



# **Disability Claims and Economic environment**

**Hoa Bui**

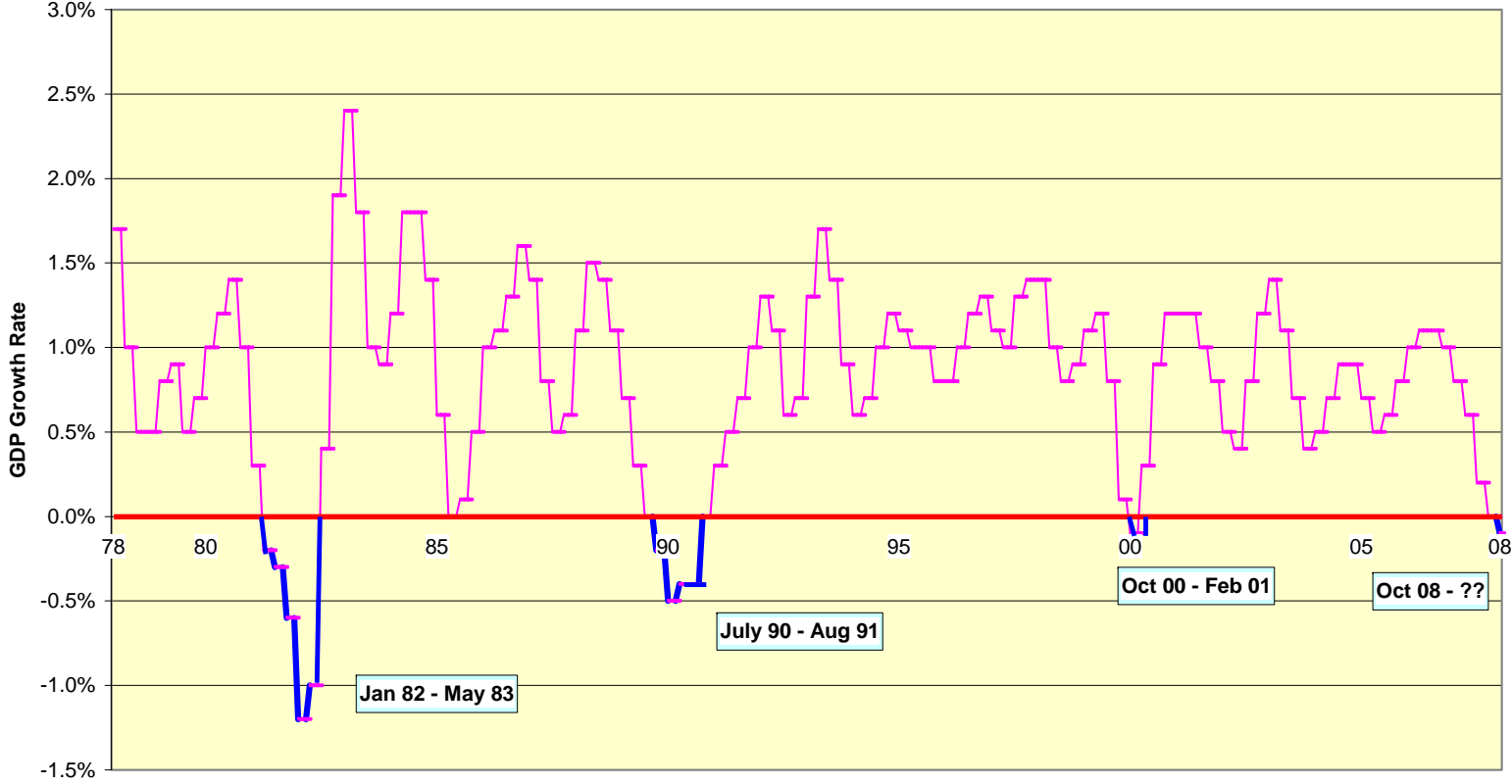
**KPMG 2009**



# Overview

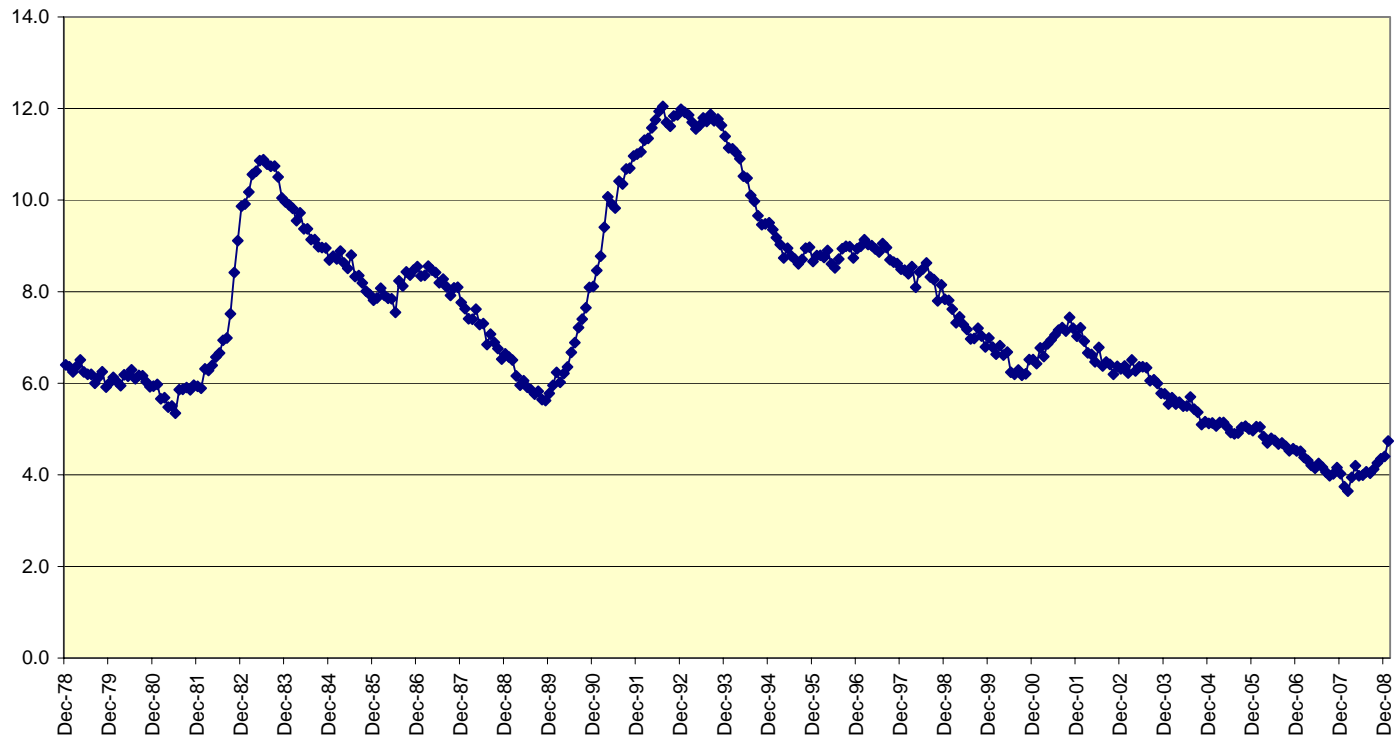
- Historic TPD economic related patterns
- Historic DII economic related patterns
- Potential outlook from early 2009

