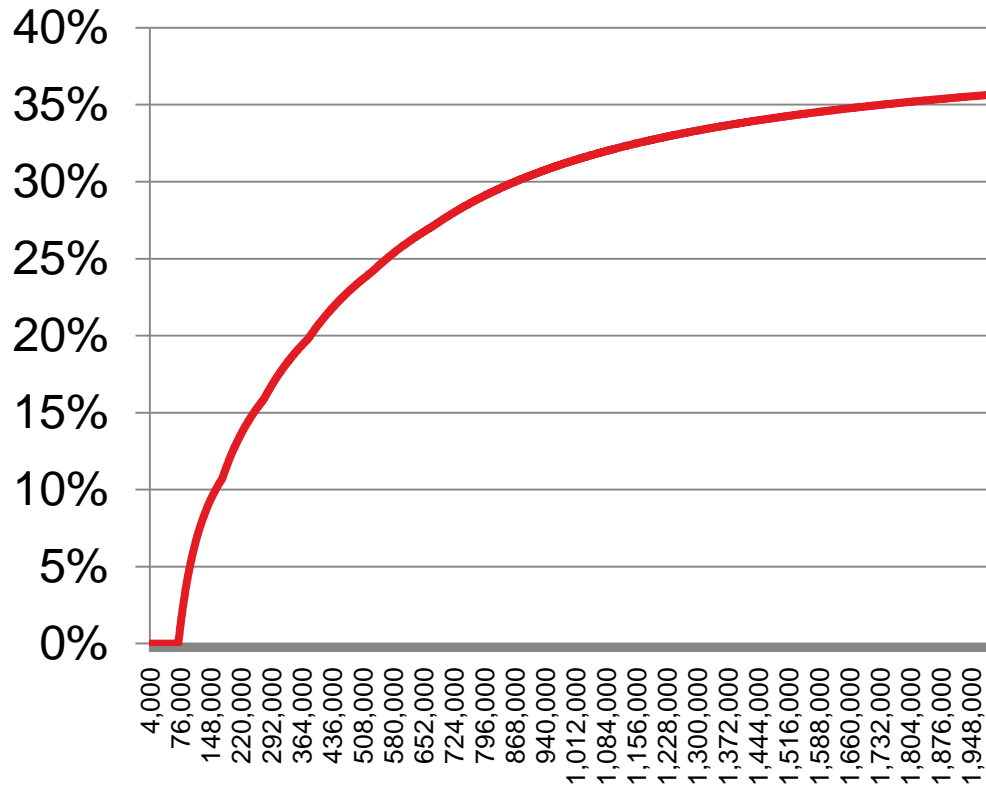
In-force and new business (and renewals)

1. Do nothing
 - Higher incidence and lower terminations
2. Step up claims management
3. Impose a max cover amount (PTO)
 - Doesn't fully solve the problem
4. Reduce cover
 - Prevent unexpected tax bills
 - Consider impact on policy size – fixed expenses
 - Consider impact on financial adviser – commission claw backs
 - Offer replacement cover?
5. Monitor RR distribution and claims experience and adjust rates

Maximum cover

75% * Gross salary * (1 - t)

Ave tax rate

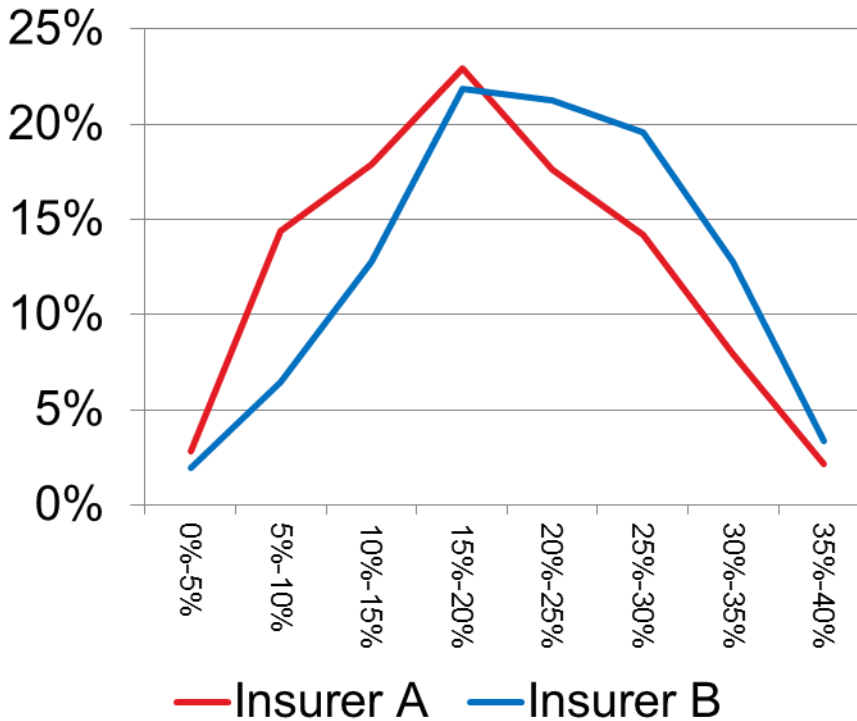


- Exact tax rate for each p/h
- Salary bands
- Tiered using MTR
- Same rate for all p/h

Maximum cover

Same rate for all p/h

Disbn of ave tax rate



- Too generous for high earners
- Too penal for low earners
- Market war?

Concluding remarks

- We think there is a cost impact
- You can limit this
- If you can't, you may need to adjust best estimate assumptions



RGA

RGA

Thank you for your attention.