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Session 64 TS
Worksite Health Products

Track: Health

Moderator: Dominique Lebel

Panelists: Dominique Lebel

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Thomas O. Morey

Summary: While many carriers struggle to compete and survive in the traditional group medical marketplace, some carriers have found markets for ancillary and supplemental health products marketed through the worksite.

Panelists discuss:
• Characteristics of the worksite market and comparisons/contrasts to those of other markets.
• Current worksite carriers and their distribution systems, sales approaches, underwriting/risk-selection processes,
pricing, etc.
• Actuarial issues and considerations associated with health products sold in this market.
Attendees learn about the profitable growth opportunities and the current status of the worksite marketplace.

MR. DOMINIQUE LEBEL: Welcome to Session 64, a teaching session on Worksite Health Products. This session has been designed for attendees with no experience with worksite. We're lucky to have a distinguished panel today. John Kidder is a principal at Wakely Actuarial, where he serves as vice president and consulting actuary and manages the firm's supplemental health consulting practice. He has

Note: The chart(s) referred to in the text can be downloaded at:
http://handouts.soa.org/conted/cearchive/neworleans-june05/064_bk.pdf.

worked as a consultant since 1997, after working for several years for a large insurance company, specializing in the worksite market. He is a Fellow of the SOA and a member of the Academy. John will discuss current worksite carriers, product distribution, sales approaches and underwriting. And second from the left here is Tom Morey, and he’s going to follow John. Tom is second vice president of United States pricing and rerating at Aflac where he is responsible for product development and pricing. He joined Aflac in 1995. Tom is a Fellow of the SOA and a member of the Academy. He will be discussing actuarial issues related to work-type products. My name is Dominique Lebel, and I’m a consulting actuary with the Tillinghast business at Towers-Perrin, where I specialize in pricing product development, modeling and embedded value reporting. We encourage you to ask questions as we go along, although we expect that we will have time for questions at the end.

So what is worksite? Well, it’s sold at the workplace, hence the name worksite. It’s voluntary. It’s not compulsory. It’s paid by employees, usually on a payroll-deduction basis, and a wide range of products are offered. Now, some people make a distinction between voluntary and worksite. They say that it’s a voluntary market that consists of products sold on a group platform, and worksite products are more individual-type products. I’m not going to make a distinction from my presentation. I think the bottom line to me is that they’re both products sold at the worksite and that the distinctions between individual and group platforms are diminishing.

So how is a case sold? Employees meet one-on-one with the broker/agent during the workday. Here they get a limited time to sell. It’s usually 20-30 minutes with an employee, and the key here is to design simple products because there isn’t much time to sell to an employee. A less effective method, sometimes used in combination with the one-on-one approach, is a group presentation. And then employees are signed up at the end or given enrollment materials. Even less effective is selection of benefits from a menu, and employees enrolled via Internet or they called an 800 number. Lastly, printed marketing materials are handed out with the company endorsement typically, and then they’re invited to attend an information session or they sign up by phone, etc. Like I said, some combination of the method is typically used and most effective is the one-on-one with the broker/agent during the day.

Now, who sells these products in general? John’s going to go into that more, but agents and enrollment specialists dominate the market. Employee benefit brokers now are starting to play a bigger role in this marketplace.

How does the billing work? It’s somewhat of a carryover from group in this case, even though a lot of the products are individual-type products. Typically, premiums are deducted by the employer from employees’ paychecks, based on a list maintained by the insuring employer, but then the employer sends one premium to the insurance company.

Now, this causes some complications for some individual writers. Some employers are slow in sending the premiums to the insurance company. Life insurers or insurers that specialize in the individual products sometimes have systems in place. If a premium is not paid within a grace period, then that automatically triggers a lapse or a non-forfeiture option, so systems have to be modified to take that into account.

What happens when employees change jobs or an employer chooses to endorse another carrier? The insurance company and the rep will typically try to change the billing from payroll deductions to some sort of direct bill. This is so the loss, changing jobs or the loss of employer endorsement doesn’t automatically trigger a loss of in force policy, which is a little bit different than group coverage.

Here I tried to show how worksite combines elements of both traditional group and traditional insurance. Now, the lines between group and individual coverage are diminishing, so this isn’t hard and fast anymore, but I think it illustrates a characteristic of worksite. And I’m not going to go into these in detail. The administrative expense with worksite should be less than for individual policies because of the mass scaling and economies of scale. But there are significant startup expenses to set up payroll deductions and such.

Commissions are on individual-style products that are typically similar to individual products, but lapse experience is much worse than individual products. So it takes a longer time to recoup that up-front expense than for individual-type products.

Underwriting combines features of individual and group. There’s some medical underwriting, although more and more often these days there’s some pressure to speed up the sales process. So guaranteed issue limits are being shrunk and simplified.
Individual products sold in the worksite typically have guaranteed premium structures. And the portable coverage aspect of worksite makes it so that individual insurance is better suited for worksite than group coverage. Although I’m going to show later that group coverage is getting a bigger share of the worksite marketplace.

Now, why is it that employers want to offer worksite products? Well, there’s a combination of reasons. Employees are interested in the products because employers cannot afford to offer the products because of inflation. They want to make sure that they’ve got quality employees. So this helps them recruit employees and keep existing employees. And I think the 20 percent for our broker-recommended voluntary is probably realistically higher, but that’s what the survey results showed.