# GDP Growth Rate & Recessionary Periods



# Unemployment rate over 30 years

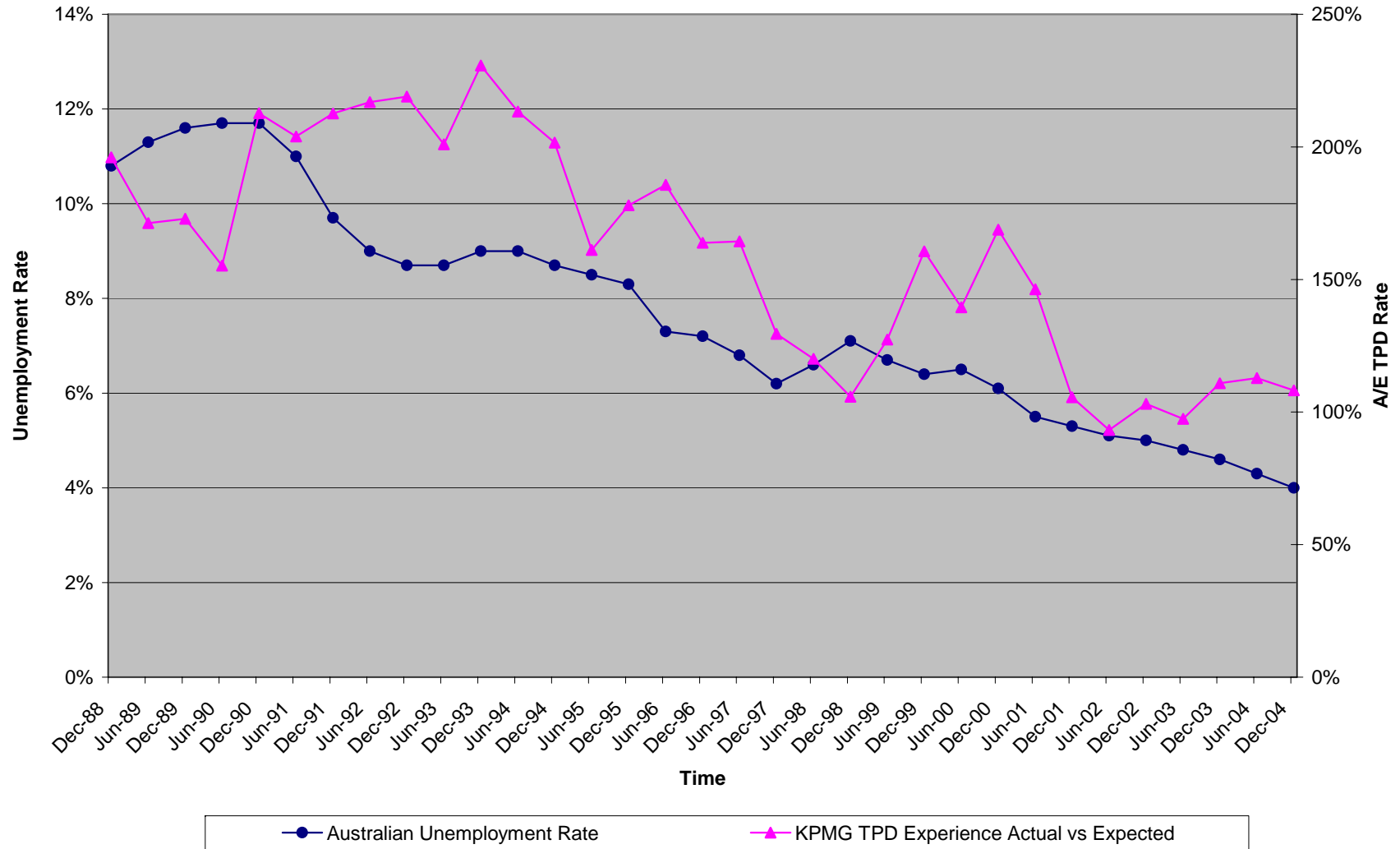
Unemployment Rate Seasonally Adjusted





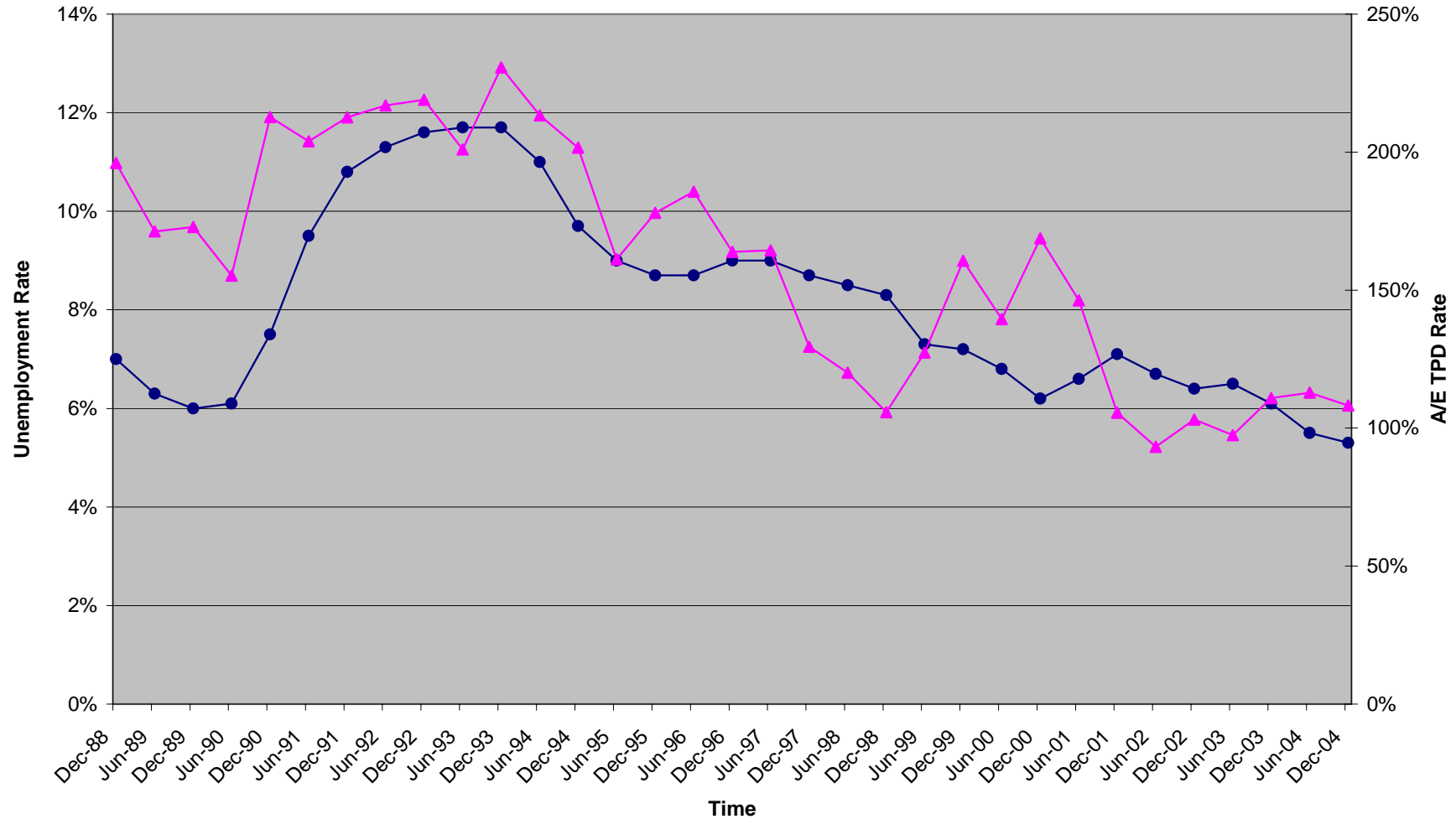
# **Historic Group TPD Economic Related Patterns**

# Historic Unemployment Rate vs. Group TPD Claims Rate



Source: KPMG Actuaries Group Life Experience Study  
 ABS Seasonally Adjusted Full Time Unemployment Rate

