HIAA®

Health Insurance Association of America

An Employer's Guide to Disability Income Insurance

An Employer's Guide to Disability Income Insurance

When you're looking at your financial plan and considering your assets, you probably think about tangible things like homes and bank account balances. But perhaps your most valuable asset is your ability to make a living.

What would you do if you or one of your employees were injured or became ill and couldn't work for a period of time? How would you pay your bills? How would your employees?

Americans rank disability as a major source of potential financial misfortune. Protection against that risk lies in disability income insurance, a product that provides income should you become sick or injured and unable to work. It protects you and your family against financial catastrophe by helping you to meet daily expenses.

More and more employers, like yourself, recognize the value of disability insurance as a benefit. These products offer peace of mind, because if employees suffer a disabling illness or accident, they can focus on recovery, knowing their financial stability is protected. By providing competitive benefits to your employees, you can attract and keep workers while increasing productivity as well as the overall health and well-being of the workforce.

Disability coverage gives employees protection and peace of mind

Almost everyone needs disability income insurance to safeguard income. In the event of a disability, insurance coverage can be the financial bridge to restored health and productivity. Yet while more people have this type of insurance today than in decades past, only about one-third of all Americans have long-term disability (LTD) insurance, according to John Hewitt and Associates, Inc. (JHA), a disability risk management consulting firm. The 2001 *JHA Disability Fact Book* also shows that only slightly more than that (roughly half) have short-term disability (STD) income protection.

Demographics play a role in the increasing importance of this type of policy. As the population ages, people are more likely to need disability coverage. In fact, the Social Security Administration anticipates a 37 percent increase in disability incidences due to the aging workforce.

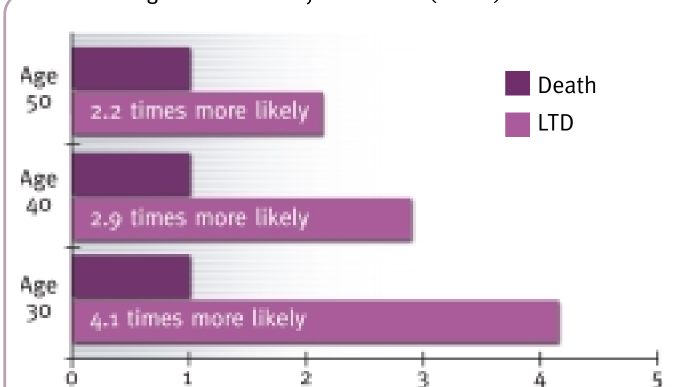
"The majority of the workforce is older, so need is certain to be greater," explained Drew King, JHA president. "The average age of a new LTD claimant is about 44. The peak of the 'baby boom' was 1961, so in 2004-2005, boomers will reach that age when they are that much more likely to experience a disability and need insurance protection."

However, it's not just older people who are disabled by illness and accident. Younger people need disability insurance, too. At age 30 an employee is 4.1 times more likely to become disabled than die.

While many people can handle a few months without income, as time passes the bills mount and solutions are hard to come by without insurance protection. Many who have

FIGURE 1

Risk of Long-Term Disability vs. Death (Males)



Sources: 2001 JHA Disability Fact Book. Adapted with permission of the publisher from the 2002 Field Guide to Estate Planning, Business Planning, & Employee Benefits, by Donald F. Cady, copyright 2002, The National Underwriter Company.

experienced a disability say the relief of knowing there is financial protection already in place for themselves and their families greatly enhanced their ability to focus their energy on getting well and returning to a productive life.

"Disability insurance is an absolute 'must,'" said Donel Young, president of Hansen & Young, a Point Pleasant, N.J.-based public relations firm. Young purchased disability insurance when she and her partner started their business in the early 1990s. Young says she wouldn't consider being without it. "Without disability insurance, there is no safety net."

Disability insurance coverage offers many advantages

Since disability protection is something employees need and want, it only makes sense that employers want to provide the coverage. Beyond the needs of workers, these benefits offer important advantages to employers.

Benefits packages can be critical to attracting and retaining talent. The *2001 EBRI/MGA Value of Benefits Survey* reports that 77 percent of prospective employees cite benefits as very important to their decisions about taking a job. This fact is not lost on employers — 56 percent of the employers who offer disability insurance cite attracting and keeping employees as their motivation for offering coverage.

