

Short-Term Disability: Where are We?

Tuesday, October 17, 2006

Session #68 – Panel Discussion

Panelists

John Murphy, FSA, MAAA – Disability RMS

Scott Haglund, FSA, MAAA – Milliman, Inc.

William Bossi, FSA, MAAA – Disability Insurance Specialists, LLC

Moderator

Peter Heinrichs, FSA, MAAA – Gallagher Re, Inc.

Peter Heinrichs - Vice President and Marketing Actuary, Gallagher Re, Inc.

Pete is responsible for providing actuarial and analytical support for Gallagher Re's life, accident and health clients, prospects and brokers, and to liaise with the actuarial staffs of Gallagher Re's Global Analytic Team, clients and reinsurance markets.

Pete has 16 years experience in the group insurance and reinsurance arenas, specializing in group life, disability and critical illness insurance. Prior to joining Gallagher Re, Inc., he was Director - Actuarial Services for Unimerica Workplace Benefits, where he served as the lead group disability and critical illness actuary. He has led the actuarial departments of Disability Consulting Group and The Hartford's Group Reinsurance Plus, and has worked with several group insurance carriers and an actuarial consulting organization.

Pete has a Bachelor of Science in Mathematics and Statistics from the University of Michigan, and is a Fellow of the Society of Actuaries and a Member of the American Academy of Actuaries.



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John Murphy – Assistant Vice President, Actuarial, Disability RMS

John is responsible for pricing of LTD, STD and Critical Illness products at Disability RMS. This work involves the pricing, valuation, experience analysis and forecasting of the business assumed by our various facilities.

John gained 14 years of disability insurance experience while working at Paul Revere, Provident, UNUM and UnumProvident. His responsibilities included pricing, valuation, analysis, planning and reporting and forecasting. For the last 4 years, he has been a disability reinsurance actuary at DCG and Disability RMS.

John holds a bachelors degree in mathematics and economics from the University of Massachusetts, and earned his Fellow of the Society of Actuaries designation in 1996.

Scott Haglund – Consultant, Milliman USA

Scott is involved primarily with individual disability, group disability and group life. With these products, he is responsible for projections, valuations, experience reviews and pricing of insured and self-insured plans. He is involved with insurance companies, employers and brokers across these industries.

Scott has gained over 20 years of disability and life experience while working for Minnesota Life, Assurant and the Principal Financial Group. While at these companies, he was involved with product development, pricing, financial reporting, rate and product filings, cash flow analysis and underwriting guidelines and pricing of large (2,000+) and small case employers. He recently has joined the Milliman USA firm based in Portland, Maine.

Scott attained the designation of Fellow of the Society of Actuaries in 1995 and is a member of the American Academy of Actuaries.

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William Bossi - Co-Founder and Managing Member, Disability Insurance Specialists LLC

Bill provides actuarial, financial, and strategic consulting services to client insurers and reinsurers, and manages the delivery of outsourced TPA services. Disability Insurance Specialists is a TPA operating in the disability, long-term care, and critical illness markets, and also provides full product development and filing services to direct carriers.

Bill has almost 30 years of insurance experience, 17 of which have been predominantly focused on disability and other health products. He began his career working for insurers in a variety of actuarial, financial management, and executive positions. His prior experience includes time with CIGNA, Connecticut Mutual Life, and Monarch Life. Bill has been an independent consultant and entrepreneur since 1993.

Bill earned a B.S. degree in Mathematics from Carnegie-Mellon University and became a Fellow in the Society of Actuaries in 1983. He is Immediate Past-President of the Learning Disabilities Association of CT and currently serves as Treasurer for that non-profit agency.

Where are the Profits?