# Unemployment vs. Group TPD (Paid) With 3 year shift – Long Term



● Australian Unemployment Rate     
 ▲ KPMG TPD Experience Actual vs Expected

Source: KPMG Actuaries Group Life Experience Study

ABS Seasonally Adjusted Full Time Unemployment Rate



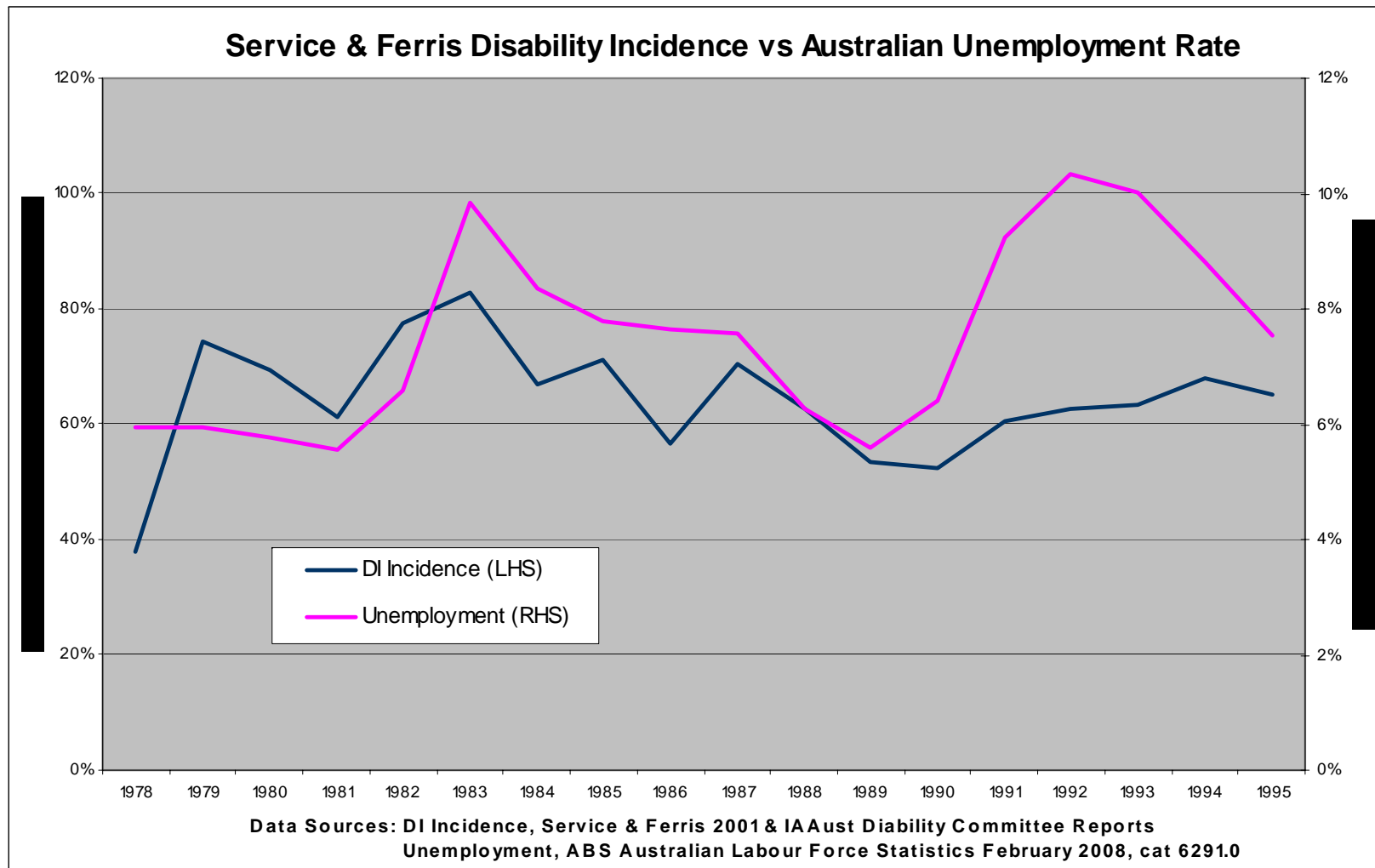
# Observations

- Historic indications:
  - Substantial increase during a recession
  - Range of increase rate depending of the period considered
  - Impacts emerging over subsequent 3 years
- IBNR impacts starting sooner (may be 1-2 years)
- Trends in longer term unemployment rates rather than short term headline unemployment may be a more relevant indicator?
- Based on history, would not expect to be seeing clear claims trends yet