"Employees value benefits more highly than their cost to the employer, and appreciate the cost and quality advantages of group purchasing power," explained Mark Andruss of Fortis Benefits. "As a result, employers with competitive employee benefits programs can more readily attract and retain the employees they need for improved productivity and growth," Andruss said. "The benefit for the employees is even more direct — peace of mind when they are healthy or unimpaired, and income replacement and better case management in times of need."

But savvy employers understand that disability insurance is both a benefit and a health and productivity tool. The rehabilitation and management tools built into a group disability plan can yield substantial savings to employers, particularly in large organizations. Such programs help people return to productivity, relieving huge direct and hidden costs of disability.

The hidden or "indirect" costs of disability, such as salaries for replacement workers or the value of lost productivity, are an expensive problem for businesses. A recent study by the Work Loss Data Institute reveals that when the total cost of disability is measured, it eclipses medical insurance costs for a business. The study states, "For U.S. employers in 2000, for all conditions together, direct disability lost-time costs were $91,360 per 100 workers, total disability lost-time costs (including direct costs) were $458,150 per 100 workers, and medical costs were $268,539 per 100 workers." The study concludes that, including indirect costs, "lost-time costs exceed medical costs by a substantial margin."

"The key value is in getting people back to work. When you ask people who experience a disability, they will tell you overwhelmingly that they want to work," said Mark Bradley, marketing director for Integrated Disability Resources. Moreover, disability experts say employers have a critical communication role with the recovering employee.

> "One of the most effective actions in helping people return to work is having a supervisor call and say, 'We want to see you back.' Without those kinds of contacts, the person worries about whether they have a job and that can lead to misunderstandings."
>
> **– Richard Quebec**
> Disability product manager at Liberty Mutual

Don Bergen, human resources director at commercial printing giant RR Donnelley, notes the employer also benefits from taking an active role in getting the employee back to work as soon as possible. Bergen is documenting savings from a two-year effort to improve disability management at the company. "From the employer's point of view, the real value is in reducing — or in some cases eliminating altogether — hidden costs of disability." *(See case study on page 7.)*

Building your company's plan

You probably already offer employees some kind of short-term sick leave, which may last from a few days to as much as six months, depending on how long they have worked for you. No laws require that employers offer LTD insurance, but estimates show that almost half of mid-size to large employers provide long-term benefits for at least five years. Typical group long-term disability benefits replace about 60 percent of salary, start when sick leave and short-term benefits are exhausted, and continue anywhere from five years to life. LTD insurance is generally considered protection against a catastrophic illness or injury.

