

Important changes to income protection insurance in 2021

By Brad Gecelter

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What happens if you're sick or injured but you depend on your income to pay your mortgage and support your family? If you're permanently employed, there's sick leave. But if you're self-employed, own your own business, or run out of leave, then income protection insurance, also known as salary continuance, is many people's safety net.

However, significant changes are underway for income protection insurance and it's important people know how it might affect them.

Why is Income Protection Insurance changing?

The Australian Prudential Regulation Authority (APRA) has mandated changes to income protection insurance to make the industry more sustainable after many insurers were consistently losing money. Some changes have already been made and others will be starting from 1 October, 2021.

The key changes for business owners and those with fluctuating incomes

The changes most likely to make a significant difference are those to the way in which individuals' income is assessed. Previously, individuals could take out insurance policies that locked in a level of coverage, based on their income at the time of application, so-called 'Agreed Value'.

1. Insurers will no longer be able to assess claims under an 'own occupation' definition until they are fit to perform their own occupation. Instead they will be assessed under 'own occupation' for the first two years, then assessed under 'any occupation' definition based on their experience, education and training. This is a huge shift by the insurers, as currently and up until October the insured will and has always been continually assessed under OWN occupation until the expiry of the policy.
2. Insurers must stop basing benefits on a person's income at the time of application and instead must use their income at the time of claim. For those with stable incomes, that means the income earned in the previous 12 months. For people with variable incomes, their past earnings will be averaged over a 'period of time' and reflective of future earnings lost as a result of the disability.

This could have a big impact on business owners who, for example, might have two very good years and then go through a lean patch or take extended time off work. If they are then injured and make a claim, their payout could be significantly less than they expect.

3. The income replacement ratio, which is the level of benefits paid in the event of a claim. Previously, this was left to the discretion of the insurance company but in future it will be limited to a maximum of 90% of their pre disability income for the first six months, and 70% after that.

Deferral of implementation of policy contract term measure

We are pleased to announce that APRA has deferred the following change to 1 October 2022.

- **Revised contract terms**

Insurance policies must be limited to terms of five years. Every five years, insurance companies will be able to review an individual's income, occupation and personal past-times (like dangerous hobbies) and then be allowed to make changes to the policies, and the premiums, before insurance is renewed. However, an individual's health **will not** be in scope to be reviewed.

The impact of changes to income protection

The good news for people with current income protection policies is that those policies are not impacted by the changes. With significant change happening soon though, it's a good time for people to review their policies to see if they are still fit for purpose before the changes come into effect.

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