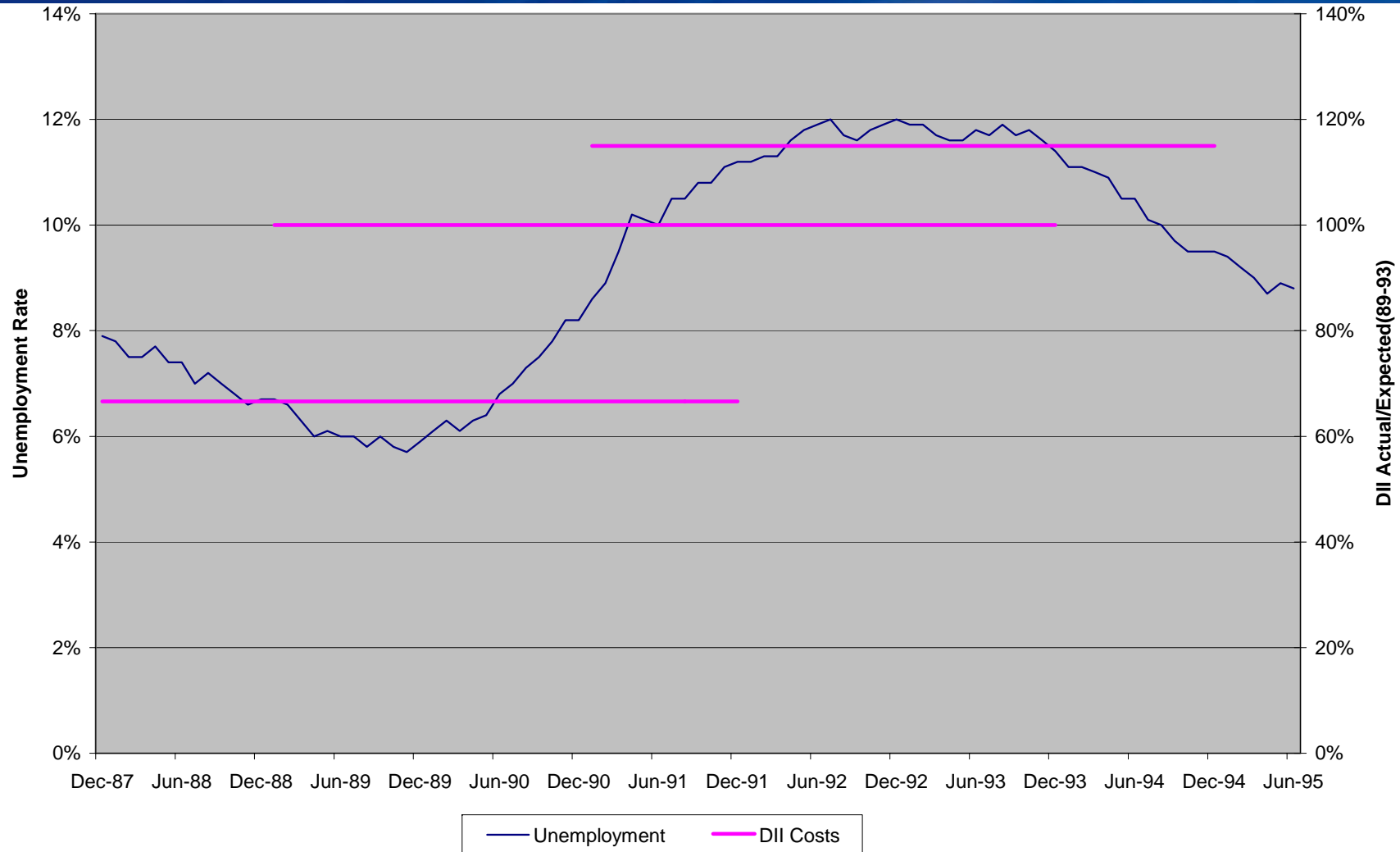


# **Historic Disability Income Insurance Economic Related Patterns**

# Australian Disability Incidence vs. Unemployment

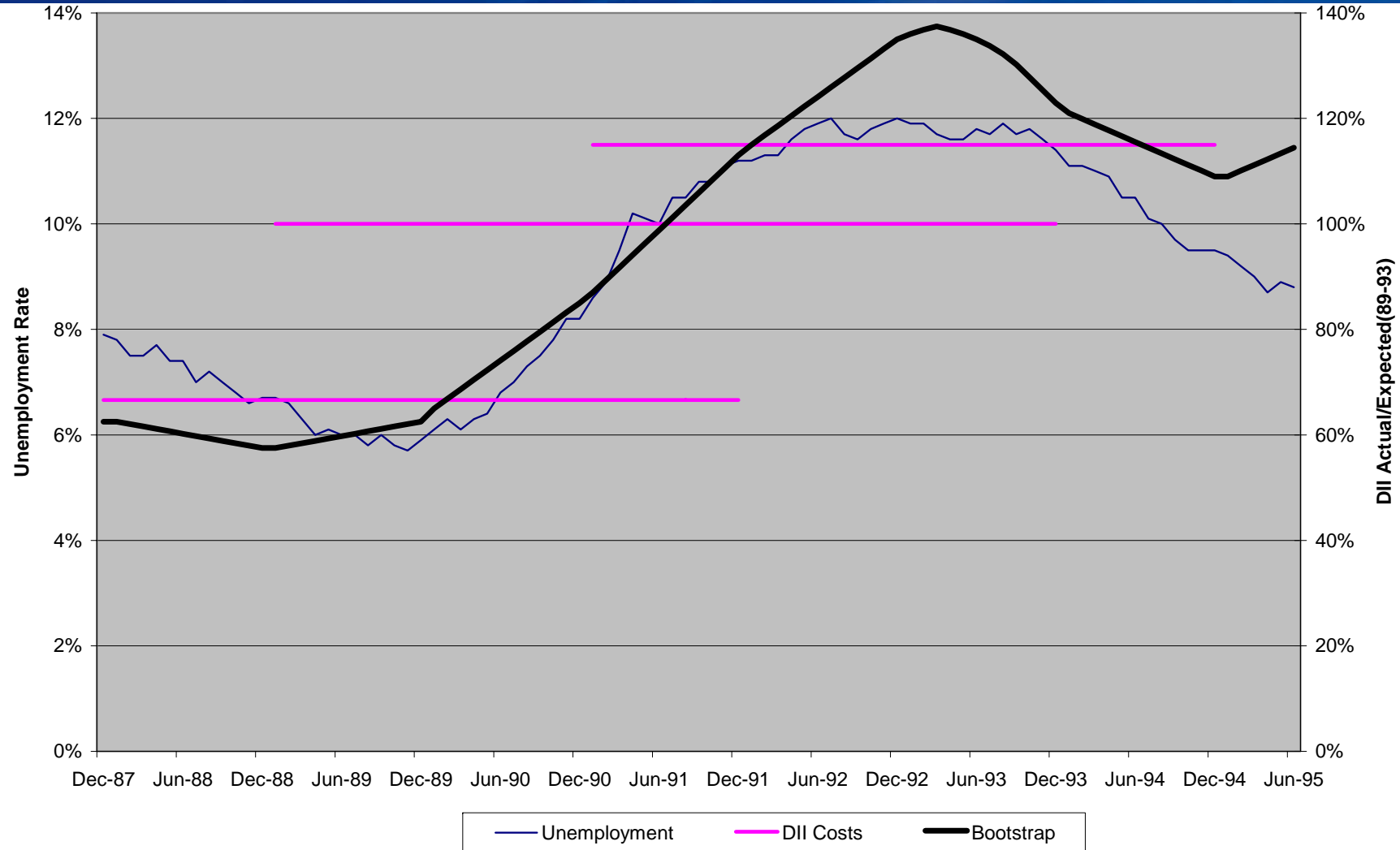


# Australian Disability Claim Cost vs. Unemployment



Source: IAA Disability Studies (84-89, 89-93, 92-95, 95-98)  
 ABS Seasonally Adjusted Full Time Unemployment Rate

# Averages Untangled



Source: IAA Disability Studies (84-89, 89-93, 92-95, 95-98)  
 ABS Seasonally Adjusted Full Time Unemployment Rate

# Observations

- DII studies covered overlapping periods of time
- DII experience has shown long term claims cost increases since the late 1980's, predominantly driven by factors other than economic environment
- Nonetheless:
  - There was significant rapid change around the 1990's recession
  - There has been static to improved experience in the more recent strong employment environment
  - Suggests underlying trend deteriorations
- The early 1990's show:
  - Some claims cost increase while unemployment fell 8% to 6%
  - Substantial claims cost increase (circa 83%) as unemployment rose towards 12%

# Observations

- Cost increase primarily driven by reduced termination rates rather than increased incidence rates
- The acceleration in DI costs appears to precede reported unemployment rates
  - Need earlier indicator than unemployment rate, perhaps ANZ job advertisement index ?
- Given current economic position, based on history, should be starting to see some trends in claim durations over the last 6 months