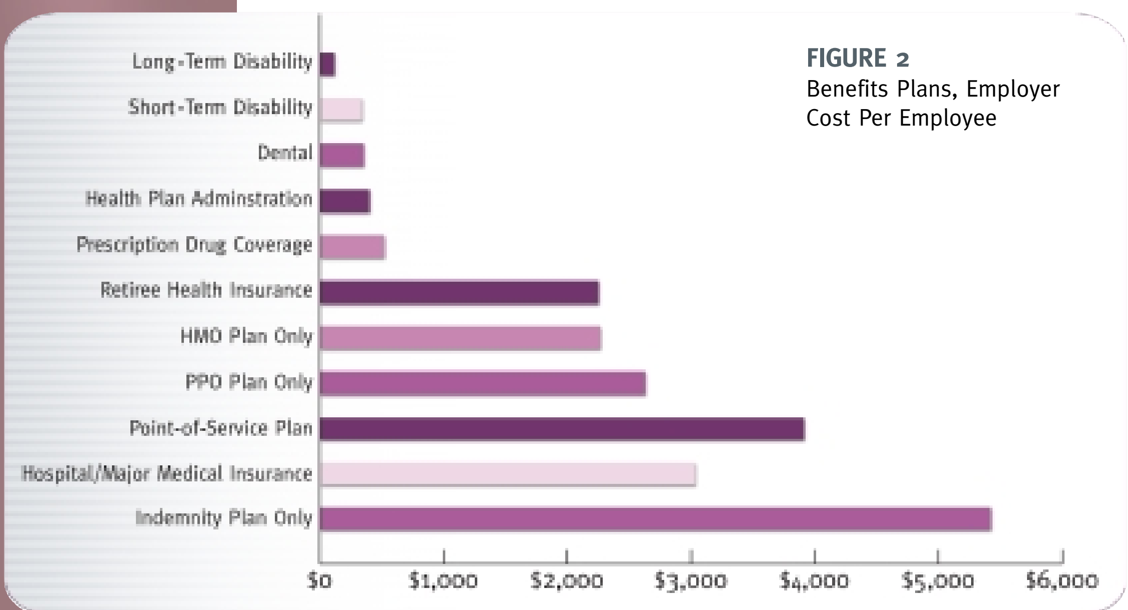


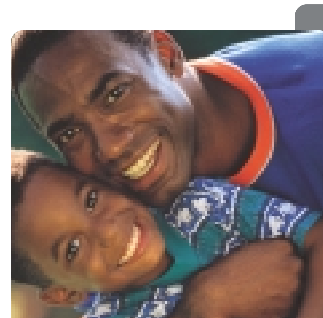
FIGURE 2
Benefits Plans, Employer Cost Per Employee

Source: 2001 Employee Benefits Survey, prepared and published by U.S. Chamber of Commerce. The full report may be ordered at 1-800-638-6582. Reprinted with permission.

There are also short-term disability plans. STD insurance also starts when you exhaust your sick leave and provides a percentage of your salary. The difference is in the duration of benefits. This duration varies with policies but is typically six months.

Employees value STD benefits because they are more likely to use short-term coverage. Their risk of financial devastation, however, is far greater if they become unable to work for a long period of time.

Ideally, employers should offer STD and LTD in a seamless package. An integrated program assures that rehabilitation experts are involved early, looking for the best ways to return a person to work and leveraging those early intervention opportunities to the benefit of both the employee and workplace.



This approach also allows employers to out-source more administrative tasks, such as qualifying employees for benefits and sending checks.

An insurer can provide the early intervention offered by STD benefits and the protection of LTD plans for roughly $300 to $450 per employee in annual premiums. The coverage can be fully paid by the employer, cost-shared with the employee, or offered as an employee-paid, voluntary benefit. In many cases, employers fund a basic plan to protect employees, and employees may then add supplemental coverage to better address their individual financial circumstances.

What to look for in a plan

DISABILITY DEFINITIONS

Long-term disability plans provide income when an employee is unable to work in his or her "own occupation," or to work in "any occupation" for which the person is suited by education, training, and experience. Some plans have the more restrictive "own occupation" standard for an initial period — usually two years. During this time the plan pays benefits if the person cannot perform the essential work functions of the job in which the person was employed when he or she became disabled. That two-year period is customarily followed by the broader "any occupation" standard. Under this standard a plan would continue to pay benefits only if the person were unable to perform any job functions for which he or she might be qualified based on education, experience, and training.

INCOME REPLACEMENT

Plans typically replace 50 to 60 percent of income. Plans are structured to balance financial assistance in a time of great need with incentives to return to work.

WAITING OR "ELIMINATION" PERIOD

Benefits in a long-term disability plan usually start 30 to 180 days after the disability occurs. It's best to coordinate coverage so that once any sick pay and short-term disability benefits have been exhausted, long-term disability benefits start immediately.

