RECORD OF SOCIETY OF ACTUARIES
1981 VOL. 7 NO. 2

NATIONAL ISSUES INVOLVED IN LOSS-OF-TIME COVERAGE

Moderator: CARL L. LOEFFEL. Panelists: CHARLES C. BLACK, JOHN C. CATON

1. Government plans and association and group plans
   a) Survey of situation in Canada and United States
   b) Purpose of the plans
   c) Financial experience of the plans

2. The future of private loss-of-time insurance
   a) Overinsurance from government, association and group plans
   b) Financial experience
   c) Policy design, underwriting and pricing implications

3. How can actuaries effect the environment in which loss-of-time coverages will be written and regulated through
   a) participating in solutions to these problems and
   b) affecting future laws and regulations

MR. CARL L. LOEFFEL: Over the past decade there have been substantial changes within the private and public sectors and in public attitude concerning loss-of-time coverage, and there is no indication that this rate of change will slacken. We have witnessed in the private sector a major increase in people covered, a trend toward long term coverage, a substantial increase in indemnity limits, and an introduction of new or revised forms of coverage. In the public sector, we have seen substantial changes in benefit levels available from such major programs as Social Security, Worker's Compensation and State Cash Sickness plans. Indeed, the change is sufficient enough that the title of this session refers to "loss-of-time" rather than "disability income."

Public concern for the disabled has been intense and pervasive. While we may be primarily interested in insuring income, witness the concern in other areas. Additional care is now required to design and retro-fit buildings to accommodate the disabled; school systems are adopting programs to include handicapped students with other students; public transit systems are acquiring equipment to accommodate the physically handicapped. In fact, 1981 has been declared the international year of the disabled person.

On the other hand, I sense that the public is finding out that many of these innovations are costly. In the loss-of-time coverage area we have witnessed increased claim costs from those 10 years earlier. In the public sector costs for Social Security and Worker's Compensation systems have accelerated.

To discuss this timely subject we are fortunate to have Mr. Charles C. Black, an actuary from the Canadian Life and Health Insurance Association, to discuss the Canadian situation, and Mr. John C. Caton, Vice President and Actuary of the American United Life Insurance Company, to discuss various forces having an impact on loss-of-time insurance. Our first speaker, who was to speak on the United States situation, is unable to attend and, hence, I will merely pinch-hit by mentioning several items, hoping they will lead to further discussion.

In commenting on loss-of-time coverage in the United States, let me refer you to the report, "Compensation Systems Available to Disabled Persons in the United States". This is the result of a study done by the Disability Insurance Committee of the Health Insurance Association of America. Under the Federal Government area the largest program is the primary and dependent benefits of the Social Security System. Additionally, there are programs for defined groups of people, such as members of the armed forces, veterans, federal employees, civil servants, longshoremen, railroad employees and miners (black lung disease). At the state and local government level, there are a number of programs, mandated or controlled, such as: Worker's Compensation, State Cash Sickness, Vocational Rehabilitation, Supplemental Security Income, and various other programs that may include benefits other than cash such as food stamps.

In the association and group plan area, loss-of-time benefits may develop from employer, employer/union or association type plans. The vehicles used to provide these include:

1. insured long-term and short-term disability programs

2. self-funded programs

3. salary continuance programs

4. special programs such as travel accident

5. waiver of premium and other disability benefits built into other security programs such as life insurance, deferred compensation, profit sharing and retirement programs.

In the association and group plans there has been quite an expansion in the insured long-term disability area. Compared to ten years ago, the number of people so covered has more than doubled. However, over the same time period, the number covered under insured short-term disability plans has only grown slightly. I suspect what has happened is that we are having more plans where the employer has a self-funded short-term or salary continuance plan, and then perhaps an insured long-term plan.

One problem in dealing with public sector plans has been the inability to coordinate benefits, especially with individual contracts. In response to this we have seen the introduction of forms that pay when Social Security, for instance, does not pay.

