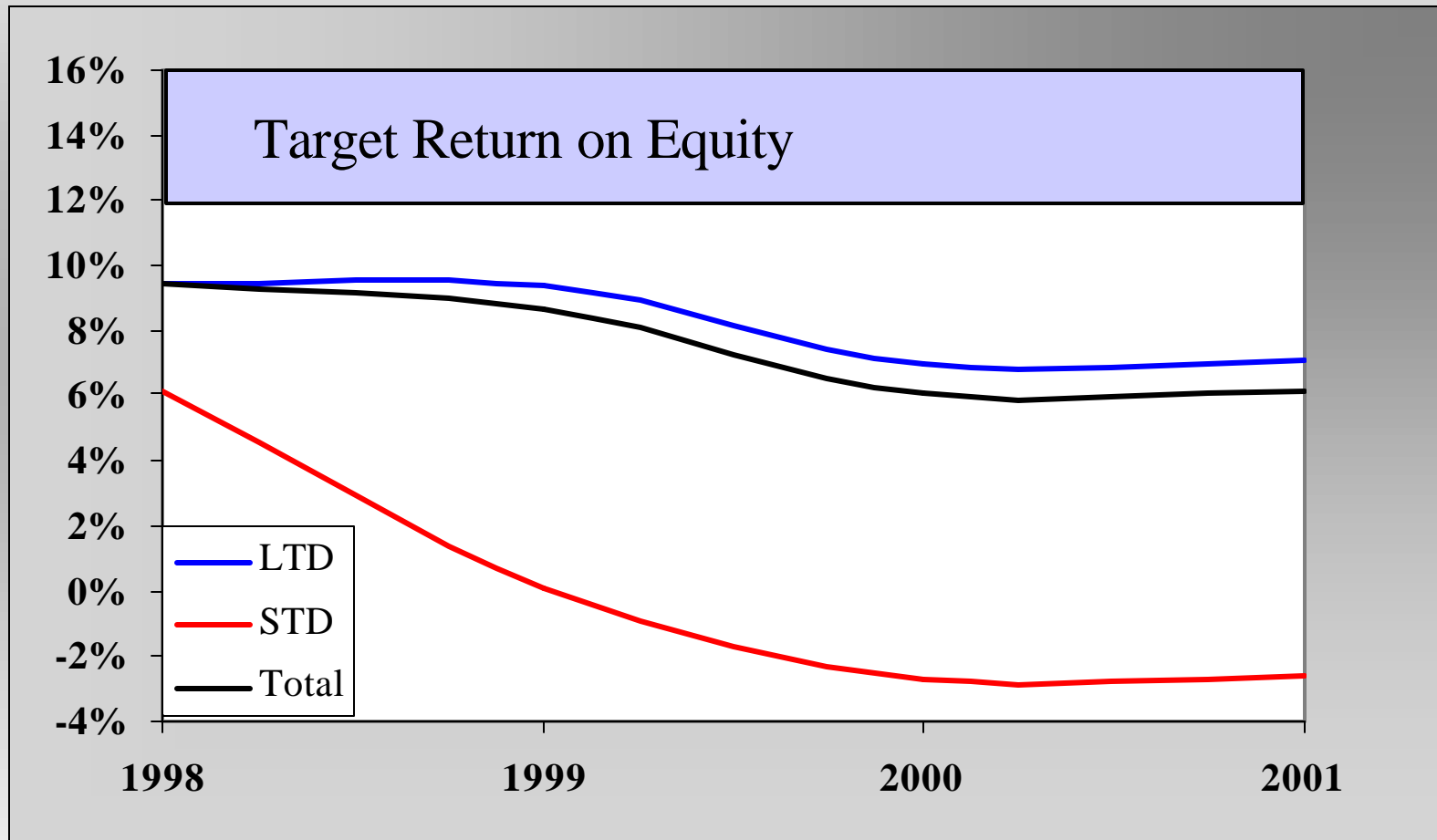


*Profitability Issues in Disability
Insurance*