A STD Reinsurance Perspective

2006 STD Sales/Earned Premium
YTD as of June 30

	Company	STD Sales Premium	STD Earned Premium
		(#'s in Millions)	
1	Hartford Life	62.2	272.8
2	UnumProvident	41.9	269.7
3	MetLife	22.7	129.0
4	Standard	22.4	104.0
5	Lincoln Financial Group	21.4	92.3
6	Prudential	20.7	87.3
7	Guardian Life	19.5	73.6
8	Aetna	18.8	56.7
9	Reliance Standard	17.5	49.1
10	Cigna	13.9	48.1
	Total Top 10	261.0	1,182.6
	Total Survey	354.9	1,526.5
	% of Total from Top 10	74%	77%

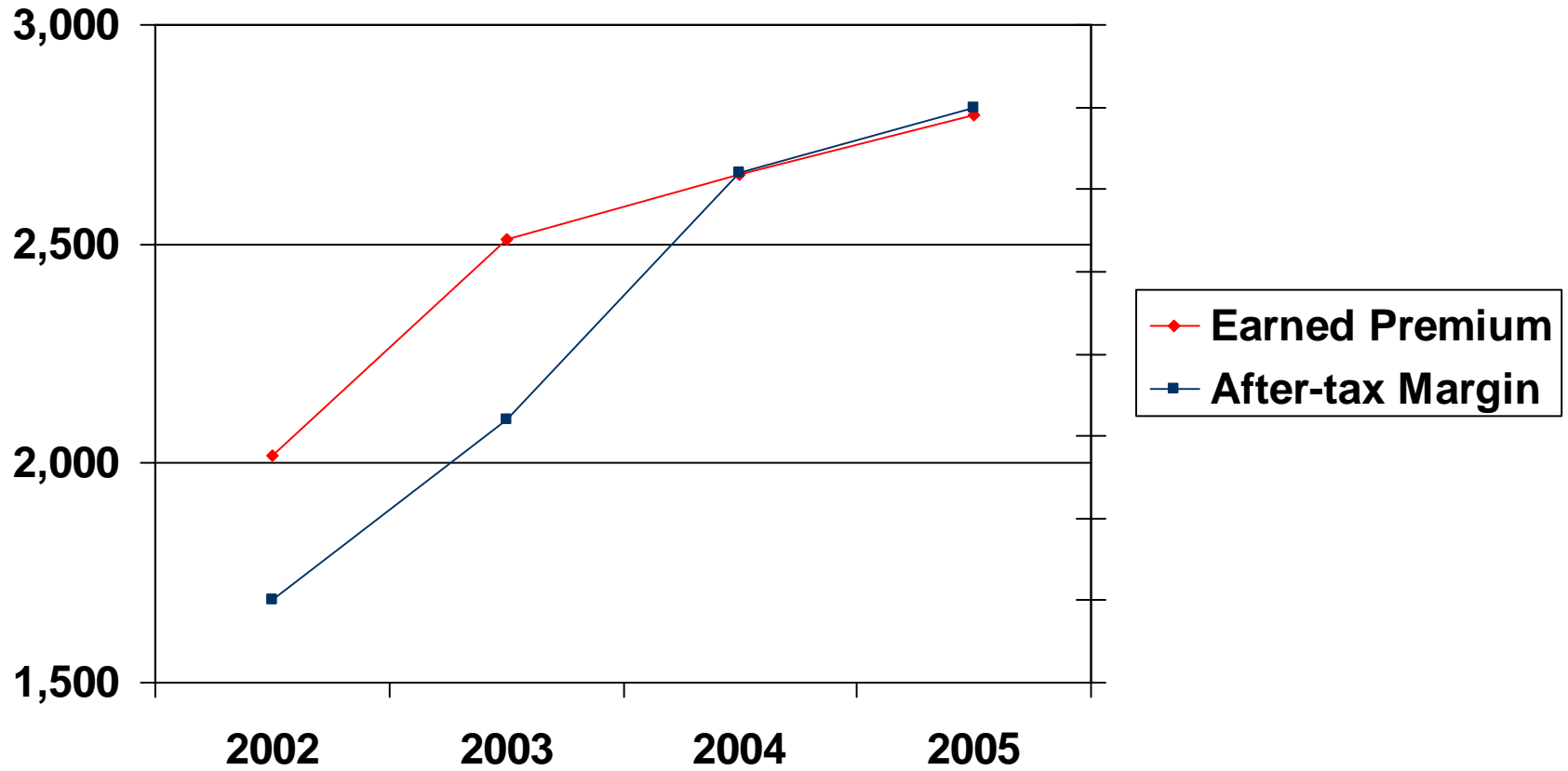
Anatomy of an STD Dollar

▪ Claims	65 cents
▪ Commissions	8 cents
▪ Acquisition	4 cents
▪ Claims Adjudication	6 cents
▪ <u>Admin/Taxes</u>	<u>12 cents</u>