Now, worksite has grown significantly since 1997. At about a 14 percent average compound growth rate. Why did that happen? Well, I think it’s a combination of a few things, such as a combination of rise in medical costs. Some employers can’t

provide the benefits that they want to if they want to keep the same margins for their businesses. So they have to transfer cost to employees. I think the couple of other reasons are they want to attract and retain quality employees, so they’re forced, if they want to compete for these employees, to offer benefits that are competitive. I think we also have more of a consumer-driven market these days. So the emphasis is on the consumer to make his own choices. And there’s been some commission compression that’s been occurring over the years, and worksites, given the high commissions that are being paid, make it more attractive to producers.

So the group platform has been increasing relative to the individual platform, even though the individual platform still represents the majority of cases sold. And I think that’s happened for a couple of reasons. I think there have been more group players entering the worksite marketplace, who then use a group platform for their products. I also think that some individual players have been switching to a group platform for a couple of reasons. The ease of the filing process makes pricing on a group basis simpler, in some people’s opinion, than pricing on an individual basis.

The other thing that’s been happening is as group carriers are getting more serious about worksite, their employee benefit producers and brokers are also increasing their sales in this marketplace.

Here I tried to compare the growth rate of the worksite marketplace to the growth rate in the total group and life marketplace. I have to caveat this. What I did for total group life and health was just take the AM Best in-force numbers, so All-inclusion does include other medical-type companies that may offer some group product. But I think the point is that the worksite growth has been favorable compared to the growth in in-force premium of the overall group marketplace.

So now I’d like to pass it over to John, who is going to discuss distribution sales, products, underwriting and other things.

MR. JOHN KIDDER: I’m going to be giving a high-level overview of the major competitors in the worksite market, their primary distribution methods, the products that are marketed in the worksite and how they’re issued. We’re also going to look at some major market segments and some key factors for success in the worksite market.

The worksite, as Dominique said, is a quickly growing market. One of the reasons that it’s growing so quickly is because insurers are trying to be more flexible. They’re trying to be innovative and meet the needs of employers and brokers out there in the market. And so the market is becoming a little bit more competitive. And it’s changing. I want to illustrate, I guess, just by virtue of the data that we’ve been provided so graciously by Eastbridge Marketing Consultants; they have given us a lot of the information. They do surveys in the worksite market, and their definition of the worksite is 100 percent employee-paid health, disability – life, health and disability products sold on either a group or individual basis with

premiums paid through payroll deduction.

That seems a little narrow in light of what some companies are doing. I see a lot of movement toward plans where employers are contributing some or all of the premiums. There are also alternative billing modes. Companies are taking advantage of technology. People want to pay via bank draft or credit cards or maybe direct bill.

If I think it’s important to recognize that as we look through these, keep in mind that the data only includes a very small piece of the market or maybe not so small, but payroll deduction is what I would call it. The worksite market is what I would call a larger overall market and it includes these alternative billing methods and contributions.

In 2003 there were about 120 carriers in the market. Unfortunately, the market is dominated by some large companies. The top five companies account for about half of the new sales. About 75 percent of the new sales are accounted for within the top 15 carriers. I’m sure everybody’s heard of the AFLAC duck. It’s become a very recognizable name and, as you can see, it is the largest carrier in this market. Followed not so closely by UniProvident and Colonial, which is a subsidiary of UniProvident. Then there are Allstate and American Heritage, and then another company that withheld its name from the study.

So how are companies issuing these products? What channels are they using to sell? Dominique touched on this a little bit, but I’ll go into a little more detail here. Career agents, they work primarily for a single company. They sell one company’s product. They’re usually compensated with commissions, although some companies compensate their agents through salary structure.

Worksite brokers focus on worksite sales. Some of the larger brokers offer support services to the employers as a way to gain access to the group. They may offer billing or even policy administration services. Employee benefits brokers market employee benefits such as group major medical and life insurance through employers. They sell worksite products, mostly on a voluntary basis, as a way to supplement the employer’s basic benefits package. And then there are other types of producers or agents and brokers who only occasionally sell in the worksite market or multi-line agents.

This shows a breakdown of the distribution by segment. The sales are dominated by brokers. They account for more than 60 percent of new sales. This number is a little understated if you think about employee benefits brokers who are selling benefits. Employers are contributing part of the premiums. This is becoming more and more common, especially with transferring costs to employees. As that happens, brokers are going to continue to be a larger and larger piece.

The products that companies sell basically break down into three categories. Life

insurance includes whole life, term, UL, supplemental A&H products, such as short-term disability. Most of them are designed to fill in the gaps and cover short-term disability. It fits in the gap between sick leave and long-term disability, accident, hospital indemnity and specified disease. They’re designed to cover expenses that major medical policies don’t cover. They allow insureds to possibly go out of network and seek better treatment or better care, or to pay expenses that aren’t really medical expenses. They’re being reimbursed based on medical expenses that you’re being billed. But what people realize is that there are costs, other costs to being fixed, such as you need caretakers and baby-sitters or even lost income.

Another one that is growing is benefits that might also be provided by the employers, such as long-term disability. I know many medical plans in which the costs of those are being transferred to the employees.