We, as actuaries, should be participating in professional and trade associations, including activities of committees and task forces that are organized for specific purposes. Additionally, we should be gathering more data that confirms or denies our practices. In a changing and questioning world, we will need to have such data to defend the use of these practices to regulators and the public. Lastly, in the area of legislation and regulation, we must be more active. While at least some of us desire less regulation, we must see the writing on the wall and take a more active role in pursuing favorable legislation and regulation. This will be an ongoing situation, where we are going to have to spot problems and construct laws and regulation so as to most effectively fulfill the needs of the public, before someone else does.

As perhaps many of you realize, beginning January 1, 1981, the Canadian Life Insurance Association and the Canadian Association of Accident and Sickness Insurers merged to form the Canadian Life and Health Association, and, at about the same time, Charlie Black joined the association working in the health area. We will be most interested in developments in Canada and your comments.

MR. CHARLES C. BLACK: There is a tendency in Canada for government involvement to come faster. National Health Insurance is a good example of this. In the late 50's and early 60's, we saw the government take over hospital insurance, and about a decade later, at the end of the 60's, a comparable takeover of medical insurance. On the other hand, in the United States, there has been much discussion, and it seems currently the possibility of nationalization of the health insurance field is much less than it has been.

In the disability field, or the loss-of-time area, we have in Canada a program of comprehensive benefits that is generally comparable to your Social Security System. It provides pension benefits, survivor benefits, and disability benefits and covers essentially all earners in Canada, whether they are self-employed or employed wage earners. The contribution rate is one distinguishing feature; our maximum contribution for 1980 was $212 by the employee, 1.8% of the first $13,000 approximately. In 1981 it will be about $233. The low contribution rate leads to the common feeling that the benefits do not cost very much. The overall benefit to cost ratio is very appealing to the public and they are not so concerned over the high taxes for Social Security as we hear from the United States.

This plan is really two separate plans. The Quebec Government operates their own plan called the Quebec Pension Plan, and the Canada Pension Plan covers the rest of the country.

These disability benefits under the national plan are much more modest than under the Social Security plan. The maximum disability benefit for the principle wage earner is about \$300 per month. On top of that, he would qualify for children's benefits which would add about \$43 per month, per child. There is no age slope as in the United States plan. The benefit tends to be flat, although it is earnings related, but only for people earning less than the maximum amount which, in 1980, was just over \$13,000 per year. This benefit has a four month waiting period and it continues to age 65.

Another benefit is available to almost all wage earners in our Unemployment Insurance Plan which again is a national plan. It has a short term disability benefit of 15 weeks following a two week waiting period, filling in the waiting period of the Canada and Quebec Pension Plan benefits.

In both instances, the disability benefits are associated with other major benefits that really led to the introduction of the plan. Disability benefits came along as an addition. The pension benefit was the key ingredient in introducing the Canada and Quebec Pension Plans. The unemployment insurance benefit for lay offs was the reason for the unemployment insurance scheme. Under unemployment insurance, the disability benefit was a loss leader to attract some groups into it. For example in 1971, when it was introduced, the teachers objected to being included. At that time no one heard of a teacher being unemployed. Or course, in the intervening years, the picture has changed and we have a number of teachers who have been very happy to have been covered under unemployment insurance. In any event, the disability benefit was added as something that would be available to those who did not expect to be unemployed for the traditional reasons.

Constitutionally, the insurance type benefits to welfare programs are the prerogative of the provinces which have agreed to rent out their territories to the federal government and the federal government, in turn, has introduced the pension and unemployment insurance plans.

Other public plans vary by province and we have the same plethora of benefits as the United States. Under the auto insurance plans in various provinces, there are disability benefits related only to disability arising from auto accidents. At least three provinces have government run auto insurance. The disability benefits started out as nominal benefits of \$35 to \$40 per week but these, while still not large, have climbed. In Saskatchewan, there is pending legislation to increase it to \$120 per week.