▪ Total Expenses	30 cents
▪ Profit	5 cents

Why is Target Profit Low?

- Capital Requirements
- ROE models show not much profit needed to earn target ROE
- Result is lower margin for error

STD Premium and Profit Margin



Underwriting/Pricing – The Conventional Wisdom

- Experience is reliable
- More Predictable
- Easier to Correct
- The Manual doesn't matter

Underwriting/Pricing – The Reality

- STD experience is more credible than LTD
- Too much emphasis on the current year
- Too little concern for volatility
- The manual matters if appropriate credibility levels are used

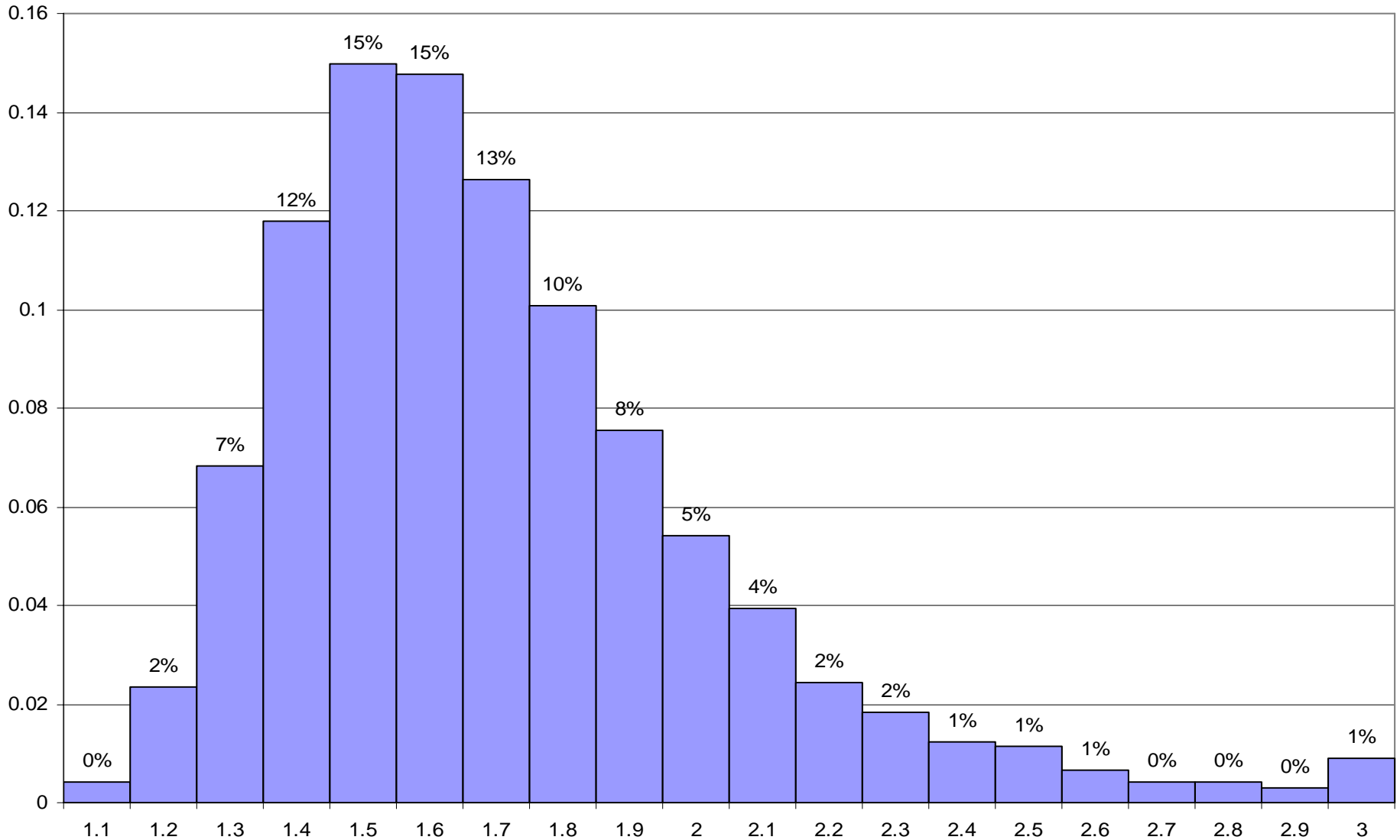
Underwriting/Pricing – The Reality (Cont)