The rule in the worksite market is conflicting. It’s important to be simple, due to the limited amount of time that an agent has to make a sale in the worksite market. And you’ve got maybe five minutes if you’re in a one-arm, one-presentation and you really don’t have a lot of time to get into detailed benefit explanations or going into, “OK, the policy excludes this and this and this.” So it’s really important to keep your product simple.

Another way to introduce simplicity is to use issue age bans; make the rate schedules easier to carry into a company. It’s easier to identify what premiums are going to be associated with whatever employee the agent is talking to. Some companies, as a matter of fact, don’t use any age bans. That, of course, makes employees feel good. It’s equity among the employees, makes a really simple rate schedule, but it also introduces a lot of risk by age. Especially for sickness products, where the claim cost curves can be steep.

Simplified underwritings and other issues; this is another way that companies are simplifying the sales process in the worksite. I’ll talk about that a little bit more in a minute. And then finally, it’s important to have clearly defined limited benefits in your policies. You want to keep the benefits simple. You want to clearly define them. That way the agent doesn’t need to spend a lot of time explaining the details of the benefits.

Back to underwriting and risk selection and mix of individual and group concepts. In the worksite there’s a basic supposition that if you engage in activity at work, you have to have some level of health. So there’s already some level of health assumed, so companies will reduce the number of questions that you would usually ask on a one-on-one, individual sale. Another way that companies are underwriting this is by looking at overall group characteristics such as industry, claim costs and lapse rates, which vary quite a bit by industry. Simplified underwriting is usually used. Usually the apps have yes or no questions, and oftentimes it’s just accept or reject. The agents want to know, all right, am I wasting my time with this person or is the policy going to be issued?

Also, a guarantee issue with minimum participation requirements is becoming more and more popular. That way, that speeds up the sale. It’s important, however, to make sure that you do set industry or minimum participation.

This next chart shows a mix of products currently sold in the worksite. Life accounts for about 25 percent of the new sales, followed by disability, which, I believe, includes short-term and long-term disability. Again, keep in mind that this chart really doesn’t encompass the entire worksite market. This is really the source of Eastbridge, so this accounts for mostly payroll deduction. I think that in actuality, if you included products that employers contribute to some of the premiums, you would probably see a larger percentage in the hospital indemnity or supplemental medical segment, and probably also disability.

So how are companies marketing certain platforms? The worksite market has blurred the lines between individual and group platforms. You’ve got an individual product that has typically been sold in the group environment. So you know you’re going to have a combination of individual and group concepts when you underwrite. As of 2003, group accounted for almost half of the new worksite sales. I think it probably accounts for a little bit more than that if you include, again, the employer contributions. I don’t have any more recent statistics, but judging by the proportion of products or clients, I’d wager to that group’s sales and stochastic individual in the worksite market.

Individual and guaranteed renewable products have been the industry standards. The appeal of these products is that you can take them with you when you leave the group. However, the products aren’t always regulated uniformly among all the states, so you’re going to have situations where one state has a mandated benefit in a certain type of product and you can’t sell the same benefits for a nationwide employer to all the employees. So, groups solved that problem because it’s less regulated. It’s less regulated in most states. A company will fill a product in all the states, but wherever the employer is domiciled, that’s what the benefit package is usually going to be.

Voluntary group products are gaining popularity. They’re sold just like individual products, except that they’re on group chassises. They’re easier to file. Most states don’t even require a filing of the rates, an actuarial justification. However, in the states that do, they’re much less stringent about the review.

There are some difficulties in filing group products. There are high-loss-ratio requirements in a lot of states where they mandate benefits. The loss ratio requirements are higher. At least one state, the state of Florida, has pooling requirements where groups of less than 51 certificates need to be pooled together and you have to do annual rate filings. And those filings have to be reviewed. However, you, in the larger groups, you can experience rate those groups.

Also, there are small group rating laws that you need to be concerned about with

group products. You need to make sure that the products you’re issuing comply with small group or at least a voice small group rating loss. Takeovers, existing and prior claimants, what do you do on a group chassis here? You’re selling to an employer. On an individual product, you can’t just go into an employer and waive waiting periods and deductibles or pre-existing condition limitations. And with group products you tend to be able to be a little bit more flexible.

So far we’ve talked about sales distributions and products. How all the products are issued and how the products are designed. We haven’t discussed what companies and we haven’t discussed whom companies are selling to. A company has to consider its target market when it’s developing a product. Are you going to sell to private employers, schools and government groups, unions or associations? These types of groups have different characteristics that you have to consider. Private employers, this really covers a large variety of employers: large employers, small employers, white collar, blue collar and no collar.

Without stealing too much of Tom’s thunder, because he is going to be discussing pricing issues, suffice it to say that there is a large variation of claim costs and mortality and persistency between different industries. Insurers usually recognize this in the form of commissions and/or rates, or both. Smaller groups tend to just get shelf plans that are developed to be sold to the masses. However, the larger the group, the more willing an insurer tends to become or becomes willing to customize those products and plans to that group.

School and government groups tend to fall in the larger categories, so plans are often customized, at least if not for a specific group, then for that specific industry or market. The market tends to be very competitive. It’s hard to make the product work in this market. You’ve got to recognize that morbidity tends to be higher and lapses tend to be lower. In a sickness-type product, that can result in higher rates. So you have to be competitive with your rates. These are more savvy buyers than in some of the blue-collar markets. Lower lapse rates will increase the lifetime loss ratio on issue age-rated sickness coverage somewhat. But that’s somewhat offset by the fact that issue expenses are more easily recouped and higher first-year commissions are easily recouped with the better lapse rates.