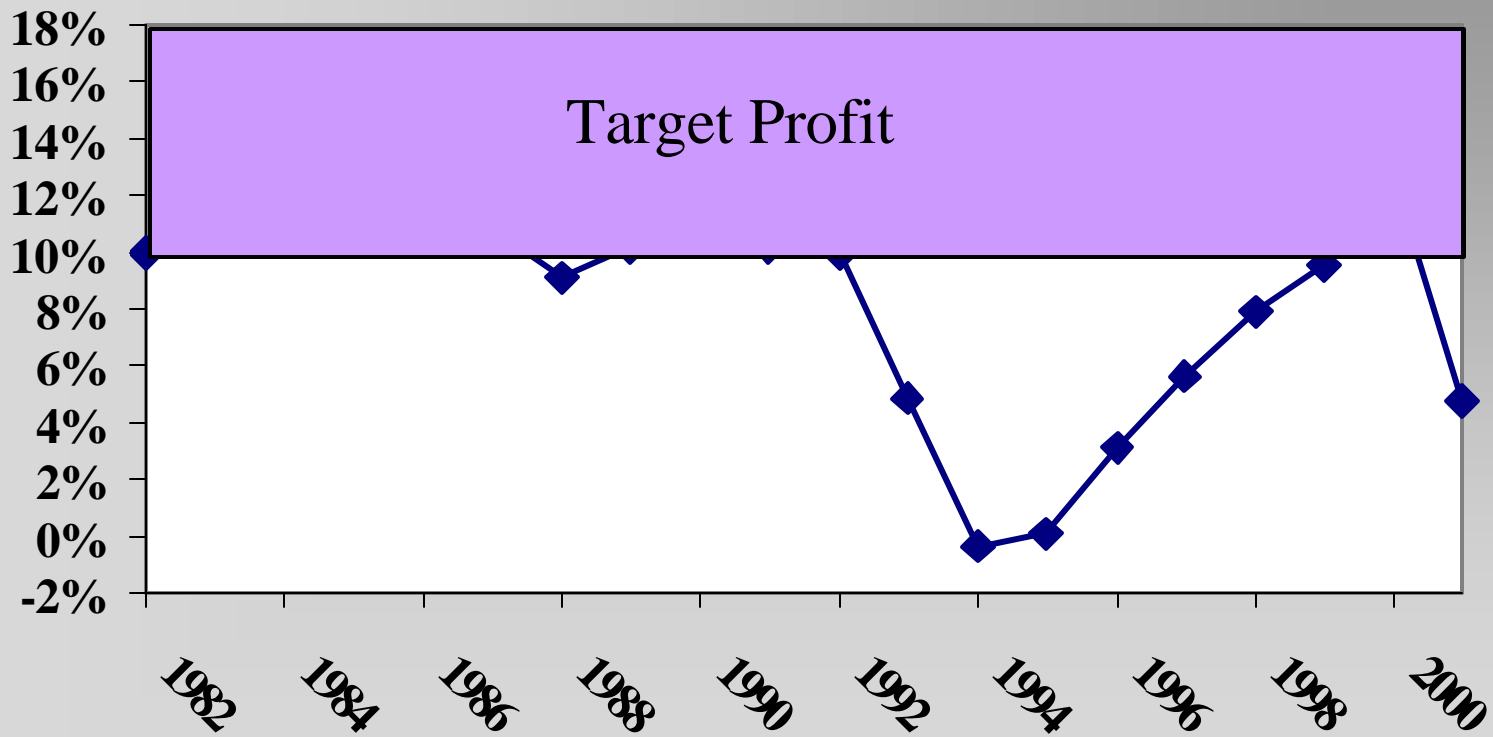
*Rick Leavitt, Smith Group
GUAA Disability Committee Meeting
October 1, 2002*