- The results are known quickly
- Mistakes are just as hard to correct
- Persistency drops when rate increases are sought
- A regimented pricing strategy leads to lower renewal increases and higher profits

Underwriting/Pricing – The Reality (Cont)

- When confidence in the manual is low, discounting is high
- Results in discounts in the wrong places
- Get comfortable with your manual and guidelines
- Expect to be out of the running often

Distribution of Ratio of Max/Min Manual Rates for STD



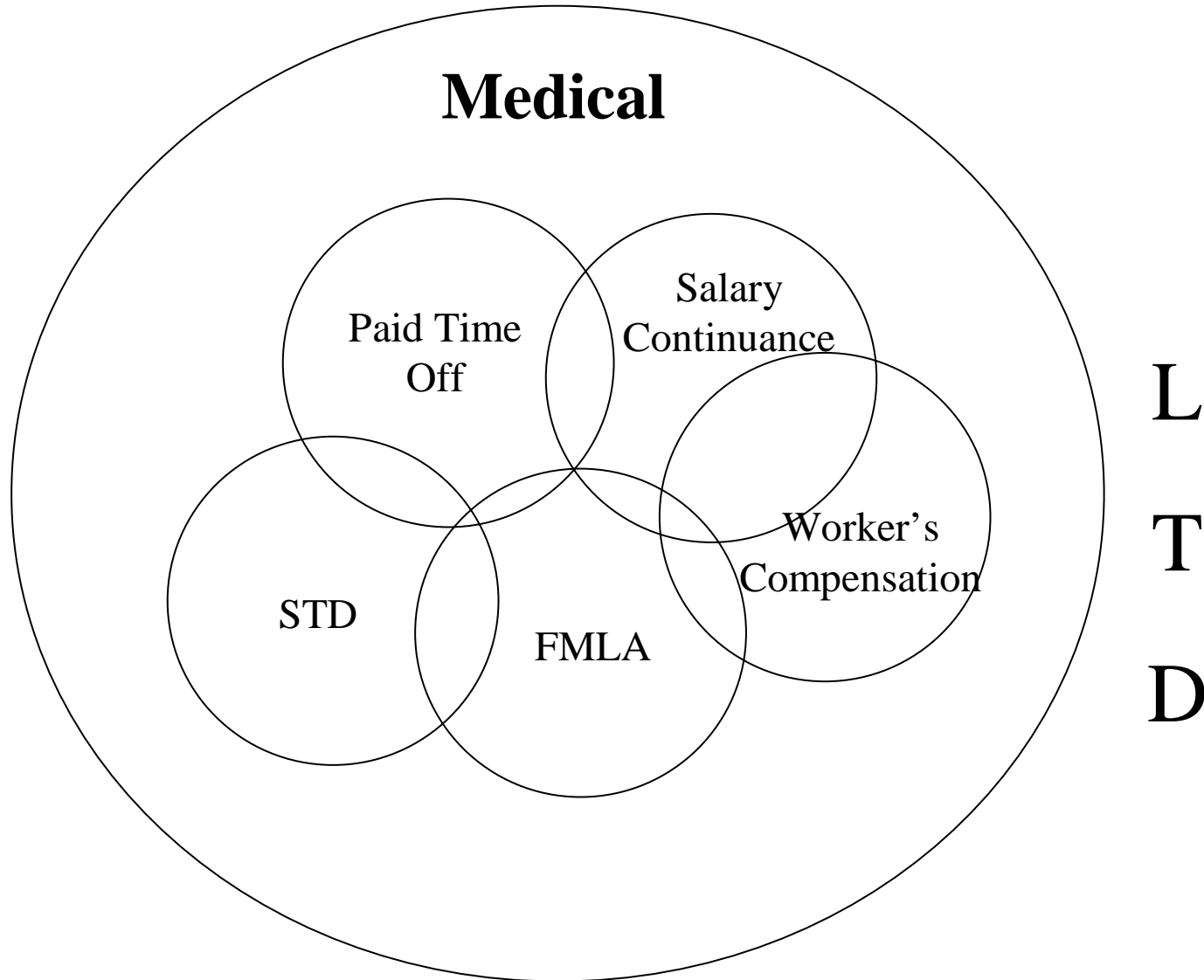
The Profit Strategy

- Accept slower growth for higher profits
- Better risk controls – better profits
- Be Aware of Low Margin for Error

Underwriting and Risk