Unions. They’re often very large groups and at least some aspects of the plan are customized for union groups, whether it’s issue guidelines, benefits or premium levels. Union products are often sold as part of a package of benefits funded by the members. The members’ dues fund them. That pretty much means you have the entire group, so participation is not really an issue. However, employees – even with 100 percent participation, the morbidity tends to be high.

Associations are another large group. The plans are usually tailored to meet the association’s issue requirements. But you want to make sure that you have an employer/employee relationship, especially in light of the fact that we’re talking about worksite here, which is an important issue with some products to make sure

that you have that employer/employee relationship, such as disability. Examples would be like an auto dealer association or association of health-care professionals. Make sure you account for the fact that these groups can have worse persistency and be careful to limit anti-selection in these types of groups.

So what are some other key factors in the worksite market? Some of these are going to be summaries and some of them we haven’t discussed yet. Simplicity, again, that’s the rule. You want to make the product simple, easy to sell. You want to make sure that it’s easy to understand by the policyholder. Product design is important. You want to recognize that you’re selling a product with limited underwriting to a potentially high-turnover market. Agents generally want first-year commissions to be high. These commissions make the sale worthwhile. It’s important to recognize how the persistency affects that. If you have too high commissions and you have that very bad persistency, you might have a low loss ratio and not make any money. Benefit design is important. Product design. Products should include appropriate waiting periods in pre-existing condition limitations in order to limit anti-selection.

Companies in the worksite market have learned the hard way the risks of offering high benefits or even unlimited benefits. I don’t know how many people here work for companies that have high unlimited radiation or chemotherapy benefits. Those products were issued in the 1980s and 1990s. When those products were developed, radiation or chemotherapy was very inexpensive. People, when they got cancer, died. And thanks to the drug companies, they managed to prolong life and people are now surviving cancer. And they’re doing it with very new and expensive drugs. And the drugs, not only are they more expensive, but people are taking them longer because they’re staying alive. So, the costs of radiation and chemotherapy have skyrocketed. So it’s important to be careful how you design your product.

Underwriting and issue guidelines, we’ve discussed that. Again, make sure that they’re simple. Look for industry and underwrite at the group level. Service the worksite market. Service is extremely important. It’s important to have a good relationship with your providers. The insureds, you want to make sure that you’re servicing their policies well and if you don’t, persistency can suffer. Employers: You’ve got not just the employees, you’ve got the employers to keep happy. They’re handling the billing. They’re offering the benefits to the employees.

And the producers might be the most important of all. Because they’re concerned about the first two: the employers and the employees. But they’re also concerned about themselves. They want your assistance in servicing the groups. They want to know what’s going on. They don’t want to be left in the dark. They want to know why decisions are being made or if you’re making changes, what’s going on. They’re looking for support. We have many clients who offer online access to their commission statements. They do everything they can. I’ve been put on hold doing rate filings and doing evaluation work for clients because their priority is their

producers. Some producer asked for something and that’s the attitude you have to have in this market to succeed.

It’s important to actively manage the blocks of business that you have. You want to make sure that it’s not satisfactory anymore to just look at loss ratios of a group and say, OK, or even a product, say OK, we’re doing fine. You’ve got to do your testing. You have to do projections to make sure your expenses are not excessive. You’ve got to make sure that your persistency is not poor. Otherwise, you might be losing money and not even know it.

And finally, pricing. Pricing is obviously important. Rates have to be competitive since companies can’t always implement the rate increases necessary to save profitability. If you miss, it’s very important to be accurate with your rating. I always worry when I develop a product and a company starts just selling it like crazy. I always end up going back and I look for what I missed. I think it’s maybe human nature, but Tom Morey is going to come up now and he’s going to tell you how to avoid missing the mark on pricing.

MR. THOMAS MOREY: So, at this point we’ve established the fact that worksite-marketed products are voluntary products, sold at employers. They can be through individual or group platforms. They can be across a wide variety of products. They can be any number of things.

In looking at the market itself, as John just went through, you see some of the particular issues in terms of product design and underwriting. I think he hit on some of the key things. Simplicity, ease of sale, it’s a relatively short period of time. What I’ve been asked to do now is to talk about some of the issues for actuaries working with this market. I’m going to approach it from a couple of different angles. One is from the angle of a company. I’m in pricing, so I’ll talk a little bit about that. The other one is from the standpoint of a regulator who has to look at these products. So as I go through, I’ll make a little bit of comment on each one.

This is the agenda I have. I’m going to talk about this checklist of things you have to go down when you’re doing pricing. There are some specific issues for this market that tie into the things that Dom and John have said so far about how these products are typically designed. We’ll address each one of these issues as it has to do with products that are designed for this market. I won’t read every name there, because you’ll see them again.

Starting out with demographic characteristics: Now as was mentioned earlier, very often for ease of sale premiums are age-banded. When premiums are age-banded, you are open to some risk from changes of age distribution from that which you originally assumed. Also, typically premiums are unisex. This may not always be true on life insurance, but very often is for simple premiums. You have a limited number of age-bands, a limited number of premiums. When you have that, you are

open to demographic risk, so it’s important to understand the demographics of the market you’re dealing in.