JHA Profit Study



Disability RMS Profit Survey

LTD Post Tax Profit

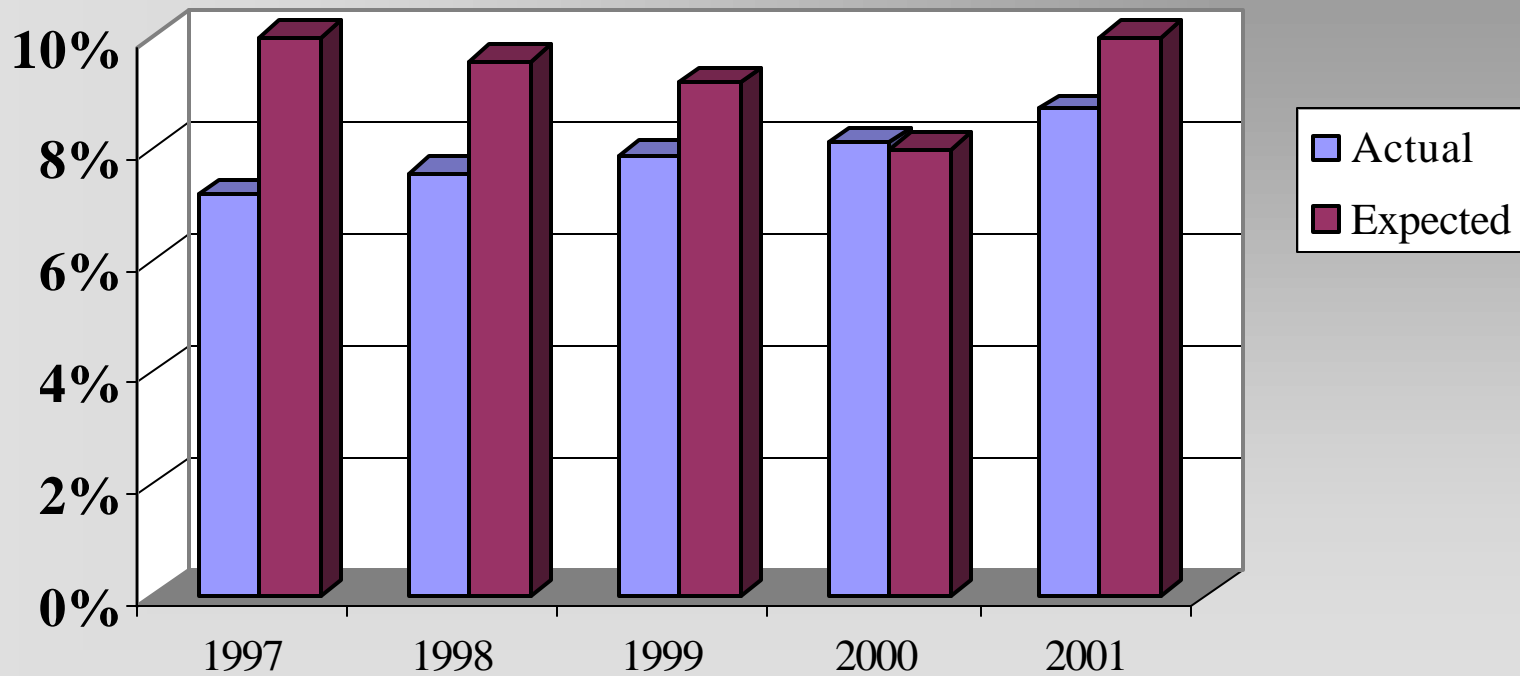


Disability RMS Profit Survey

- ✍ 30% of Companies reported meeting their internal profit target
- ✍ Reported Target margins ranged from 3.4% to 22%
- ✍ 90% of Companies reported recent price increases
- ✍ 50% expect future price increases

