

Insurance Association of Connecticut

Insurance and Real Estate Committee

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SB 141, An Act Concerning Disability Policy Offsets
And Dependent Children

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The Insurance Association of Connecticut wishes to register its serious concerns with SB 141, An Act Concerning Disability Policy Offsets And Dependent Children, which would prohibit group and individual long-term disability (LTD) insurance policies from having certain offset provisions.

The purpose of LTD insurance is to provide replacement income to eligible individuals who become disabled, equal to some pre-designated percentage of their pre-disability income. In addition, standard provisions establish an offset, to be subtracted from the policy benefit, for certain defined sources of additional income, such as Social Security benefits. The claimant still receives the same percentage of their pre-disability income, but in the aggregate from multiple sources.

Offset provisions are approved across the nation by state regulators. LTD policies are priced with the actuarial assumption that a portion of eligible claimants will have benefits offset by other income. That assumption allows LTD policies to be more affordable. Any statutory restrictions or prohibitions regarding the use of offsets will cause a corresponding increase in the cost of the policy.

Offset provisions are accepted as a product of sound policy design and cost considerations. Both the federal Social Security Disability Income program and Connecticut's statutory disability program for state employees (C.G.S. 5-169 and 5-192p)

contain offset provisions which reduce program benefits due to benefits received from other sources. In fact, the state program specifically allows a reduction for "any federal disability Social Security benefits," including dependency benefits (SB 141 would prohibit such dependency benefit offsets in LTD policies).

Group LTD insurance is usually provided through employers, who may pay up to 100% of the premium. Years of selling LTD policies has shown insurers that it is an extremely price-sensitive market, since LTD insurance is a voluntary coverage. The typical plan design for an LTD policy provides for a benefit of 60% of the insured's pre-disability income. Part of the reason for designing LTD plans with a maximum benefit amount is to encourage a return to work when the claimant's health condition permits.

Section 1(a) would limit offsets in group LTD policies to "benefits payable from other sources as a result of the disability." The vagueness and breadth of that language leaves it unclear as to its effect.

Is section 1(a) intended to prohibit offsets for retirement benefits? For example, offsets are made for benefits from defined benefit plans, as funded by the employer. The disabled claimant would not have made the retirement claim if not for the disability. However, insurers do not offset for benefits from 401k plans that the employee funds, nor do they offset for retirement benefits that the claimant was already receiving prior to the disability.

Insurers use offsets in group LTD policies in order to control costs and to ensure that the claimant's post-disability income does not approach or exceed his or her pre-disability earnings. It would be counterproductive for an employer to voluntarily establish an LTD program for its employees that would in effect create a financial incentive for them to remain on disability longer than necessary.

Insurers may also coordinate policy benefits with earnings the claimant generates while out on disability. Policies are structured to encourage the claimant to return to work on a part-time basis while disabled, and may provide that policy benefits plus part-time earnings may total up to 100% of the claimant's pre-disability earnings, usually for the first year of disability. After that period, policy benefits may be further reduced by a portion of the outside income.

If section 1(a) is interpreted to prohibit such a coordination, part-time employees on disability could be making more in the aggregate than their fellow full-time employees (non-disabled) working the same job.

As written, the last new sentence in subsection (a) would prohibit changes in LTD offsets to reflect increases in other disability benefits occurring on or after the claim commences, which is problematic. For example, this provision ignores the fact that the Social Security Administration usually provides a claimant with a rough estimate of his or her Social Security Disability Income benefits, once determined to be eligible. Inevitably that estimate must be corrected to accurately reflect the SSDI benefits actually available to that person, once all wage data has been collected and updated by the Social Security Administration. SB 141 would prevent such a correction, leaving the insurer with incorrect information on which to base its coordination of benefits.

IAC would also question why C.G.S. 38a-519(a) should be amended in section 1 to apply to a group health insurance policy "or plan". "Plan" has no apparent relationship to policies providing disability income protection coverage.

In section 2, individual LTD policies would be subject to the same offset prohibitions as in section 1. Individual LTD policies are bought by individuals and usually tailored to their particular needs. Reimbursement may be set at a percentage of

income or at a flat dollar amount that is set with the individual's income in mind. The applicant usually has the option, by rider, to choose whether the policy contains offsets or not. By choosing an offset product, the applicant can save appreciable dollars on premium requirements. By prohibiting some offsets, SB 141 would take away that flexibility for consumers, remove or limit choice and increase premiums, creating disincentives to buy the product.

Individual LTD policies can also be sold on a "group platform". An employer may arrange for its employees, usually lower wage earners, to have the option of purchasing individual policies whose terms have been pre-set according to the employer's design, including offsets. The policy would be less expensive for the employee than if he or she tried to buy a policy as an individual, due to the economies of scale. In such an arrangement, the employee also benefits from the fact that he or she can take the policy when leaving that particular job, and can continue to pay the lower rates.

SB 141 will create a disincentive for employers to set up such an option, as statutory restrictions on offsets would create the possibility of overinsurance, creating financial disincentives for employees to return to work. Premium costs of the products will go up due to the absence of offsets, creating less reason for employees to buy the product, resulting in less protection for their families in the event of disabilities.

IAC would ask the Insurance Committee to consider the public policy implications of SB 141.

- Less than 40% of employees across the country have private LTD coverage (group and individual).

- Statistically, three out of every ten workers will, before they retire, face a disabling condition that prevents them from working.
- In 2009, for the first time less than half the employers who provided LTD policies paid for or shared in the cost of the policy premiums.
- Disability claims are pouring into the Social Security Administration (3.3million claims expected this year, up over 25% from two years ago). This has led to much larger case backlogs, resulting in longer delays for eligibility determinations.
- LTD policies cover claims that SSDI does not. One insurer reports that almost 60% of its claimants receiving disability benefits under their policies were not awarded SSDI benefits.

By eliminating or restricting LTD offsets, SB 141 would (1) increase the cost of LTD policies, giving employers and/or individuals less incentive to purchase the coverage; (2) give employers less of a reason to offer LTD benefits, given the greater likelihood of overinsurance and the corresponding disincentive for their disabled employees to return to work when able; (3) create market pressures which could result in the reduction of benefits payable under the policy (say, from 60% wage replacement to 50% wage replacement), in order to negate the cost impacts of SB 141 and reduce the likelihood of overinsurance. Such a product would likely be less attractive to employers/individuals, giving them another reason not to buy.

The net effect of SB 141 could be more disabled persons having to exist on no LTD benefits, or on reduced benefits, as they wait many months for Social Security

Administration decisions, and the relatively modest replacement rates of SSDI if found to be eligible.

IAC would respectfully suggest that SB 141 would have a detrimental impact on the long term disability insurance marketplace and on the very consumers the bill is intending to help. We know of no other state that has passed or is even considering legislation similar to SB 141. IAC opposes SB 141.