- Resurgence of 24 Hour Coverage
- ASO → Insured
- Larger Cases
- General Rating

Resurgence of 24 Hour Coverage



Resurgence of 24 Hour Coverage

- What happens when combining coverage
- Measuring benefits of absence management
 - ASO fee impact
 - FMLA impact
 - Employee absence impact

ASO to Insured

- Expected Savings (??)
- Expected Changes
- Consider

Claim Cost = Number x Length x Size

Larger Cases

- What do they know you don't
- Why insured (why now)
- Expected length of coverage
- Experience review

General Rating

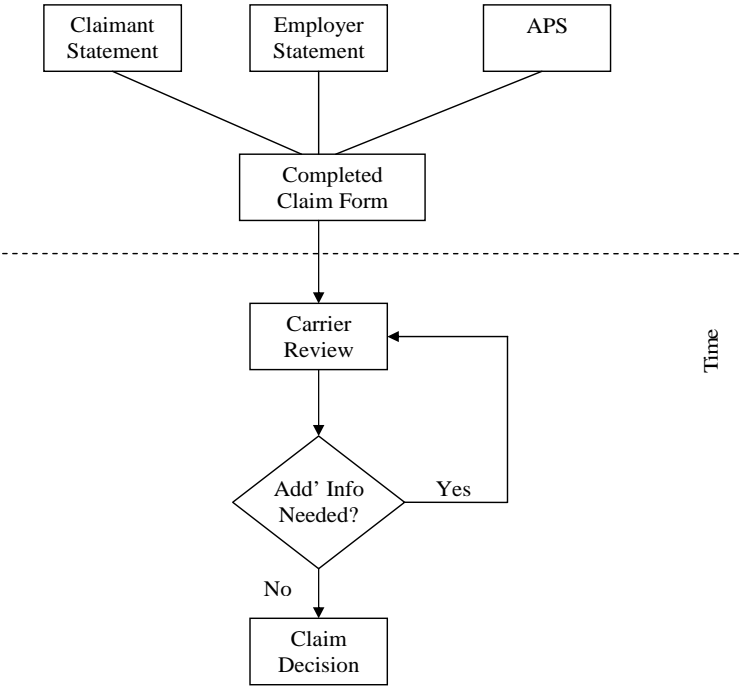
- Low margin
- More underwriting and actuarial discipline needed
- Futurism → what can you do to reduce uncertainty