Now, looking at age, every one of us, of course, as actuaries, is familiar with the baby boom. We know what the baby boom is. We hear about it. We know what it’s doing to Social Security, planning issues, etc. But I don’t know to what degree we understand it, as we should. To say that there was a baby boom back in the 1940s and 1950s, and then there was a baby bust that followed, starting in the mid-1960s, what exactly does that mean? Well, it means something important for worksite-marketed products. Because there may be more people say at age 50 in the United States than there are age 20. Now, you wouldn’t think so, but it’s one of those things where when you actually get to thinking about it, and you’re trying to think of a distribution from year to year, how it changes, it’s important to try to project the future. Also, there are demographic trends in the workplace with gender and also with families themselves.

Now these are the baby boomers (see Morey slides 5–6, page 3). Now what this chart is, is on the left-hand side is the scale of the number of births. The number of births is the black line that’s on there. That was the actual number of births in the United States. The white line is the fertility rate, or the birth rate per thousand. Now you can see that during the baby boom, we had a locally maximized birth rate; and a completely maximized number of total births in the United States. Now what does this actually mean in terms of pricing?

Well, what it might mean is, if you’re looking at people born in 1947, there are more people born in 1947 than there were in all the previous years. So you have a much bigger segment of the population. Looks like the maximum, and I can’t remember, I think it’s around 1956, 1957, so you’re sitting here and looking at this thing, and you know that you’ve got people of a certain age, there are more of them then there are of any other age. Even with mortality rates, that thrust of the population is coming through; it is going to effect how you do age-banded premiums. You can set premium rates for one year, but typically with individual products, you sell a product over a period of years. What’s right in one year has to be right in all the others. You have to account for demographic trends.

Similarly, you have very few of these younger people, and once again, you get to a local minimum of fertility rates, but also the underlying population that supported it was less. So now you have considerably fewer people in these ages.

What this means in terms of worksite marketing is two things. No. 1, from a marketing standpoint, where are the people who you can appeal to? From an actuarial standpoint, your age distribution may not follow any sort of a classical pattern, as you vary it from one calendar year to the next. Individual guaranteed renewable products are typically in the worksite market; a tradeoff versus group guaranteed issue product. The usual balance or tradeoff is between guaranteed

issue and guaranteed renewability. It’s very difficult to have both.

In this case, when you’re talking about guaranteed issue, or talking about guaranteed renewable products from year to year, you have to account for the fact that the demographics of the underlying population are changing and are going to change in the case of any products you sell as well.
Another trend in the workplace is women in the workforce. It’s common knowledge that the degree or percentage of women in the workforce has increased during the last 30 years. Here we’re looking at it over a 32-year time frame. However, where the changes have occurred varies a great deal by level of education. If you look at the percentage of workers who have less than a high school diploma, between 1970 and 2002, the amount of change was appreciably larger for women, but not nearly as large as you go up the scale of education. As you go up the scale of education, there’s been more and more demographic change. When you get to dealing with specific industries, as John mentioned earlier, or things like this, it’s important to keep in mind that the distribution of gender may change from year to year. If you’re using a unisex product, which is simple and designed for worksite sale, you have to take into account that one of the hardest things to do when you’re setting your premium rates is to come up with unisex rates that take this sort of thing into account. Lapse rates may vary by men and women, but the premium rates don’t. Lapse rates may vary by degree of education. The premium rates either may or they may not, depending on whether a product is industry rated, and even that is just an approximation.

The important thing in all this is to keep in mind the fact that when you design a simple product, you have all the same complicated type of considerations you always have when you’re doing gender-specific or age-specific products. You have to find a way to account for it in the pricing. The challenge for the regulator is to look back at a product that’s been brought in, say at a certain level, and try to figure out whether or not the assumptions that are being made are reasonable. Regulators have an interest in not having companies come in with large rate increases, or any for that matter. They would prefer to see that these sorts of things are taken into account. It’s the sort of thing where I think companies and regulators can share information in terms of what they expect to see. A lot of this is, when you get into the future as speculative, but very often you can find relationships between sales patterns and census information and you can use census projections from there to go.

Family types. Once again, these types of products are typically sold with very simple types of rate tiers. Maybe a few family structures rather than family plus one and family plus two -- although that’s also seen sometimes. In looking at that, it’s important to understand the family structure that exists out there. Now this is information from the U.S. Census Bureau, and if you look at married couples with children, obviously during that 33-year time frame, the percentage of the population that consists of married couples with children has shrunk a tremendous degree. Some of this is a little bit misleading because some of that is the fact that

you have baby boomers in the higher ages whose children have left home. So there is a little bit of the age demographic shift that underlies this as well. But clearly, there has been more of a trend over time toward men and women who live alone, non-family households, other types of family households. The loss, of course, has been in married couples either with or without children as a percentage of the population.

In framing your actuarial issues, it’s important to understand where the trends in this sort of thing are going. Largely in terms of if you subsidize premiums to any degree, between one family class or another. But also, if you’re trying to design products with an understanding of what’s going to happen to people in the long term, products have to be designed to be simple, but they also have to be designed to be able to grow with people if you’re going to guarantee renewability. If you’re not, and you’re going to price from year to year, these things become more acute concerns if you price on the margin.