We have Worker's Compensation legislation in each of the provinces covering job related accidents. Traditionally, these benefits have been what is referred to as of the "meat chart" variety. By meat chart, we mean that for a given accident there is a table of benefits indicating how much the benefit should be, such as 20% of earnings. It is a table benefit related to the portion of the body and the extent of the injury and is generally not related to the actual impact on earnings. There is a trend to change this to a more reasonable type of loss of income benefit. Saskatchewan is a good example. About 18 months ago they revised their benefit to essentially 75% of earnings, on a tax free basis, covering earnings up to about $24,000 per year. This is fully indexed to the cost of living and works on a loss of earning concept. The administrator would look at earnings prior to disability and the individual's capacity to determine what he is capable of earning. The benefit is then based on the loss of earnings, based on the loss of earnings capacity. This is fully indexed so that the total earnings capacity grows based on pre-claim earnings. There is a study in Ontario recommending coverage up to $40,000 of earnings to also include substantial death and survivor benefits.

In general, these are the major government plans. There are veterans benefits, but our armed forces are much smaller in relation to our economy and they tend to be career armed forces.

Group insurance benefits for disability have been growing. When the Unemployment Insurance Plan was introduced in the early 1970's, an opt out feature was included so that the group insurance plan could provide benefits that are at least as good, and then the employer gets a premium reduction under the Unemployment Insurance Plan. Group plans were able to retain a substantial amount of coverage but the introduction of the government benefits focused attention on the disability area and led to more interest and enrichment of group disability benefits. Growth has been substantial in terms of the number of people covered and the adequacy of benefits.

Individual benefits are not a major factor. There are quite a number of insurers that market individual coverage, but relatively few who make it a key part of their marketing effort. This is related to the fact that there is really no market for health care benefits in Canada. Therefore, individual loss-of-time coverage tends to be an adjunct to life insurance.

The major public issues are threefold. First is coverage. What about the thousands of Canadian workers without coverage? Second, is the issue of adequacy. What about those who do have some coverage but have grossly inadequate coverage? The third is the impact of inflation. What about those who may have adequate coverage in today's terms? If disabled on a long-term basis at 12.4% inflation those benefits do not remain adequate very long.

This is the International Year of Disabled Persons, and the Canadian Government has been promoting this. They appointed a special committee of the House of Commons which held hearings across Canada to identify problems and make recommendations. They indicated the need for a comprehensive plan for coverage is not sufficiently broad or adequate and did not deal with inflation.

They did not say how the plan would be set up, but stressed the comprehensive nature of it. Industry suspects that in the eyes of the government it will be a government program, especially when looking at Canada's traditional approach. The report was released about six weeks ago and further hearings will be held in the months ahead. The industry is putting together its submission on it now.

In the meantime, we have a very active province in this area. Saskatchewan is a western province which for years has had a farm economy. In recent years they have discovered resources that have had a tremendous impact on its economy. The government has been formed by the New Democratic Party, our third major political party. This party is socialist, is very concerned for the social welfare of its citizens, and is very interested in disability and medical care protection. It was the birthplace of nationalized hospital and medical plans. So we look closely at Saskatchewan.

For the last few years, they have been talking about government disability benefits and our understanding is that soon, perhaps within a couple of weeks, there will be a paper issued by the government discussing this area and, we believe, recommending a provincial run program of disability benefits. Our expectation is that this program would be largely an extension of their workers' compensation plan. So, it would be a generous plan with a long term residual benefit and a partial disability feature through the loss of earnings concept I mentioned earlier. Through the past few years, the industry has tried to stay close to the government. The Canadian Association of Accident and Sickness Insurers employed an actuarial consulting firm to review one of the proposals of five years ago and attach realistic cost figures to it. We wanted to bring to the attention of the government and the public what those benefits would cost. The figures the review came up with were about three times what the government had been using. This sort of actuarial input had a real impact on the government and convinced them that they should discuss this further.

We have tried to talk with the government, find out what the costs would be and point out impacts that the plan would have on other government goals. For instance, if the government provided a plan of very generous Long-Term Disability benefits, it may not be possible for insurers to market dental insurance because if there is no hospital, medical or disability premium, the coverage is just too thin to offer small employers. Supplemental coverages would also be difficult to market and many individuals currently with coverage, would end up with less coverage. Our role has been to point out the facts and, secondly, to try to emphasize that, if the government is serious in its support for this coverage, private insurance is flexible enough to administer a similar plan.