Risk Environment

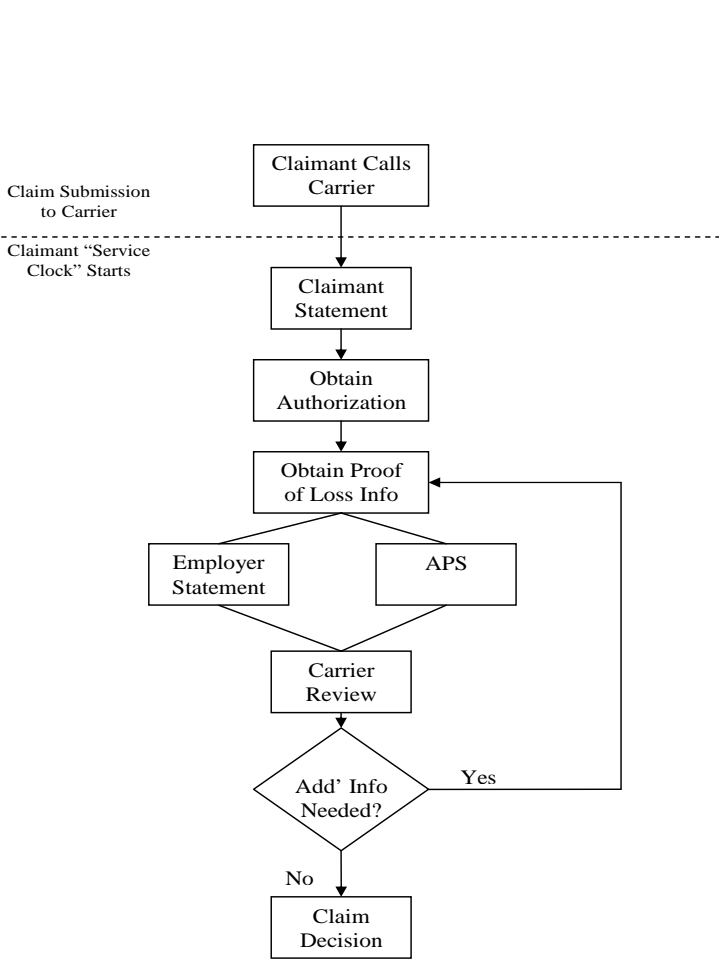
- Traditional ER STD vs. Voluntary STD
 - antiselection
 - contestability
 - pre-ex conditions
 - impact on expenses
- Medical Management vs. Policy Adjudication
 - what's appropriate to the specific situation?
- Customer Service Focus
 - paper vs telephonic claim submission methods