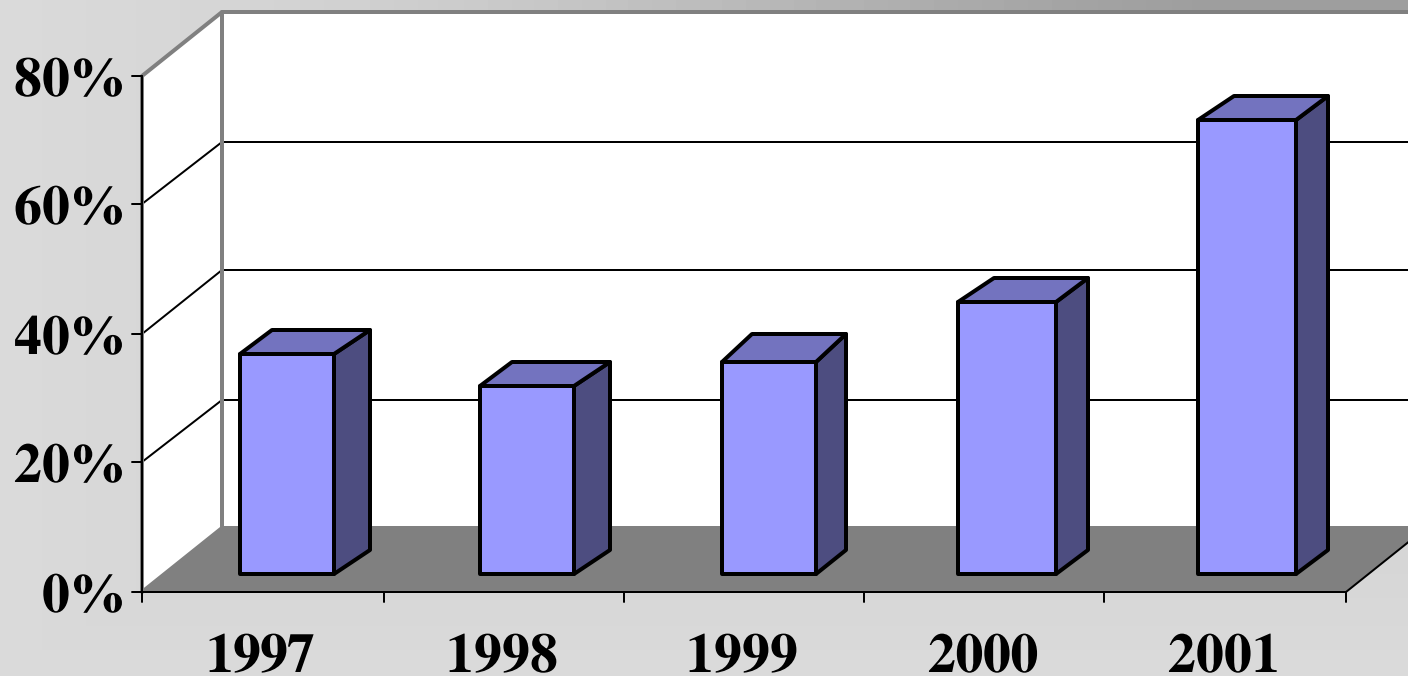
Disability RMS Profit Survey

Trends in Closing Ratios



Disability RMS Profit Survey

% Companies Happy with LTD Close Ratios



*Top Ten Reasons for Lower
than Target Profits*

#10 – Contract Improvements are over valued

What's it Worth?

Maximum Capacity Language	3 to 5%
Prudent Person Language	1 to 2%
60% Gainful definition	3 to 5%
Limits on subjective disabilities	5 to 10%
Mandatory Rehab	3 to 5%
STD Benefits Management	3 to 5%

Total Value: Are these really worth 15 to 30%???

9: Increasing Contrib and Low Participation

Typical Segment Analysis

	Pct Premium	Margin
Non-Contrib	60%	11.7%
Contrib	40%	-5.0%
Total	100%	5.0%

2001 Growth

7% Growth in Traditional LTD inforce premium

22% Growth in Voluntary LTD inforce premium

8: Over reliance on Benefits Management as a profit lever

“Sell it low and let Claims clean up the mess”

Hidden Costs

Increasing ERISA Appeals and litigated claims

Inadequate reserves after low-lying fruit has been picked

Questions

How much is good claims management worth (vs. adequate)?

Are Doctors supportive of sound disability management?

Do Employers want disabled employees back?

7: Sales Rep and UW Inexperience

- ✍ High Turnover... lack of seasoned performers
- ✍ Transition to multi-line underwriters – lack of LTD focus
- ✍ LTD Risk Evaluation is complicated
- ✍ Lack of sound and consistent UW training
- ✍ UW moving out the field

6: Market Stagnation - Churning

Less than 1% Growth in Inforce Employers

2001 New Case Sales 39,787

2001 Change in Inforce Cases 836

Premium Lapse Rate 12%

Broker Survey: Average 5 quotes per case

Why are close rates less than 10%?

5: *External Environment*

✍ Investment Income is down.