I would mention quickly a couple of other issues. In Canada, we are still grappling with the maternity issue. Should maternity be treated as a disability or an unpaid leave of absence? We have variations by province since human rights issues are largely under provincial jurisdiction. In general, we do not cover absence due to normal maternity as a disability; we do cover complications. The general areas of human rights, equal employment opportunity, equal opportunity for benefits and nondiscrimination continue as hot issues.

Another issue has been called disclosure. This relates to group benefits, disability in particular. Essentially it is recommended that if an employee is not told about a major change in his benefits, such as termination, change of carrier or benefit formula, the insurers would be liable for up to six years to provide benefits to that employee. The industry has resisted this strongly, saying we are prepared to provide the employer with material in terms of a release in bulletins and letters, but we have no way of identifying employees who are insured and communicating to them what has happened.

Another area is rehabilitation. In conjunction with 1981 being the International Year of Disabled Persons, there has been great emphasis on rehabilitation as a positive aspect of our loss-of-time business. It is positive in that it is very rewarding when it works and, secondly, it provides major communication possibilities for the industry.

In summing up, the actuary has a very positive and major role to play. It is difficult to separate his role from the industry's role or the consultant's role. We have a role as a professional but, also, through our employers we share that role in pointing out what the facts are, insuring people understand them and communicating our knowledge of the process to regulators, members of government and other decision makers.

MR. CARL L. LOEFFEL: In addition to the items discussed, there are a number of other factors operating on loss-of-time coverage. These are more general and impact Canadians as well as Americans. To discuss these aspects, let me introduce Jack Caton.

MR. JOHN C. CATON: My experience with loss-of-time or disability coverages is all in the individual insurance area so when I refer to disability insurance, that is what I mean.

There are many outside forces, most of them beyond our control, which have an impact on the disability business today. I would like to discuss what I feel are the 4 major outside forces at work now. They are:

1. Declining Work Ethic
2. Increased Technology
3. Inflation
4. Government

First of all, there has been a declining work ethic for several decades. More government involvement in our lives is part of the problem with its proliferation of subsidies and welfare programs. People become dependent on these programs. There is a growing sense of entitlement to these programs. There is less loyalty to many of our oldest traditions. Less loyalty to country, less loyalty to family and less loyalty to the job. Less incentive to work obviously has a direct affect on our loss ratios. Our industry has reacted to this trend with tighter underwriting rules and limits, more precise definition of occupations, longer elimination periods and an unfortunate abandonment of the lower occupation market.

The second major outside force is increased technology. The first thing that comes to mind here is computers. They decrease the cost of handling business. They help us sell the business with sales illustrations. They help us communicate through agency terminals. They help us as actuaries study our experience. They allow us to consider complex product designs.

Medical technology has been a blessing for the life insurance business, but it may be a devil in disguise for the disability business. It certainly can create a squeeze for us in the annuity business as more and more retired people die later. We can be comforted by the fact that medical research has found cures for virtually all infectious diseases thereby reducing or eliminating many disabilities. But, medical research is also finding ways to keep people with chronic diseases alive longer. This could have a devastating affect on the length of disabilities.

Inflation is the next outside force and it is particularly evident right now. It is costing us more and more to do business today. The savings from technology can only go so far. Higher interest earnings are not as beneficial to our business as it is to life insurance and annuities. We will be doing more belt tightening.

Inflation is a reflection of our economy which is very cyclical. A cyclical economy means both boom and bust periods. We are learning that unemployment can be associated with most any part of the economic cycle and not just a recession. We all know what unemployment can do to our business. Anyone with a little common sense can see that a guaranteed premium on a product dependent on such a cyclical outside force is ludicrous. Non-cancellable insurance does not fit. The only trouble is that it sells. At least it is encouraging to see a ground swell of interest in limiting our non-can business to the best occupations.