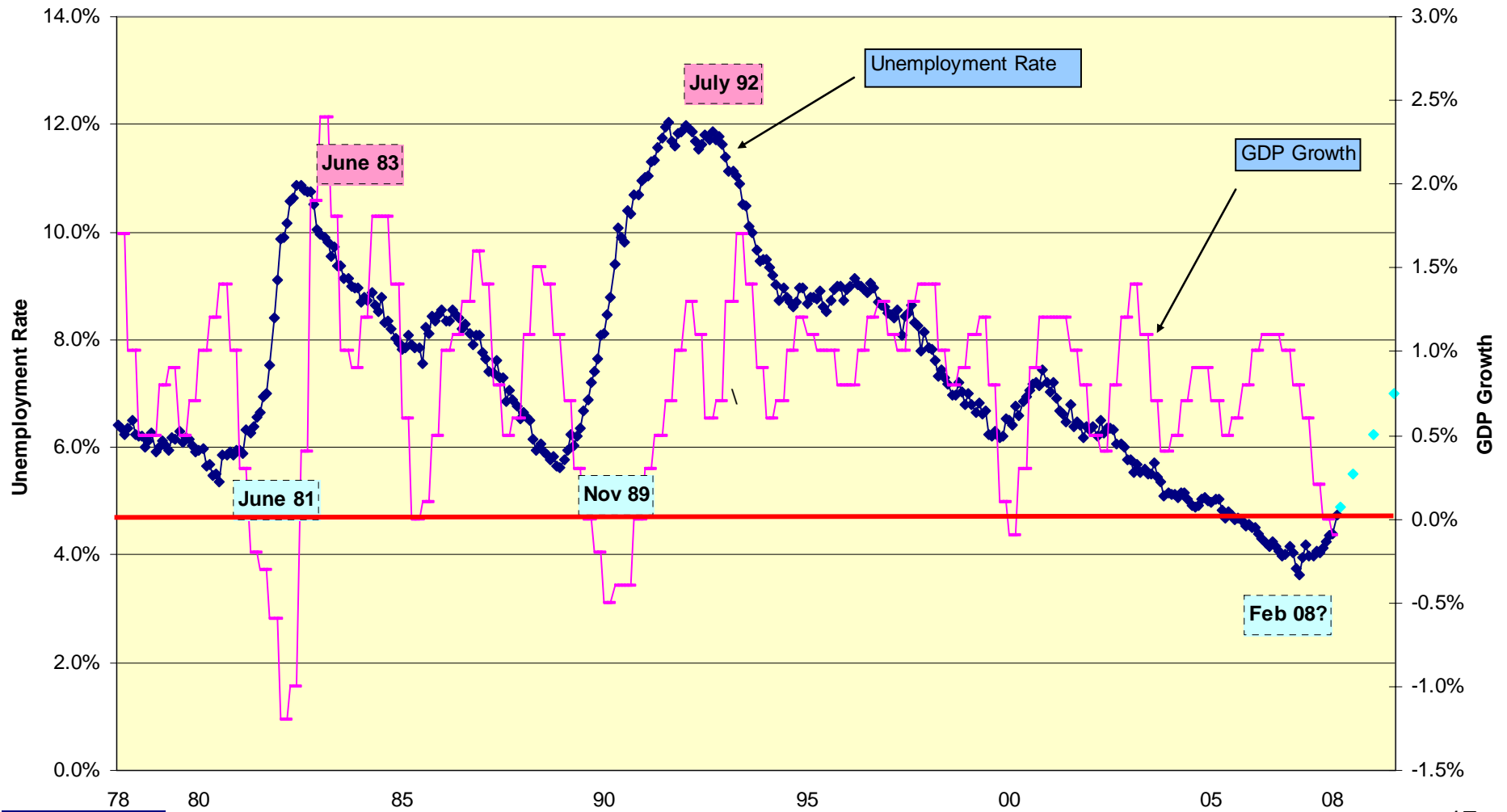


# Potential outlook from early 2009

# Potential Outlook for economy

- Latest Government forecast
    - Growth 0.75%
    - Unemployment 5.5% by mid 2009 <sup>1</sup>
    - Unemployment 7.0% by mid 2010 <sup>1</sup>
  - In March 2009, government admits forecast now dated – actual now expected to be worse
    - Unemployment Mar 2009 – seasonally adjusted 5.7%
  - In March, IMF forecast contraction of the world economy by as much as 1% - 1<sup>st</sup> time in 60 years
- 
- 1. Source: Australian Government, Updated Economic and Fiscal Outlook 2008-09

# Unemployment vs GDP Growth



# Forecast Experience Potential

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## Forecasts

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	<u>Unemployment</u>	<u>TPD Costs</u>	<u>DII Costs</u>	<u>Term'n Rate</u>
31-Dec-08	4.4%	100	100	100
30-Jun-09	5.5%	107 - 121	110 - 121	92 - 96
30-Jun-10	7.0%	114 - 141	121 - 141	78 - 89

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Note: DII Costs forecasts relate to termination rates deterioration mostly. Significant incidence deterioration could add to these cost increases.

# Potential Outlook for claims experience

Based on history, our hypothesis is that as unemployment increases :

- **TPD**

- +5% to +15% increase per 1% increase in unemployment
- Emerging over subsequent 3 years
- IBNR impacts starting sooner (may be 1-2 years)

- **DII claims costs**

- 7.5% to 15% increase in claims costs per 1% increase in unemployment
- Emerging quickly
- In the form of reduced termination rates

# Health Warning

*Please note:*

- *The world has changed since the 1990's, so history may be a cloudy crystal ball for the future*
- *The causes of the 1990's recession are very different to the causes of GFC*
- *There is a lot of noise impacting the analysis*
- *There is a wide range of underlying interpretations and current estimates*
- *Speed of change may differ from the past*
- *Claims management has come a long way since the 90's*
- *Claims termination rate may well revert to "normal levels"*



*A Berkshire Hathaway Company*

# Claim Challenges and the Big 'R'

**Jane Dorter**  
**Head, Client Services**  
**Gen Re LifeHealth Australia**

Prepared for the LDG, April 2009

# Global Financial Crisis – Impacts

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Global Financial Crisis Impacts:

Unemployment Rates

Disability Experience

US Forecasts

Australian Insights

Links to Claims Response

## GFC Headlines

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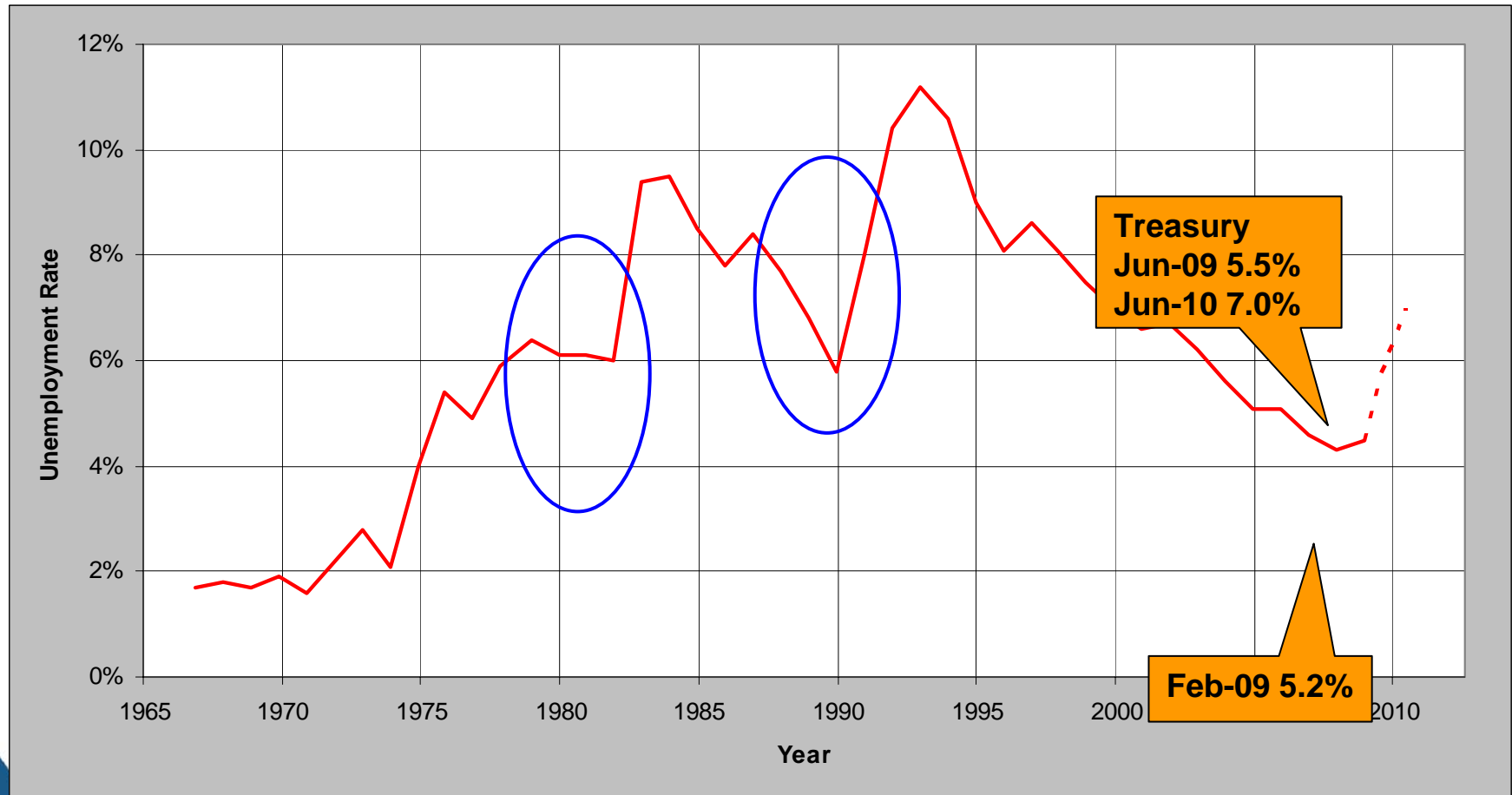
“Crisis forces companies to cut raises, bonuses, and benefits.”