That’s the incredibly short course on worksite demographics. Another thing that has to be looked at is policy lapsation. What is it that’s different about worksite policy lapse than, say, just a standard individual product? Well, it’s got some strong ties to factors that are outside the control of the insurance company. One of them is how often people change jobs within the workforce. Guaranteed renewable-type insurance is designed so to make it easy for an employee to take it with him when he leaves the workforce. However, very often because of changes in the workforce, or economic stresses that are put on the employee, he may lapse policies at that time. There’s only a limited amount that companies can do about that. It’s outside the control of the companies.

Obviously, that means that in designing products that are either lapse supported or the opposite of lapse supported, it’s important to realize that there is a degree of risk that’s involved for the company that has to do with factors they cannot control. Sometimes state insurance departments have a philosophy that termination risk resides with the company. They will not hear of allowing for rewrites in cases where the risk has been one of termination rates. Other states have a different philosophy. It varies, and it sometimes varies based on interpretation.

There are also other factors outside your basic plan design, and a lot of it has to do with things that are sort of going on in the world at large. Say you’re a supplemental health provider and people buy based on where they think the gaps are in their major medical plans. Well, if their major medical plan changes year after year, they may decide that they either need or don’t need the coverage that they had. Some companies are looking for different ways to try to address that issue. There also can be other environmental issues that change things -- whether people are saving more or less money; what’s going on with the government; what’s going on with things like health-care savings accounts or medical savings accounts; what’s going on with unreimbursed medical plans. Do states have specific

health plans? All of these things have to be taken into account.

There is, in the end, a peculiar pattern of lapsation with worksite-marketed products. If you come to it from a different market, where people sit down over a table and are sold individual insurance with a fairly long presentation, you’re liable to greatly underestimate the size of the lapse rate.

These are some environmental trend numbers. I’m not going to go to them in any tremendous detail here. The important thing to note on here is that on the left-hand side is the size of the deductibles (see Morey slide 12, page 6). This is between the year 2000–2004 and this is from the Kaiser Health Foundation. Mostly what you see here is that deductibles for every type of major medical plan are going up. Now the employer has an employee population that is aware that the deductibles are going up. If the deductibles are going up, it’s probably because the employer can no longer afford to pay for plans with deductibles that are lower. So what do they offer instead? Well, worksite-marketed products are usually the solution the employer will come up with, in terms of being able to address a variety of health issues. On the right-hand side, it gives you an idea of where the different sorts of medical expenses are. Hospital and physician and long-term care expenses. Retail expenses: Who out there knows what these are? Retail expenses are like medicine. Like nonprescription medicine and things people buy. Nobody covers that. Nonprescription medicine, it turns out, is a pretty high-cost item in terms of total health care in the United States. I don’t think most people think about it, because it’s not a particularly onerous burden on any one person. It’s interesting to note how much of the cost comes from retail-type items in the health-care market. Contractual relationships. Dom did a good job of going over the peculiarities of worksite and what it is, but it’s important to note that even though your premium collection relationship was the employer. For individual business at the very least, the contractual relationship is with the employee and the sales relationship is with both. There is a relationship with what you approach an employer to offer them your products. They have to agree to it. Then you have to make sales to employees of individual products. Obviously, in cases where there’s a group mechanism used, you abrogate some of that.

Underwriting. This has been touched on already, but I want to deal with it a little bit. In selecting risks, you want to look at what risks are appropriate for the type of coverage offered, but you have to balance that versus the fact that very often there’s a speed and simplicity of underwriting that’s required. He mentioned earlier that there are yes or no questions that are like, well, I answered it, yes, so I’m not allowed to get the coverage. Those types of knockout questions are very common because they accomplish a goal. We’ll take people of a certain class of health risks and we’ll do it on a very broad, simple basis, with easy to understand questions. Have you ever had a heart attack? That might be a yes or no question for a certain type of policy.

Also, there’s classification of risk. As well as selection of risk, there’s classification, and typically this is done in very simple basis. Where there is sub-classification needed, and one of the questions that the pricing actuary had is how much sub-classification is necessary to preserve the stability of the product? I know it’s an area where regulators sometimes have an interest in understanding how sub-classifications are arrived at and to what degree they either add or do not add to premium stability.

An issue when you do underwriting that is this simple is the opposite of selection, which is anti-selection. In certain cases where your underwriting is deficient or you’ve got holes in your policy provisions (or sometimes where you have multiple product offerings), you put the selection in the hands of the insured. Selection in the hands of the insured is typically called anti-selection. It can show up sometimes in places where you’re not expecting it. Obviously, with guaranteed renewable insurance, your ability to deal with anti-selection is low, because if it’s on the long-term basis, as was mentioned before, like with actual charge, chemotherapy-type benefits, once you’re in that position, you can’t really ever get out of it. The fact that you have the right to raise premium rates does not mean you’ll ever be in any way whole on those types of things. So it is important to deal with anti-selection at the underwriting level; it is absolutely imperative to deal with it at the policy level and not put an anti-selective mechanism into the hands of insureds.