Inflation has had a favorable effect on us. It can bail us out of overinsurance situations after issue or during a claim. It can provide increasing incentives to return to work. However, inflation leads to the bug-a-boo called indexing and our industry is jumping on the bandwagon with both feet, and probably without enough thought. Every week someone else comes out with an inflation rider or some other scheme to keep benefits current.

Don't get me wrong. I am in favor of cost-of-living benefits, but I am afraid that we are over-reacting. I'm afraid that we may fall back into the trap of the early 1970's when we were trying to upstage each other with more and more liberal provisions in our policies. Consider this; if we index disability benefits for the CPI and also index pre-disability earnings for the CPI, where are our margins? Indexing beyond age 55 or 60 is also a big risk -- an age range where many disabilities occur.

The final major outside force influencing us today is the government at all levels of our society. Obviously, we are being hurt like all other industries with excessive regulation through an alphabet soup of federal agencies. Then we have to deal with an increasing array of state laws and regulations. This has had more influence on medical insurance than on disability insurance.

There are many different public disability programs including veterans benefits, black lung benefits, federal employees, longshoremen, railroadmen, workers' compensation, state cash sickness plans, and so on. But the predominant public program that we are concerned with is social security. I am particularly concerned because of my involvement on the Federal Affairs Subcommittee of HIAA's Disability Insurance Committee headed by Ben Jones, President of Monarch Life. He is doing a fantastic yeoman's job for the entire disability insurance industry. He and his subcommittees have accomplished a lot in a short time. The Research Subcommittee has published a booklet of all the Compensation Systems Available to Disabled Persons in the United States. It is an overview of the 40-50 various plans and their costs and interrelationships. It is somewhat mind-boggling that it is possible for an individual in the right circumstances to qualify for as many as 30 sources of disability benefits.

A disability income record (DIR) system is up and running which should be of great help to us. It is administered by the medical information bureau (MIB) and allows participating or associate companies to search the central MIB files at time of issue of a disability policy or at time of claim to determine what other coverage is in force.

Getting back to social security, there is a definite attitude on the part of the present administration and many members of Congress to put the system on a sound financial basis and, more importantly for us, provide the so-called floor-of-protection on a fair and equitable basis. As far as disability benefits are concerned, this means eliminating fraud, more consistent determinations, more case review and reasonable benefits.

We saw the first step last year with the 1980 Amendments which, among other things, limits the maximum family benefit to 150% of the primary insurance amount (PIA) or 85% of the average indexed monthly earnings (AIME) or less. My committee headed by Gerry Parker of The Guardian Life Insurance Company of America provided valuable input to the Social Security Administration (SSA) and the House Ways & Means Committee for this legislation.

My brief experience in this area has proven to me that our congressmen and even the bureaucrats will listen if we just take the time to communicate our problems and needs to them. You have more influence with your local politicians than you realize. You should get involved if we are going to expect our companies and our industry to be treated well by the government. Even if it is just a letter to your senator or congressman - it helps.

I think many of you would be surprised to learn what the bureaucrats are considering today for Social Security disability benefits. Let me give you a couple of examples:

The Office of Management and Budget has proposed 3 changes:

1. Reduce payments to ineligibles through tighter management of the system.

2. Stricter recovery of work test - this would require 6 out of last 13 quarters of coverage as well as 20 out of the last 40 quarters (or 1/2 since age 21).

3. A Mega-cap which would limit disability benefits so that they would not exceed previous after-tax earnings. I hope this idea is pursued because they are surely on the right track. But, they will probably exclude too many programs from the Mega-cap starting with private programs, veteran benefits and Worker's Compensation.

The President's Commission on Pension Policy is considering the "Viability of a Universal Disability Program for All People" which may include an overall cap on benefits from all sources. Ben Jones addressed this commission last November and said that one idea under consideration is to require insurers to provide a 1099 form during a claim which must be reported along with earnings for prior years. Then some sort of tax could be imposed when benefits from all sources exceed some cap when related to pre-disability earnings. This may sound far out, but it is an indication that favorable changes may be in store for the future.