“November/December redundancies highest in seven years”  
(2008)

“Microsoft announces first layoff in its history.”

“Recovery not expected until 2010, at the earliest.”

# Unemployment Forecast



“No escape from recession, says RBA, as OECD warns of 25m jobless”  
– *The Australian*, 1 Apr 2009

# Global Financial Crisis - Impacts

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Disability Experience – relationship to unemployment rates

Last recession to hit Australia was in 1990/91

unemployment rate increased from 6% to 10%

disability income market was \$200 million in premiums

Today

unemployment rate increasing – March '09 = 5.7%

disability income market in excess of \$1,300 million in premium income

# Global Financial Crisis - Impacts

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Disability Experience – relationship to unemployment rates

KPMG Actuaries data suggests for every 1% increase in unemployment rates:

Disability Income claims costs ↑ 7.5% to 15%

TPD claim costs ↑ 5% to 15% (with 3 year lag)

With unemployment forecast to be at least 7% by mid 2010 then we are potentially looking at a 20% to 40% increase in claim costs.

KPMG Actuaries' opinion is that, if history repeats itself, impact will be felt most in termination rates of claim, rather than incidence rates.

# Global Financial Crisis - Impacts

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Disability Experience – relationship to unemployment rates

What do we think ?

Claim costs will increase

KPMG prediction of 20% to 40% increase is realistic

Since 2002 we have seen disability claim costs decrease substantially – about 25%, so not unreasonable for this to reverse (unemployment rate was around 7% in 2001)

Note: most of this improvement was a result of decreasing incidence rates of claim, not termination rates.

Potential to get a lot worse if unemployment rates blow out

## US Forecasts

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USA – in period between 1999 and 2005 when unemployment rates rose from 4% to 6% and then dropped back to 4.5%, incidence rates for Long Term Disability remained flat.

Unemployment in the US is now over 8% and predicted to go over 10% in 2010

Previous recessionary periods of 1970's, 1980's, and 1990's with lower growth and higher unemployment resulted in increase in claim incidence and fall in claim terminations

US downturn of 2000-01 (pre 9/11) driven by technology sector and bursting of the “dot.com” bubble resulted in some increase in notified claims without an increased percentage of open claims. Many did not proceed past claims assessment - possibly due to increased focus on claims management

*Warren Buffett, March, 2009*

*“An economic Pearl Harbour...and an important war which could be won...with an expected recovery in five years...”*

# Global Financial Crisis - Impact

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US: assumption that in some occupational sectors where employment and wages are falling there is likely to be increased disability claims incidence

Predictions of an increase in claims incidence for:

real estate, construction, financial services/banking, investment/mortgage brokers, manufacturing, automotive sectors.

Predictions of a flat/lower disability claim incidence for:

healthcare, medical research, public sector, technology, law firms, and consultants

# Global Financial Crisis - Impacts

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- Interesting hypothesis in the US:

Current recession's impact on disability claims incidence may not be as bad as predicted. Why?

Household and consumer debt has risen to historic levels, home equity and retirement savings disappeared...workers cannot afford to claim disability and accept 60% of their earnings for prolonged periods.

# Global Financial Crisis - Impacts

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## Claims response:

Australia: if we assume previous investigations that indicate

- i. evidence of strong link on Group TPD
- ii. Worker's Compensation incidence

International: investigations prove

Canada: strong link on DI

New Zealand: strong link on Worker's Comp incidence

USA: strong link on long-term DI claims

UK: inconclusive on PHI experience

**Unemployment** seems intuitively to have a link to disability experience

D. Russell. Tower UW Conference – Moving Forward in Risk Management. March 2009.

# Global Financial Crisis - Impact

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## Claims higher than expected

- new admitted
- new reported
- open claim not closed



## Lower Profits

- higher payments to claimants
- reserve for future payment

## More Capital set aside

- ensure reserves are sufficient

D. Russell. Tower UW Conference – Moving Forward in Risk Management. March 2009.

# Claims Response

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All disability products relate to the *ability to perform work* for remuneration, therefore unemployment impacts through:

- Availability of work

But also the *motivation to work*

- behavioural (benefits of additional source of income)
- fraudulent claims - insurance fraud may increase

Particular concerns around more “*subjective*” disability causes

- psychological conditions
- muscular-skeletal conditions

Other potential risks:

Underemployment – drop in working hours and remuneration – partial claims

High levels of personal debt – self employed undeclared income

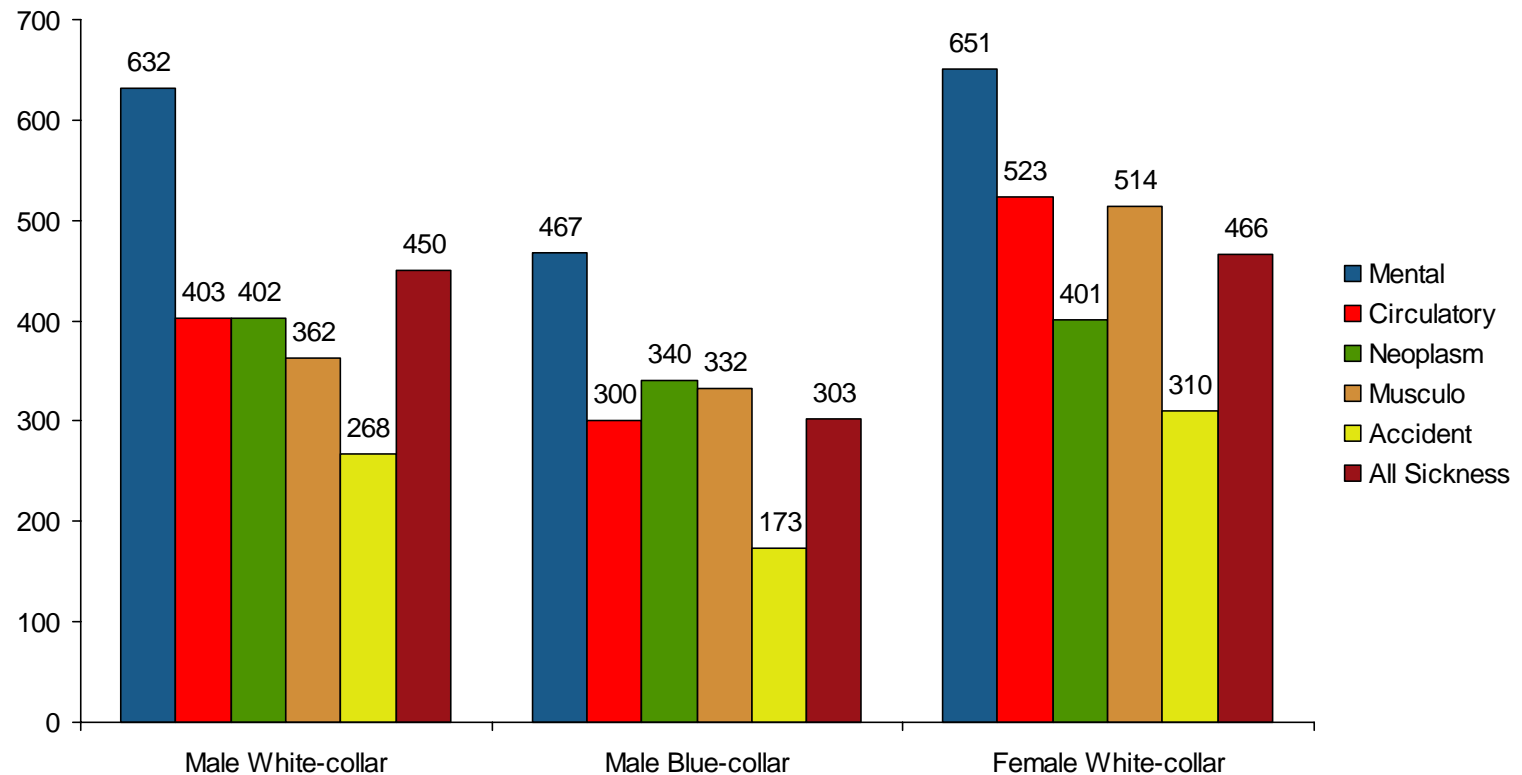
Suicide rates - economic issues may increase suicide rates for middle/upper income classes – wealth/debt ratio loss

Where should our response be?