Let me talk a little bit about claim costs for pricing. I apologize a little bit for what comes after this because this is how to talk about claim costs without actually showing any claim costs. So take my word for it, these are really claim costs. When you’re developing claim costs if you’re a consultant or if you’re an insurance company, it’s definitely best to use worksite-specific data. If you’re dealing with guaranteed renewability, you’ve got to be able to project forward for life, which means you also have got to deal with any number of trend issues.
One of the things I do not think was mentioned earlier is that when you’re dealing with guaranteed renewability and you’ve got a product for life, you typically do not leave inflation in the benefits. Because there is no way to control premiums for life, benefits are subject to inflation. I guess we alluded to it tangentially, talking about actual charge benefits for chemotherapy. If you’ve got to project forward for life, typically, you set indemnity, flat-type benefits, which are determined at the time of policy issue, so that the only risk you run is that of the frequency of claims.

Underwriting means claim costs typically vary with wear off. You expect to start low with sickness-related conditions and gradually build up higher, and in doing demographic-claim costs, you’ve also got to look at the demographic trends we alluded to earlier.

Now here’s a classical sort of a pattern (see Morey slides 20–22, pages 10–11). This is not by duration. This is by age and there’s also a durational pattern, but typically a classical type pattern. You have relatively few sicknesses or health-related conditions at lower ages. Then it gets quite a bit higher and then there is

something of a leveling of that at a certain age, but there’s an age of declining health for all those people who ever hit 40 and say, “The day I turned 40, everything started falling apart.” Well, yes, it looks like 50 is worse.

This is a very typical pattern for this type of thing; it’s not unusual. However, it’s not unusual at worksite marketing to see a pattern like this. What this is, is it’s really the same pattern, but there’s something wrong with your underwriting or policy provisions that allow people to select against you in the very first year that a policy is sold. A nightmare for insurance companies is to sign up people who already have the condition, a condition that you cover. Through a variety of causes, it is very possible for this to happen. Sometimes through state regulations that may require certain types of coverage. For instance, say you are required to cover newborns from the moment of birth and a person who takes the policy is pregnant, and with a high-risk pregnancy. This is something that has happened in a number of states to any number of companies, and they can tell you, if it’s only that bad, they’d be happy.

However, it’s not unusual to see a claim cost pattern like this and when you see it, you know there is something wrong with your policy design. It is also possible to have this in a controlled fashion, with other peculiar type of designs, but most of the time this would be a sign that something is wrong.

Here’s another pattern, and this one is a little bit harder to read. This is more typical of what you might see with accidents. Of course, what I would expect with accidents is for those two bottom ages to be higher than they are. I think if you were looking at accidental death, they would be. But when you’re actually looking at accidents, and you’re looking at the age of the primary insured, you also have to take into account accidents on parts of their children and various family compositions, and things like that. Sometimes you’ll see claim costs that look relatively flat, like this, and it would be very odd to have premium rates that were low, went higher, went lower, then went higher again. So, typically, this is the sort of case where you smooth this kind of thing out in your premium rates and maybe charge one rate for everybody.

Expenses. Normal actuarial considerations are what apply here. You have got the normal things, but you know the cost of issuing the policy and cost of maintaining the policy.

One important thing to take into account in doing this is states have gotten more and more interested in looking at expenses and trying to figure out the reasonability to determine the reasonability of people’s pricing. I don’t know how many of you out here are regulators, but if I put myself in the place of a regulator, I get a filing in my hand and I’m supposed to evaluate whether it’s any good. It’s nice to have a little bit of information. It gives me an idea that all these things are thought through. To the same degree, a pricing actuary is asked to sign a memorandum for a health policy saying that this meets all the actuarial

considerations; many of the reviewers seriously take their responsibility to try to be able to validate that to some degree. Most expense issues with worksite are not that unusual. They only get to be unusual to the degree you start making special concessions for accounts or doing special work with them, which is more in the group of the large group area.
Taxation. I put this slide in here just because anyone who is doing PD has to have something with taxation in there. There really are two types of taxation issues with worksite-marketed products. One is taxation of the policyholders themselves and the policies themselves to whether they are pretax or after-tax dollars. Another thing is that sometimes benefits can be taxable. People know that for things like disability insurance, where the employer is paying for it. They may not be as aware of it in terms of certain types of lump-sum policies and things that people do, where it’s possible for the benefits to be taxable. It’s one of those things where, when you design a product, it’s important to be clear and be able to be clear to your policyholder, what the ramifications are of purchasing a product. A person who bought a very large lump-sum critical illness product might be in for a shock when he finds out the benefits are taxable and didn’t know.

Also, there’s the taxation of the company. Obviously, when setting your assumptions, you want to look at premium taxes across states and similar things, as well as income and other taxes. It’s really in terms of how you measure your profitability.

Other actuarial issues. There are really three types of requirements in terms of regulatory requirements on the front end. One of them is reporting requirements, which include things like that of the reporting from year to year of experience. That varies a lot from state to state. Some of them have more stringent requirements than others. Loss-ratio requirements are typically required at filing. There has been something of a trend away from loss-ratio requirements However, they still exist and are going strong in one form or another in all 50 states and Washington, D.C.