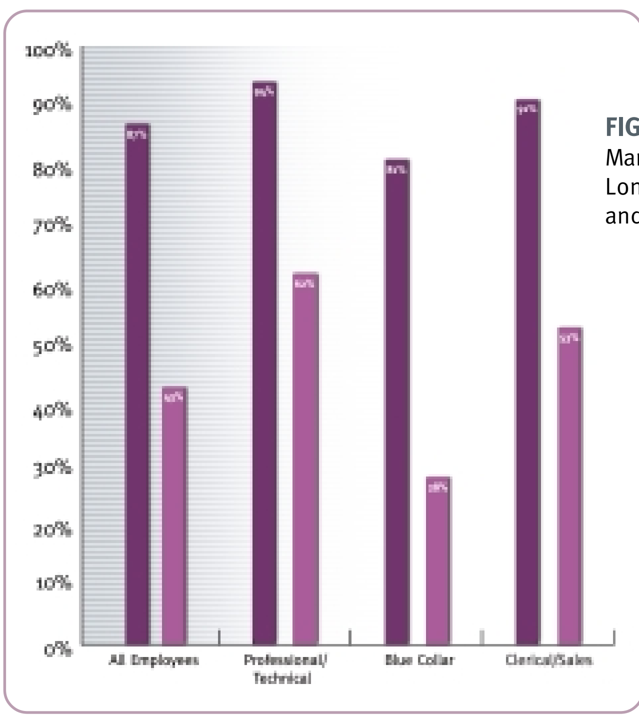


FIGURE 3
Market Penetration – Long-Term Disability and Life Insurance

Life
LTD

Source: Bureau of Labor Statistics, 1997

RESIDUAL OR PARTIAL DISABILITY

Residual or partial disability benefits help when an employee experiences a disability and then returns to work part-time. The partial payments offset earnings lost while the employee makes a transition back to a full-time schedule.

REHABILITATION

Look at the rehabilitation and disability case management capabilities the insurance carrier offers. Consider how successful the carrier has been in helping people return to productive work. Also, look into how well these rehabilitation and management resources coordinate with services your company provides on its own, or through other benefits service providers. Easy integration for seamless administration is key to program success.

EASE OF USE

It is a big plus when employers and employees have plenty of easy, timely ways to get information. Large employers often value on-line access or other simple methods to obtain facts about their short- and long-term disability experience: How many people are out? How long on average? At which locations? Employers of any size often find value in receiving help with the Family Medical Leave Act (FMLA), Americans with Disabilities Act, and other regulations. Disability insurance plans are a potential tool for making FMLA notification in a timely, accurate way. From the employee perspective, plans often work best when there are multiple ways to get information — mail, fax, phone, on-line. The easier it is for employees to access information they need — such as status of a benefit check — the easier it will be for the employer's human resource or benefits area.

CUSTOMIZATION

It is essential for short- and long-term disability insurance providers to customize a plan with an eye on a company's existing benefits and information systems. This is particularly true for large organizations of 2,000 or more employees that may

State and federal programs offer only limited help

Many people believe that the state or federal government will step in with financial help if they become disabled. While it's true that some assistance may be available, it may very well not be adequate for individuals and their families' needs.

Most salaried workers in the United States participate in the federal government's Social Security program. Most know Social Security for its retirement benefits, but the Social Security Administration (SSA) also administers disability benefits. In March of 1999, $4.2 billion in Social Security disability payments were sent to 7.2 million Americans.

Your salary and the number of years you have been covered under Social Security determine how much you can receive. The average monthly benefit from the Social Security disability program in 2000 was $801, according to the SSA. This contrasts with average monthly consumer expenditures for two-income families with children of $4,091.

Also, just because you apply for benefits doesn't mean you'll receive them. The 2001 *JHA Disability Fact Book* reported that among the 1.2 million applications for Social Security disability in 1999, only 52 percent were approved. And, because of an application backlog, the waiting time to receive Social Security disability is often two to three years.

When thinking about your financial needs and what Social Security Disability Insurance (SSDI) will — and will not — cover, there are some important points to remember.

- The standard to qualify for SSDI is more stringent than just about any private plan. A person must be unable to engage in "any substantial gainful work which exists in the national economy." This contrasts with private coverage, which usually defines disability as the inability to do one's "own occupation" or an occupation that matches training, education, and experience.

- The same SSDI definition also requires that a person be severely disabled. Their inability to work must result from a condition that, as described by the SSA, is expected to result in death or that has lasted (or can be expected to last) for a continuous period of not fewer than 12 months.

  The test of disability with private coverage is generally the ability to perform the essential functions of one's job and does not require a "permanent and total" or long-term disability. Also, private plans offer different degrees of disability acknowledged and numerous plan features. Some features make payments for "partial" disabilities, and coverage can even be purchased to continue contributions to college savings during the period someone is unable to work.

Workers' compensation only covers you at work

Workers' compensation is state-mandated indemnity insurance. It covers both lost income and medical expenses when injuries or illnesses happen at work.

This type of coverage evolved as industrialization resulted in increasing risk for America's workers. Today, however, 63 percent of all disabling injuries or illnesses occur outside of work. For those injuries or illnesses, workers' compensation insurance can't help. That's where short- and long-term disability insurance help fill the gaps. People want the higher levels of security against unforeseen expenses caused by illness or injury that can happen anywhere. Disability income insurance offers this security.

