

CHAPTER 3: CODE OF GOOD PRACTICE FOR DISABILITY INSURANCE

Application of this code:

The code is intended as guidelines for best practice. If members follow these guidelines disability business will be written on a sound basis, while still allowing for healthy competition. This will benefit not only insurers but also their clients. Members should thus follow the principles of this code unless a considered decision is made to deviate from the code.

Most of the principles outlined in this code of good practice apply to both group and individual business. However, there are some distinct differences between these types of business, and where sound practice may differ the distinction is made in the code.

Introduction to disability insurance:

Disability insurance is different to death insurance as death is an easily defined event. In many cases of disability there may be a wide range of opinions as to the extent of the insured's disability. ***This highlights the importance of the definition of disability in the policy document.*** An accurate assessment of disability can only be made in terms of the stated definition.

It is not uncommon for a claimant, doctor or employer to consider the claimant "disabled" without reference to the actual definition of "disabled" in the policy. To address these different perceptions requires effective communication between insurers and their clients at point of sale and throughout subsequent processes.

It should be emphasized that the various functions in the insurance of disability are interrelated. Both the claims managers and underwriters need to give input into product design and contract wording. The initial product pricing should be checked regularly by the regular monitoring of claims experience.

The scope of disability insurance:

In normal usage the term "disability insurance" lacks clarity because it can refer to a wide range of insurance benefits that need not necessarily result in occupational disability. Therefore it will be useful to clearly distinguish between two broad categories of disability insurance, which we will call "**Income Replacement**" disability insurance and "**Non Income Replacement**" disability insurance. The distinction between these is:

- Income replacement disability is defined in policy contracts in terms which relate to the insured's inability to follow gainful employment due to health reasons, and compensates him for financial losses caused directly by this inability. The extent to which the insured must be unable to follow his own or any other occupation will be defined in the policy contract. It is not meant to insure against the ability to **find** suitable work. The compensation for loss of income due to occupational disability may take the form of a monthly income or a lump sum payable either as a single payment or as a series of instalments.
- Non-income replacement disability benefits, such as dread disease benefits, are not dependent on the claimant's ability to work or otherwise. Some of these benefits may be restricted to accidental causes only.

The scope of this code of good practice:

This code of good practice mainly focuses on income replacement benefits due to occupational disability.

Broad principles for disability insurance:

Disability insurance involves not only the transfer of risk from the insured to the insurer but also the management of the cost of providing the disability benefits. It is important to identify factors that contribute to increased disability insurance costs and to implement sustainable strategies to contain or manage these risks. An essential strategy is to ensure that the products provided are closely aligned with the real needs, and not only the perceived needs, of the insured individuals.

Also, any such strategies must be consistent with employment practices that are the result of labour legislation affecting people with disabilities. These include the:

- Labour Relations Act
- Employment Equity Act
- COID Act
- Skills Development Act

As the management of claims is such an important factor in the writing of sustainable sound business it is very important that whoever manages the assessment and administration of claims retains a significant share in the risk itself. This ensures that technical aspects, which influence claims experience, are taken into consideration and draws the insurer's attention to the claims trends as they develop.

Where disability insurance is not intended to cover loss of income (i.e. the category described as "Non-income replacement" disability insurance above) particular care should be taken to ensure that the insured benefit is not excessive in relation to the contingencies being covered.

Types of income replacement benefits:

From an insurer's point of view, in general monthly income benefits are preferable to lump sum benefits because:

- Claims assessment is ongoing and benefit payments may be stopped if this is indicated, whereas once a lump sum benefit has been paid, it is irrevocable.
- An insured may be encouraged to claim more readily for a lump sum than for an monthly income benefit because of the apparent value of the lump sum, even though, in reality, its income-generating potential may not be so high.

From the insured's point of view, income benefits match the real need more closely, particularly as lump sum benefits are usually payable on permanent disability only, and not on temporary disability.

However, lump sum benefits may well be more appropriate than income benefits in cases such as key man insurance, business insurance, and cover for mortgages and other loans.

Distribution channels and communication:

The sound underwriting of disability business starts with the intermediary. Too often, disability benefits (particularly capital benefits) are added to a policy as an afterthought. It is therefore important that all intermediaries are properly trained in the appropriateness of the various disability benefits in particular circumstances.

A conscientious intermediary will always perform a full needs analysis for all types life business, to ensure that appropriate advice is given. This is a very good business practice, particularly for disability insurance. It ensures that:

- All the applicant's current cover is taken into account
- That a genuine need for further cover is established (or otherwise). This goes a long way in preventing over insurance.
- The intermediary should ensure that the client fully understands the scope and all the limitations of the insurance being sold.

It is important also that advertising and marketing material gives the right impression of what is covered and what is not covered. Such material must be clear and avoid ambiguity. The same applies to all policy documentation, including application forms and other questionnaires.

Underwriting - Individual Life:

The medical, occupational and financial underwriting of disability business is very important and its emphasis will often differ from that of pure death cover. Factors that are not generally important for life cover may be very important for disability cover (and vice versa). Some examples are a history of back pain or depression or a family history of any disabling condition. It is recommended that application forms be designed to identify these factors, and include such information as income history (over at least three years), level of education, pursuits of a hazardous nature and full details of other disability cover.