Claims incidence or Claims duration?

# Mental illness the longest running claim

## Average length of claim in days



Based on 2 companies cause of claim data only  
Weighted by claim numbers  
Only causes with number greater than 100 claims shown (except female white-collar circulatory)

# Global Financial Crisis - Impact

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What would a GFC Claim look like?

## Medically Disproportionate Disability Outcomes

- There is clear evidence of many compensable claims having medically disproportionate disability outcomes
- It is estimated that in approximately 20-30% of cases, the level of disability and associated distress is significantly greater than may be expected from the physical factors alone
- US Research on Disability indicates in approximately 5% of cases, the physical and social outcomes are seriously affected to an extent that cannot be explained by initial or the remaining condition
- In extreme circumstance, the effect of adverse psychosocial conditions can lead to permanent incapacity for work and profound psychological and social withdrawal – even in cases where the initial injury or illness is apparently very minor.

Psychology, Personal Injury and Rehabilitation: The IUA/ABI Rehabilitation Working Party, 2004

# Global Financial Crisis - Impact

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## Claims Focus on Incidence:

- Increase in notifications requires increase in risk profiling

## Claims Focus on Duration:

- Decrease in termination rates requires increase in RTW management

## Shift in Claims Management Ideology

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- Acknowledgement that research now supports psychosocial factors are equally, if not more important, than biological factors within a claim
- Accurate Profiling of claims (upon receipt of the claim) is still key to this 'stepped' approach and is critical for screening the 'high risk' and 'at risk' claims early.
- Recognition that the biological factors alone can no longer presume to imply, or be equivalent to the length of disability
- Decision regarding the Disability Claims Management Model utilised in your Claims Department and the potential to integrate biopsychosocial mechanisms into your current claims management practices and processes

Risk Profile Model and Duration Management Model

## Brief Screening of Psychosocial Factors

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- Competency of Claims Professionals to:
  - Build Rapport
  - Basic Interviewing Techniques
  - Questionnaires
  - Utilising Stem Questions (\*poor outcome predictors)

Presence of a belief that pain is harmful or severely disabling

Fear-avoidance behaviour and reduced activity levels

Tendency to low mood and withdrawal from social interaction

An expectation of passive treatment rather than active participation



# Predictive Factors of Improved RTW Outcomes

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## INDIVIDUAL FACTORS

- Positive Expectations and increased self-efficacy about RTW
- Low levels of depressive symptoms
- Low levels of fear-avoidance of work

## INSURER FACTORS

- Proactive Case Management can influence the trajectory of a claim
- Delays in processing of claims can have a strong impact on the probability of chronic work disability

## HEALTHCARE PROVIDER

- Positive recommendation for RTW to patient
- Proactive communication with addressing workplace factors
- Reassurance regarding prognosis, and encouragement of maintenance of activities

## WORKPLACE FACTORS

- Work Accommodation
- Increased job control and decreased job demands
- Sense of legitimacy of injury and symptoms
- Non-confrontational Approach from Supervisor

# Global Financial Crisis - Impact

How will companies cope with the impact

## Claims Management

- resourcing appropriately
- management information
- allocation of resources
- both new claims and claim terminations

## Product Design & Pricing

- pricing loadings for the economic cycle
- price appropriately for vulnerable group schemes
- re-pricing existing
- group premium guarantees offered

## Underwriting

- careful of vulnerable industries
- financial underwriting important
- vigilant of churning

## Risk Management

- reinsurance options
- risk concentrations monitored

# Global Financial Crisis - Conclusion

Australia's recession = Expected higher IP claims costs

What will your response be?


Warren Buffet, letter to shareholders

... of the 2008 year:

*"By yearend, investors of all stripes were bloodied and confused, much as if they were small birds that had strayed into a badminton game."*

...by March 2009:

*"I've never seen Americans more fearful ....it takes five minutes to become fearful, much more time to regain confidence. The system does not work without confidence could recover in five years."*



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# LDG – April 2009

Claims' Challenges and the BIG "R"

Darren Parsons – Retail Claims Manager, AMP



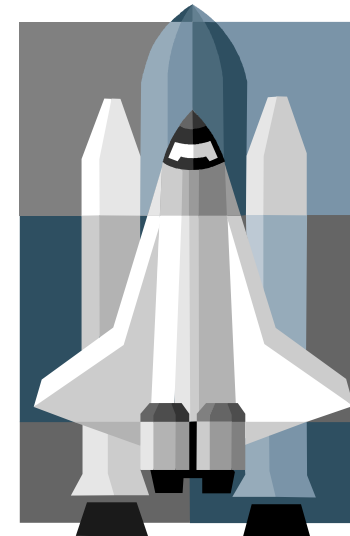
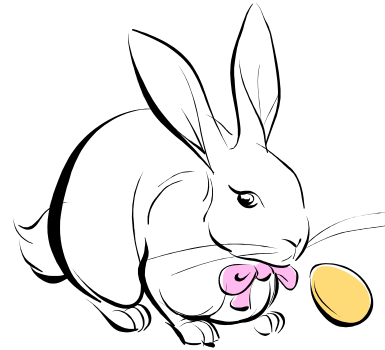
# Agenda

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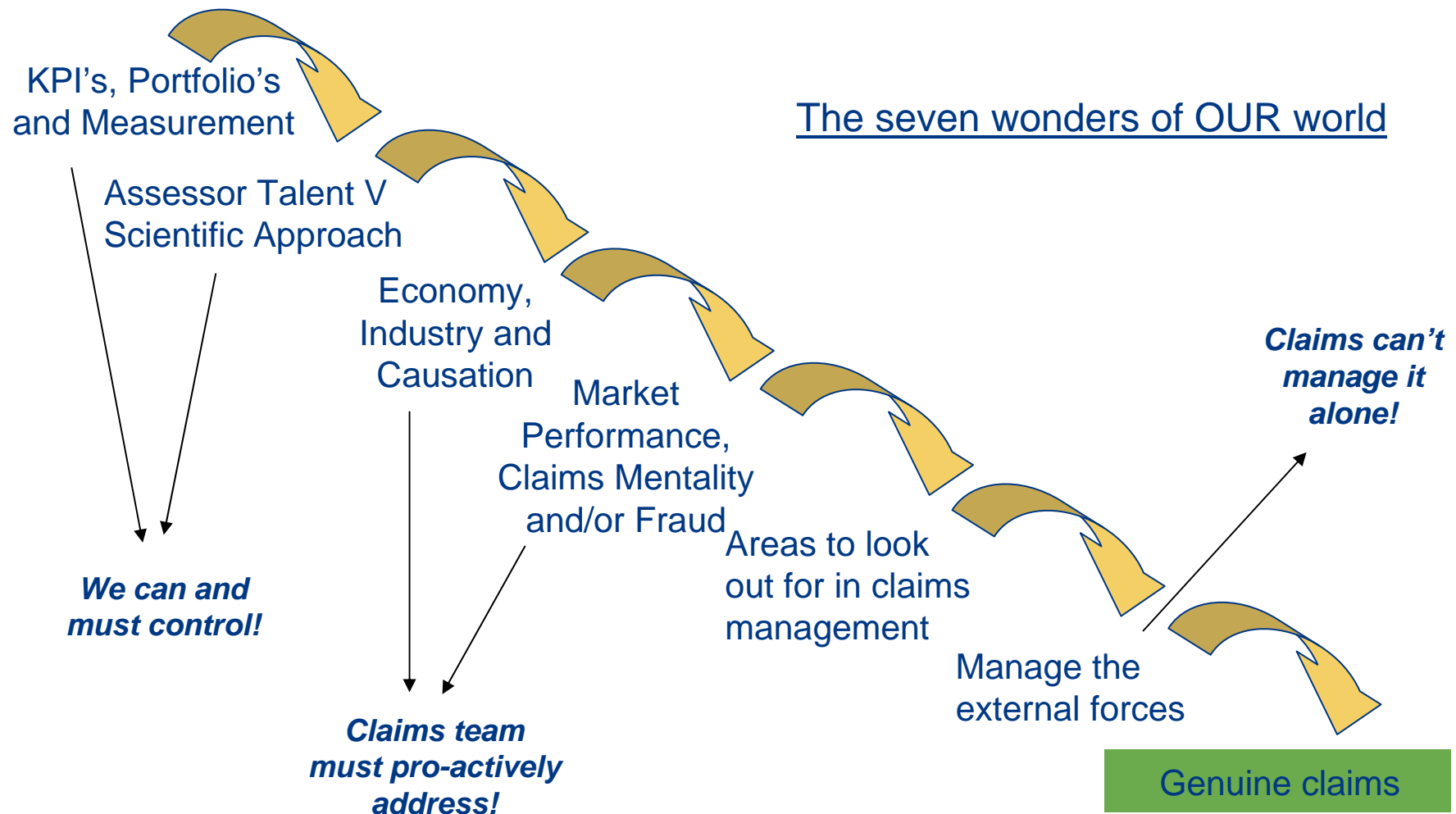
- Hoa's discussion paper – “Economic indicators and recent investigations”
  - Jane's discussion paper – “Insights from Australia and US”
  - Darren's discussion paper – “Local feel – what are the fundamentals”
- 
- Key focus for me – Unemployment V Disability !