Consumerist requirements were a little bit newer. I use this term to describe a class of things where regulators start asking the company for things that companies typically haven’t had to say, like when you price something, what your profit margin is. Has anyone here run into that with Colorado or New Jersey? Where they ask you what your profit margin is? We’ve run into the case where the department doesn’t know on what basis they want us to say what it is. We’ve gotten into explanations trying to say, well, what do you mean by profit? When you’re dealing with consumerist, as opposed to reporting a loss ratio, you’re typically not dealing with actuaries, and it can be very hard to have the conversation with someone who doesn’t have the technical apparatus. Most of the time, when you’re dealing with loss-ratio reporting requirements, if you are a regulator, you are an actuary, and you’re dealing with an actuary at a company or vice versa.

The profitability measures that people use for worksite marketing really depend on what your strategy is and what you’re going for. Some states, as I said, have

profitability projection requirements. Monitoring of ongoing experiences is obviously needed in this type of business. This is like one of those things that you throw on the end of every answer to an actuarial essay question. You have to monitor ongoing experience. You really do have to monitor ongoing experience because if that's how you learn, and then that's how you're able to adjust your changing issues.

I'll turn it back over to Dominique.

MR. DOMINQUE LEBEL: We'd like to open it up for questions.

FROM THE AUDIENCE: Craig Cox, American General. John, you mentioned that if you file on a group basis, you have to avoid the small group rating laws? Can you go into more detail on that and how it's done?

MR. JOHN KIDDER: Well, yes, depending on the products, certain products are excluded from small group rating laws. However, when you're dealing with health products, a lot of States will require you to comply with small group rating laws and so you've got to make sure that you don't issue to groups that are considered small groups. It varies by State.

FROM THE AUDIENCE: OK, and I'm sure that hits the mini-med product very high?

MR. JOHN KIDDER: Yeah, for example, I think Florida may define a small group to be 50, is that right, Linda? Fifty and below. And in other states, it may be as low as 10 or 15. One other distinction there is, I believe Florida's definition of small group is number of certificates issued, and perhaps some other state requirements are actually number of employees in the group.

FROM THE AUDIENCE: Joe Pizani, self-employed consultant. When some of the companies got in the worksite marketing, one of the thoughts was that it was a more natural distribution channel because of the affinity of the employees at the workplace. I was wondering in your experience, and this is to anybody who wants to answer it. In your experience are you seeing that evolving to the point where at some point, companies may be able to go in and sell things like 401(k), retirement plans, maybe a non-financial plan because of the nature of the workplace as a distribution channel. Is that coming to bear at all?

UNKNOWN SPEAKER: I would say yes. I think that eventually if we look at the future of worksite, we're going to see a lot of different types of products being marketed. Probably casualty products, life products, 401(k) products and in my opinion, in the evolution of worksite will change, especially as define benefit plans are replaced by define contribution plans. There's a mind-set that the approach is going to be more of a defined-contribution approach to a lot of these products. The evolution is related to the increased consumerism that we have, and the fact that a

lot of people get most of their benefits at their worksites. So I think the trend will be to offer all sorts of different benefits at the worksite.

FROM THE AUDIENCE: Alex Cogan with AIG. I'd like to ask the panel a question on the issue of participation, and in particular, for group insurance-type plans. First of all, as you mentioned, to get guarantee issue, you typically require minimum participation. But oftentimes, it's very difficult to predict in advance if you're actually going to be able to achieve that. So what you people do if you don't achieve it, in terms of counseling the group, or reunderwriting the group, and also in terms of pricing, do you see trends or companies looking at pricing with different pricing points, depending on the participation level achieved?

UNKNOWN SPEAKER: To handle the second question first, yeah, the morbidity does vary quite a bit by participation, and unfortunately in the voluntary market, it's not generally very good. So, the rates will generally reflect that. A typical minimum participation requirement might be 30 percent to 50 percent. It depends on the product. Could you repeat the first question?

FROM THE AUDIENCE: What do you do when you don't meet the participation? What do companies do?

UNKNOWN SPEAKER: That's going to vary by company. I know of some companies that will send the group back. They reject the group and make the agent fill out the applications. Other companies have something called guarantee to issue. They'll issue something. They'll make the employee fill out the application and issue something, but it might not be what the person applied for. It might be a very stripped-down version of it or have a conditions waiver. Still other companies are kind of wishy-washy and they'll go ahead and issue the group and deal with the agent later.

FROM THE AUDIENCE: I'm Vince with Manhattan Insurance Group, and we hear a lot of talk about association business growing. What's a nutshell description of a successful model for association business?

UNKNOWN SPEAKER: That's a good question. I think the key, again, is employer/employee relationships. An association of self-employed individuals generally is going to be a little tougher to verify in common, things like that. It's going to depend on the product. Different associations are going to have different characteristics, so a mini medical product may do fine in one association, like say an association of truckers. Believe it or not, I have a client who has an association of truckers. And disability product just doesn't work that well. A good model is going to be tailored to that individual association. We just go to consider all of the factors.

FROM THE AUDIENCE: I'm kind of interested from the group perspective but I'm curious about the commission structure and whether worksite products tend to have a higher commission level in the first year?

MR. DOMINIQUE LEBEL: Can you identify your name and company please?

FROM THE AUDIENCE: Lance Stevens, Standard Insurance Co.

UNIDENTIFIED SPEAKER: I seem to be closest to the microphone, so I’m fielding a lot of things. Yeah, because of the persistency issues associated with group products, the commissions tend to be either levelized or first-year commissions are lower than, say, for a guaranteed renewable product.

MR. DOMINIQUE LEBEL: This concludes our session and thank you for your participation.