5 Yr Corporate AAA bond yield: 3.61%

✍ Economy is anemic... consumer confidence is down

✍ Aging of the work-force

✍ Shrinking of the workforce

✍ Workplace stress at an all-time high

✍ Disability entitlement

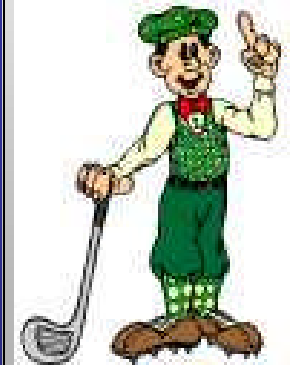
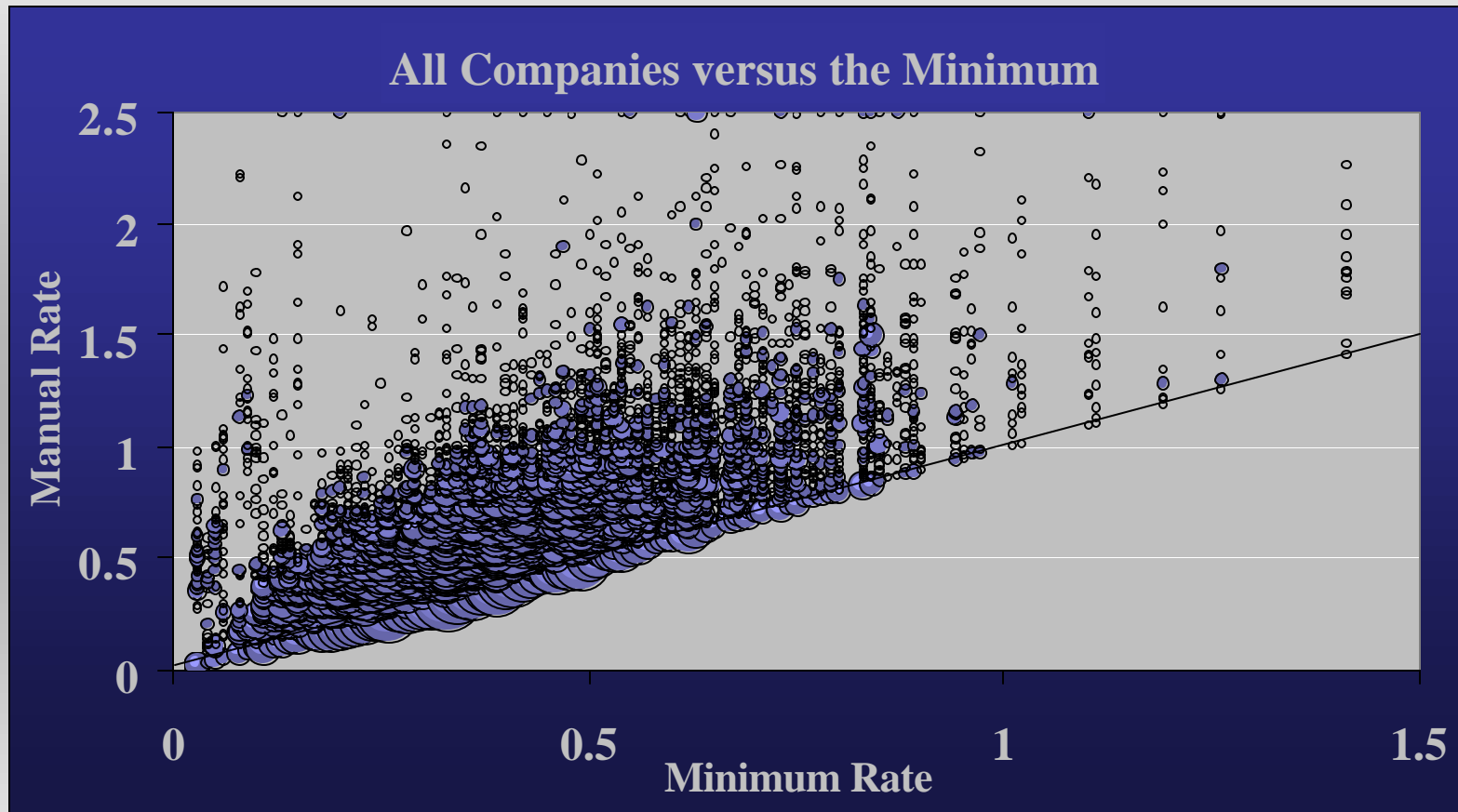
✍ Increased litigation

✍ Increased medical costs means more competition for benefit dollars

4: *Lack of UW and Sales Discipline*

- ✍ What is your Quote to Manual? How enforced?
- ✍ Number One question is still “*Where is the competition?*”
- ✍ The “Business Decision”
 - UW guidelines say “NO”
 - Benefits say “we would never...”
 - UW says looks like a bad call
 - \$\$\$\$ say “Sell it”
- ✍ Can you avoid the stupid decisions???

3: Pricing Volatility



Average Manual Rate: \$0.60

“Best Ball” Manual Rate: \$0.41

2: Acquisition Pricing and the UW Cycle

Inforce Premium per Life:	\$195
New Case Premium per Life:	\$177

Who's Hot and Who's Not?

1: Profit Targets are Too High

1990

AAA 5Yr Corporate Bond Yield	9.5%
LTD Profit Targets	12% to 18%

2002

AAA 5Yr Corporate Bond Yield	3.6%
LTD Profit Targets	12% to 18%

Blame the Stock Analysts!

Other Ideas

- ✍ Reserving Issues: Hard to peg true costs
- ✍ Expenses are too high
- ✍ Brokers too quick to shop the product
- ✍ Lack of information... poor occupation data
- ✍ No Innovative Product Design in 30 years
- ✍ Lack of documented risk evaluation
- ✍ Focus on experience and not on exposure

What else ????