You may be interested in the position that HIAA's Federal Affairs Subcommittee is working on right now. It is not in final form, but I'll share the concept with you.

Fundamentally, we feel that the basic structure of social security disability benefits should be divorced from the basic structure of the retirement benefits. They have tagged along ever since enacted in 1954. The most ridiculous extension of the retirement benefits and survivor benefits is in the area of dependents' benefits. Why should a disabled worker receive 50%

more benefits just because he has kids? Or better yet, why should a single disabled worker receive less because he has no kids? What we want to propose is a reasonable schedule of replacement ratios related to a worker's after-tax earned income using FICA covered earnings. The replacement ratios would provide an adequate income at the lower income levels, say below $12,000, but reduce sharply at the middle and upper incomes to maintain the floor of protection principle inherent in the Social Security system. We are considering replacement ratios graded from 90% of net earnings at the minimum wage level which is about $7000 down to 45% of net earnings at the maximum average wage level. Of course, people earning in excess of the maximum would have actual replacement ratios far lower than 45%. The pre-disability earnings should be based on more recent earnings. The AIME takes into account earnings over a long period. We are suggesting that they use the best 2 of the last 5 years of indexed earnings used in the AIME calculation.

I can assure you that all parties involved - the SSA, the Reagan administration, the House Ways and Means Committee and the Senate Finance Committee are interested in Social Security. Maybe disability will not be included in any amendments this year, but we do have hopes for next year.

In the few minutes remaining I would like to give you a thumbnail sketch of my view of the individual disability business and new disability products in this decade. In a word I am optimistic. It appears that we have retrenched quite well since the poor experience of the middle 1970's. If we do not fall back into the trap of one-upmanship, the 1980's should be a profitable decade for us. We are doing a lot of things better today than we did a few years ago. There is more sensible product price and design. Underwriting rules and limits are sounder. We should do a better job of monitoring our experience because the tools are there. We should improve our methods. A series of loss ratios is not an accurate record of the true experience of a policy. It is much better to study the actual to expected claims experience by duration, plan, age, etc. Also, actual to expected termination rates should be studied.

We are much more cognizant of overinsurance. Financial underwriting is tighter. The majority of companies offer some form of coverage that integrates with social insurance plans. But, there is one area of overinsurance that most of us overlook and that is the situation with 2-income families. The problem simply is that when one of the spouses becomes disabled, the loss of after tax dollars is less than if the claimant were the only wage-earner. This is because, as many of you are painfully aware, the Congress, in its infinite wisdom, has allowed the 2-income family to be thrown into much higher tax brackets than seems equitable.

My company has been recognizing this problem in its issue limits for over 2 years now by making a deduction from the issue limits based upon a percentage of the combined incomes. As an example, if you had a family making

$60,000, with half contributed by each party, American United Life's (AUL) regular issue limit would allow a benefit of $1500 for either worker. When this is combined with the after tax earnings of the non-disabled spouse, the family has the $1500 of tax free income plus the earnings on a $30,000 income from the the healthy spouse. This produces more income than when they are both healthy. We have, therefore, devised a deduction shown in the chart, which brings the replacement down to just under 90%.

There is now and there will be a movement toward pure loss of income approach or no-occ policy. American United Life has been marketing such a policy for 8 years with favorable results. We call it the Income Replacement policy. The insuring clause says simply that, if you are sick or hurt and your income falls below 80% of your average earnings, we will pay you a portion of the benefit you purchased equal to the portion of income you lost. It makes sense. You don't use an occupation to buy groceries. You use the income from that occupation. Or to put it another way; the purpose of insurance is to insure the economic loss from an event, not the event itself.

There are several advantages to the income replacement policy.

1. Provides the benefits really needed which is replacement of lost income.

2. Provides a partial benefit without a requirement of a period of total disability.

3. Our policy recognizes income as it is received, not as it is earned. Therefore, we calculate our benefits at the time an actual loss occurs. For a policyholder who is not on salary, this can provide a tremendous incentive to return to work because benefits are not reduced or terminated until income begins flowing. For a professional, it may take several months to build up his accounts, even after returning to work on a full-time basis and we would continue to pay benefits. The income replacement policy encourages return to work at one's own job which is the desire in almost all cases.