Claim Submission Workflows

PAPER Claim Submission Model



TELEPHONIC Claim Submission Model

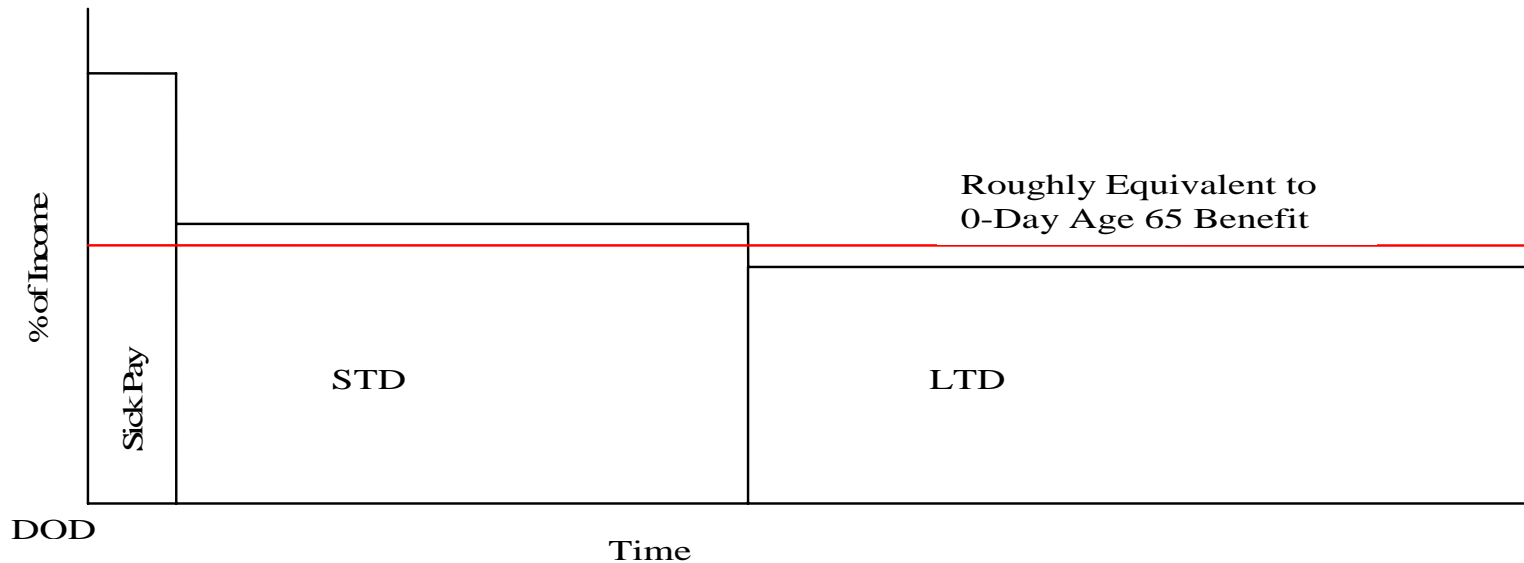


Time



Risk Environment

- Integrated coverage
 - What is it really?
 - What does it cost?



Claim Management

- STD Profitability is very sensitive to claim duration
- If pricing anticipates 65% loss ratio and 5% profit, and average claim duration is 50 days, then a 1 day increase in duration adds 2% to claim costs (equal to 1.3% of premium)
- Additional claim costs of 1.3% of premium drops after-tax profit margin to 4.15% or 83% of expected
- » **A 1-day difference in expected claim duration is worth 17% on the bottom line!**

STD Claim Management - Operational Challenges

- Quick turn around time for decisions
- Accuracy of payments
- Offsets, integration, and overpayments
- Written policy vs. sold policy
- Claim submissions before policy issuance
- Communication demands
- Phone call volume

Claim Management

- Maternity Claims
 - % of claims
 - duration vs. other disabilities
 - adjudication challenges
- Claim Adjudication consistency with pricing
 - claim reality vs. pricing assumptions

Sensitivity to Claim Duration

Pricing Basis					
Census Data		Weekly Benefit	Expected Incidence	Average Claim Duration (wks)	Expected Claims
M 20-40	150	\$ 875	5.0%	5.5	\$ 36,094
F 20-40	250	\$ 750	10.0%	8	\$ 150,000
M 40+	300	\$ 950	7.0%	10	\$ 199,500
F 40+	300	\$ 900	7.5%	9	\$ 182,250
	1000				\$ 567,844
Actual Basis					
Census Data		Weekly Benefit	Incidence	Average Claim Duration (wks)	Claims
M 20-40	150	\$ 875	5.0%	5.5	\$ 36,094
F 20-40	250	\$ 750	10.0%	9	\$ 168,750
M 40+	300	\$ 950	7.0%	10	\$ 199,500
F 40+	300	\$ 900	7.5%	9	\$ 182,250
	1000				\$ 586,594
					103.3%

» **Profit margin is 57% of expected**