# BIG “R” = Recession, Risk & Response

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# The mystery of claims management



# KPI's, Portfolio' and Measurement

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- ❑ KPI's don't lie nor change, they simply become more critical during challenging economic times
  - Review your KPI's, eg E2E times, finalisation or termination rates, average claim durations and claims costs
  - Set and manage objectives/expectations on Notifications V Initial assessments
  - Ratio of Partial claims V Total claims on book of business
  
- ❑ Portfolio levels on claims inside 12 months must be maintained and where applicable reduced
  - Be prepared to juggle entire portfolio to ensure claims in the early stages are targeted
  - Even small % increases in average portfolio can equate to significant increases in claims durations (months)

# KPI's, Portfolio' and Measurement

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## □ Measurement, measurement, measurement!

- Weekly snapshots on performance
- Identify potential 'problem' claims early and target them
- Forecast expected performance in immediate month and Quarter, on all KPI's
- Quarter on Quarter performance

# Assessor Talent V ‘Scientific Approach’

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- ❑ Scarce availability of experienced Assessors in managing IP claims (any market – bull or bear)
  - Much difficulty in securing and retaining experienced Assessor talent in market
  - Large % of Claims Assessors may not have been exposed to previous situations where there has been an economic downturn
  
- ❑ Maintain and enhance growth of our people
  - Maximise training initiatives even during the busy times
  - Our people will be the biggest KPI on our experiences and trends - entrust and empower them

# Assessor Talent V ‘Scientific Approach’

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- “Scientific process approach” is a key
  - Review your claims guidelines, they may need to be tightened and policed for these specific times
  - Introduce or reinforce a documented process including Business Rules and tight claims management controls – referral points
  - Mandatory steps in process complement Assessor talent and produce outcomes

Balance the best between your talent and your way of doing things

# Economy, Industry and Causation

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- ❑ Business' folding, Retrenchments and Income dropping and/or flattening – incidences rise during challenging economic times
  - Particularly those on commission based salaries and where significant bonuses are payable
  
- ❑ Specific occupational classes to watch include:
  - Commission based remuneration employment
  - Building and construction
  - Manufacturing and Retail

# Economy, Industry and Causation

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- ❑ Prevalence of Subjective conditions will rise including:
  - Psychological (Anxiety, Depression, 'Pressure' and Stress)
  - Muscular-Skeletal, Pain
  - Fatigue
  
- ❑ Expect to see Surgical claims rise, eg Knee, Shoulder
  - moves to have longstanding medical conditions addressed during 'slow' times or unemployment

# Market Performance, Claims Mentality and/or Fraud

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- ❑ Potential for fraud heightened during tough economic times
  
- ❑ Blurring of “Wealth Creation” plans V Income “Replacement” plans
  - Right of return demanded by consumer
  
  - Blame game

# Market Performance, Claims Mentality and/or Fraud

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- ❑ Durations of IP claims blow out due to termination rates declining
  - Greater incentive (Subconsciously or Consciously) for 'claims mentality' to present/rise
  - Consumer supplements income and/or fulfils 'rights' of personal exertion income through Insurer
- ❑ Usual or own occupation definitions lock in long term claims when no job/employment to return to
  - Insured knows the wording and may play on capabilities until market picks up

Important and fundamental question to ask up front – Why off work?

# Areas to look out for in claims management

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- ❑ Raise awareness and process in carefully viewing lapse/reinstatement records of policies for 6 months and immediately prior to claim

- Instincts by consumer, cease disposable expenses
- Mid term financial difficulty, compensate losses

## ❑ Late Notifications

- Problematic in good times, but investigate these claims even more during these times

## ❑ Profiling claims

- Capital City V Regional

# Areas to look out for in claims management

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- ❑ Financial review and understanding the status of business prior to claim
  - Particularly Partial Disablement claims must be closely managed
- ❑ Early intervention and rehabilitation processes to be heightened in these times
  - Significant opportunities lie in performing rehabilitation, especially during challenging economic times (particularly focusing on vocational realities and labour market)
- ❑ Commencement of condition or symptoms V business and job performance

# Manage the external forces

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- ❑ Closely monitor product performance during these challenging times, what is sound philosophy under your product, what is not
  - Increase Stakeholder communication
  - Update trends, experiences and future lessons
  
- ❑ Fast track professional development of field managers (BDM, BRM)
  - Increase claims awareness and prepare Planner force for raised intensity at time of claim

# Manage the external forces

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## ❑ Importance of financial underwriting intensifies

- Also look closely at specific occupations/industries
- Weigh up appropriate offer – may see an increase in indemnity plans being offered

## ❑ Product value and conditions to be tested

- Agreed Value philosophy
- Reduced TD waiting period to qualify under PD & extension of benefit period under PD
- Inability to invoke business income offset clause

# Genuine claims

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- ❑ Despite the challenging economic times and the need to tighten some practices relating to claims management, never lose sight of your goal to pay all genuine claims
- ❑ Resist the temptation to bottle neck genuine claims by ‘over the top’ claims requirements. Hence, “as little as possible, as much as necessary” must still apply
- ❑ Continue to manage your claims in a method that is consistent with and reflects your core business goal including your product and underwriting philosophies

# Genuine claims

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- ❑ Ensure you maintain and develop caring relationships with your claimants, customers and Planners so that they continue to be advocates of our companies and hence reflecting our industry in an appropriate manner **especially at these challenging times of need**

**This can be the Best and Worst times of publicity for our industry and your company – make it your Best !**



# **Claims and economic environment Actions**

**Hoa Bui**

**KPMG 2009**



# Actions

- Review Claims management practices
- Improve analysis tools
  - Experience studies
  - Analysis of profit
- Improve management information
- Review Underwriting practices
- Pricing and product changes
- Reserving : IBNR , economic overlay
- Managing stakeholders expectations

# Questions

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