4. Income replacement avoids overinsurance by recognizing all sources of income for personal services. Also the policy can integrate with Social Security, Worker's Compensation and state cash sickness benefits on a dollar-for-dollar offset basis.

5. Pure income loss insurance is easy to sell, particularly to professionals. It is often used as a door opener. Our agents find it easier to get interviews.

6. So far income replacement has been profitable. Since its introduction in 1973, the incurred loss ratio has been 48%. In contrast, the regular disability insurance we sold during the same period experienced a loss ratio of 85%.

There are some disadvantages to income replacement.

1. It is more difficult to train agents because you have to unlearn disability concepts.

2. There is another step to claims administration due to proof of income - but this is a feature of residual disability as well.

3. There is a danger of early partial retirement which is an unknown risk with this product.

4. Policy language is untested and pricing is somewhat less precise until we can gain some experience.

All things considered, we are very pleased with the income replacement product.

The 1980's should be good for us. Whatever products we are selling, we should sell a lot more premium. There are many untapped sources that we can get to, particularly in the small business market. I hope we get away from competing so hard for the 400,000 or so physicians and look for others. If we don't fill the gap, I'm afraid the government will step in. I encourage you all to be creative, because there is a lot of business out there.

MR. LOEFFEL: Are there problems integrating private disability benefits with government benefits in Canada?

MR. BLACK: In the group area, a company could use an offset approach or, if the private benefit were small, ignore the Canadian Pension Plan or the Quebec Pension Plan benefits, because those benefits are quite modest, only $300 or $400 per month. However, the Worker's Compensation benefits are generous and usually the private plan would be written on a non-occupational basis, or will carve out the Worker's Compensation benefit. We had thought integration or offsets were flexible and straightforward but just in recent months some doubt has been cast on this. Class action suits are virtually unheard of in Canada, but we are facing one in Quebec. A group has launched a suit against forty or so insurers on behalf of disability claimants who have had offsets applied against the Quebec Pension Plan. At the moment the companies are saying this is not a valid class: each company's contract is different, within a company each contract issued to each employer is different, and this is not an homogeneous class. Until this is determined, we are not sure where we are headed.

On individual insurance there is some archaic wording in the provisions required in Canada. One is the relation of earnings to insurance, which in effect, protects insurers from benefits exceeding 100% of pay, but this does not take taxation into account. We have run into great difficulty in persuading regulators to recommend to their governments amendment of the law. There is a strong feeling that in offsets, insurance companies are the bad boys.

The government is trying to provide benefits and then the insurance company takes it away, which becomes particularly sticky when, as so often happens, the government is late in making its determination. Since the company has already paid benefits, it is then in a recoup situation.

MR. LOEFFEL: In line with that question, could the insurer in effect underwrite against the government by obtaining the favorable risks, or is there a mechanism preventing them from doing such?

MR. BLACK: Under the unemployment insurance plan where we can compete, that could happen. The government does not appear to be too concerned about this. We had some discussion early in the game, they were aware of this, and they did not feel this a big enough problem to worry about. Remember the disability benefit, in their terms, is just one small part of the unemployment insurance plan. In relation to their goal of providing adequate disability insurance, they are happy if the private plan is providing coverage because usually it is more adequate coverage.

MR. LOEFFEL: Jack, if you differentiate in your underwriting between people who are married and people who are not married as to how much you will write, have you run into any discrimination problems?

MR. CATON: I cannot say that we had problems. That question did come up. We talked with our legal department and our underwriters. We have a strong opinion, particularly from our legal department, that we would not have trouble with it. Its only one of many factors in the underwriting process. We have income limits by income and occupation class, and we have unearned income rules. There are a great number of things that determine what we will sell people and marital status happens to be one of them. That does not mean we will not be sued, but we are going ahead and, hopefully, nothing will come of it.