- Social Security disability doesn't necessarily cover all employees. Because the U.S. workforce is aging, the SSA reports that the proportion of workers covered has climbed more than 80 percent. However, people must work a set number of years to qualify for SSDI. This leaves younger workers with added exposure. By contrast, the younger worker usually qualifies under private disability plans within a year, or less, of starting a job.

  Some states offer disability protection. California, Hawaii, New Jersey, New York, Rhode Island, and Puerto Rico fund short-term disability coverage (26 weeks in most states, except California) through a combination of employer and employee contributions. In all other states — representing about 80 percent of the workforce — employees have no comparable protection unless their employer provides it as a benefit.

  SSDI and state-funded programs provide limited disability income assistance to individuals who qualify for the benefits. But these programs are only the most basic safety net — in most cases, they don't provide adequate financial support to maintain a worker's pre-disability standards of living.

already have some form of disability insurance and are making a change or addition to their program. Look at how well the plan will work with and transfer information from prior plans. See if the plan offers provisions that solve problems specific to your organization.

COORDINATION/INTEGRATION

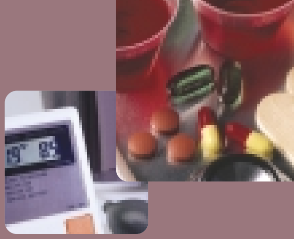
The best plans coordinate the short- and long-term benefit processes, and also coordinate with other health and welfare benefits the employee may need to access — workers' compensation being a prime example. How tightly the different benefits need to coordinate or integrate depends on the size and nature of the organization. Larger companies likely will have more benefit programs to coordinate and greater potential gains from active management of those programs because they will have more claim situations. Smaller companies, especially those with little or no human resource staffing, primarily need a quality plan that works well at all junctures in the process — communicating the benefit to the employee, serving the employee as a customer, and integrating easily with other benefits.

Another alternative in coordinating benefits would be to supplement your group disability insurance with individual disability income insurance. Group disability insurance is a very valuable benefit, but may leave a gap in coverage for some individuals (i.e., those who are highly compensated). Supplemental individual disability income insurance can be customized to help fill any gaps in coverage. You choose if the individual policies are employer- or employee-paid. (Contact your insurance representative or financial professional for more information.)

Case study: Disability management offers big benefits for employees and employers

Like many firms, commercial printing company RR Donnelley has tasks that get put on hold because of other pressing matters. But these days, people on transitional duty following a disability are tackling those tasks at the Chicago-based company, proving that a little forethought can boost productivity and improve return-to-work outcomes for employees.

Don Bergen, human resources director at RR Donnelley, was all too familiar with the scene that would unfold on



the morning an employee was due to return to transitional work. A supervisor would scramble for an assignment the person could do, inevitably resulting in assigning unfulfilling tasks and increasing the risk that the return-to-work effort would fail.

Working with Ann Arbor, Michigan-based independent human resource consultant D. Kerry Laycock, and a team of occupational nurses and other resources under the disability plan, Bergen's group developed the "transitional duty task bank." The concept was simple: Ask people on the plant floor what needed to be done, document the best ideas, and share the ideas across all plants on a Web-based system.

RR Donnelley employs 34,000 people, and on any given day, there may be 700 people absent for a variety of reasons. "A single plant employs from 300 to 1,500 people, so the number of people absent amounts to a whole plant full of people not working," Laycock observed. "Looking at it from a task-based perspective, we asked what the pay-off would be if we could return even a fraction of those on disability to the company as productive labor, doing work that needs to be done."

Detecting compressed air leaks in manufacturing equipment, calibrating scales important to press runs, photographing and documenting damage to incoming shipments — these were all tasks significant to the company's performance. These replaced the menial, make-work assignments that were all too common before. Plus, everyone could see the value added, Laycock said, boosting the esteem of the returned worker and plant productivity. It also saved worker replacement costs and overtime pay that might have been required.

Ideas such as the task bank are the heart of managed disability or absence management strategies. Insurance carriers and disability managers deliver these strategies to address a larger mission — to create incentives for increased work capacity while helping to restore a person's ability and confidence to do productive work.

Bergen says RR Donnelley is documenting savings from a two-year effort to improve disability management, only part of which was the task bank. He knows the gains are big. One indicator: "We actually have had people at our plants say, 'We need more people on transitional duty to get all these things done.' "

HIAA®

Health Insurance Association of America

www.hiaa.org