Also, in that area, the biggest fear we had in putting in a 2-income family limit was that our agents would give us resistance on it. We put together some charts that illustrated the problem and distributed them at the same time we introduced the product. I have been amazed at what little resistance we have had.

MR. BLACK: I have two questions on your loss-of-income policy. First, are you alone in offering this and is anyone offering this in group? Second, how do you protect against people who take early partial retirement?

MR. CATON: There are about a half a dozen companies selling a no-occ policy now. There is a groundswell of interest in this concept and I know of some companies working on it. We may see some hybrids with the residual approach with no your occupation definition but, perhaps, maintaining some disability wording. It is a good trend.

In answer to your second question, early retirement is the largest risk we are taking with this policy. It is hard to determine what this risk might be, but we are hoping the positive aspects of the policy will offset the long term partial retirements we might get. We will get some such claims but yet some might otherwise totally retire rather than partially retire.

MR. BARRY SCHILMEISTER: As far as the professional marketplace, do you feel the declining work ethic applies to physicians, lawyers and other professionals? Also, in regard to lower income people who are difficult to cover due to other social benefits, can we price a product that people will be willing to buy with their marginal dollars?

MR. CATON: I do not see a decline in the work ethic in people in the upper occupational class.

I think the way to reach the lower classes is to approach them on a mass marketing - salary deduction approach, with simpler and more conservative underwriting. You cannot pay an agent adequately to call on people for $100 of premium, but those people need some extra coverage. I think they would buy it. They buy reasonable amounts of life insurance on a salary deduction basis, if presented properly, and with our schemes of integration we have an opportunity that we are not taking advantage of.

MR. BLACK: Jack, you mentioned a universal disability plan that came out of the president's commission on pension policy. Would this cover everybody? Would it be a comprehensive plan? Would private insurance fit into it?

MR. CATON: It was an outgrowth of their pension hearings, considering a universal pension program. The report I received indicated it was to monitor disability benefits from all sources, not necessarily providing it by government but controlling the total benefit perhaps by the tax system.

REPLACEMENT RATIOS FOR WORKING COUPLES

APPLICANT PRESUMED TO EARN 50% OF COUPLE'S EARNINGS

(1) Gross Annual Income of Applicant	(2) Gross Ann. Income of Couple	(3) Net Inc. with both working	(4) Spouse's Net Inc. Applicant Disabled	(5) AUL Issue Limit	(6) Total Inc. AUL & Spouse	(7) Replacement Ratio	(8) AUL Limit After Deduction	(9) Total Inc. AUL & Spouse	(10) Replacement Ratio
$12,000	$24,000	$1,569	$ 858	$ 700	$1,558	99.3%	$ 600	$1,458	92.9%
18,000	36,000	2,188	1,210	950	2,160	98.7	750	1,910	87.3
24,000	48,000	2,806	1,569	1,200	2,769	98.7	900	2,469	88.0
30,000	60,000	3,396	1,928	1,500	3,428	100.9	1,100	3,028	89.2
36,000	72,000	3,955	2,279	1,800	4,079	103.1	1,300	3,579	90.5
48,000	96,000	5,060	2,929	2,200	5,129	101.4	1,500	4,429	87.5
60,000	120,000	6,162	3,528	2,600	6,128	99.4	1,800	5,328	86.5
90,000	180,000	8,918	4,916	3,600	8,516	95.5	2,800	7,716	86.5
120,000	240,000	11,673	6,294	4,600	10,894	93.3	3,800	10,094	86.5
150,000	300,000	14,429	7,672	5,000	12,672	87.8	4,200	11,872	82.3

-Insured is married and has 2 dependent children.
-1979 Federal Income Tax Tables using
  Table B up thru $18,000 income
  Schedule Y over $18,000 assuming 20% itemized deductions
-State Tax - used Virginia as estimated average for U.S.
-FICA Tax 6.13% of first $25,900 of earnings ($1,588 max.)
-Deduction for 2-income families is 10% of combined husband's and wife's monthly income less $100. This deduction cannot exceed $800. If applicant earned income exceeds 80% of combined income, use half this deduction.