When considering other disability cover one can generally ignore cover where the insured is not the beneficiary, such as key man and other business insurance. However, it is important to establish that the insured will not benefit even indirectly. The smaller the business, the more likely it is that there will be some benefit to the insured. It is therefore important that the details of other cover include such business insurance, so that the underwriter can make an informed decision.

A proper description of the occupation is essential. If the applicant's occupation has distinct functions each main function should be described, and an approximate time allocation given. For example, there is a big difference between a self-employed motor mechanic who spends 90% of his time working on cars and 10% doing the books, and one who has employees doing most of the work and so spends 10% of his time working on the cars and 90% in a general administration and supervisory capacity.

Disability claims experience will deteriorate rapidly as the benefit approaches the claimant's earned income.

- For this reason, 100% benefits should be discouraged or only paid for a limited period, i.e. not exceeding 2 years.
- The normal benefit should not exceed 75%. In order to avoid a too high replacement ratio, we recommend a standard benefit as per Appendix A.
- Where lump sum benefits are involved, the equivalent monthly income should be estimated by using the appropriate factors in Appendix B.

Underwriting – Group Benefits:

Factors to consider on scheme level in Group Benefits:

- Scheme size
- Nature of industry
- Geographical location
- Demographics of members
- Occupational risks

Selected individuals will still be underwritten, using principles similar to that used by Individual Life.

Policy provisions:

Besides including many of the factors mentioned earlier, as well as the actual definition of disability, the policy should contain provisions covering the following:

- The claimant should have the initial responsibility of providing medical and other documentary evidence of disability, at his own cost. It is the insured's responsibility to prove that he is disabled in terms of the policy provisions.
- The claimant should be obliged to have whatever medical or other examinations the insurer may reasonably require.
- The claimant could be expected to follow reasonable and appropriate medical advice.
- For individual business the insured person is obliged to advise the insurer of any change in occupation from that described in the application form, and the policy contract should specify how the cover will be affected if the insured becomes unemployed.
- Where the insured does not earn an income, it is recommended that the disability benefit be based on a pre-determined sum assured rather than a benefit calculation that is based on estimated earnings ability.
- The policy should include a provision that encourages early submission of claims. (It is essential to assess disability as close to the date of disability as possible. This is important because useful medical treatment and rehabilitation opportunities may be missed. If the claimant has not been working for an extended period, it becomes difficult to return to work as the

sick role becomes more entrenched while the claimant loses confidence in his ability to work.)

Policy exclusions:

Individual policies could deal with such matters as claims resulting from the insured's unhealthy or dangerous lifestyle (e.g. alcohol abuse) and certain medical conditions (e.g. yuppie flu). Instead of being excluded, many sub-standard conditions can be accepted by imposing longer waiting periods, maximum benefit amounts, maximum benefit periods or premium loadings.

For group benefits, the office may want to generally exclude pre-existing conditions for some period. Exclusion of certain conditions, whether pre-existing or not, can also be a very useful underwriting tool in individual cases.

Finally, for individual business the application form and policy should include a clear warning about the possible repudiation of a claim and cancellation of the policy if the insured is found to have not disclosed some relevant information.

Claims assessment and disability management:

The disability claims processes are critical. On the one hand it needs to identify and decline those claims that are motivated by reasons other than objective disability, e.g. fraud and minor health problems. At the same time the process needs to be efficient and allow empathy with claimants who have significant physical and/or mental problems that render them occupationally disabled.

- The assessment of occupational disability claims requires the ability to gather and explore all the relevant medical and occupational information before making a fair judgement on the validity of a claim. A thorough analytical and decision making process and good communication skills are important tools to reduce contention about the assessment and outcome of disability claims.
- The management of monthly income benefits claims requires sound judgement on the rehabilitation potential of each individual claimant so that the claims can be managed in an appropriate and cost-effective manner.
 - Should Return-to-Work be the aim, the process requires the co-operation of all key stakeholders, i.e. the attending health professionals, employer and claimant. The family of the claimant as well as employee representatives are also important partners in this process.

- Where appropriate, the insurer should encourage additional treatment that may alleviate the claimant's condition and, if indicated, should support and facilitate rehabilitation.

Disability product development and claims practices, as well as disability management need to take cognisance of the relevant legislation on disability issues, e.g. the Employment Equity Act, Labour Relations Act and relevant codes of good practice.

LOA Agreement - Sharing of Claims Costs

A member office may request claims information from another member office. This information shall be limited to:

1. Any claims decision that has already been made on that particular life assured and/or,
2. Any medical information submitted by the claimant and/or,
3. Any medical information obtained at the member office's expense and/or
4. Any other claims information (e.g. investigative reports) obtained at the member office's expense.

For any medical or other claims information obtained at the member office's expense, the requesting office agrees to pay 50% of the costs associated with collecting that information.

Over-insurance and aggregation:

To avoid over insurance it is preferable to act **at the new business stage rather than to reduce benefits at claim stage**. If all offices follow these guidelines it should rarely happen that benefits need to be reduced at claim stage.

The only circumstance in which the above may not generally be true is where the insured becomes covered under a group scheme subsequent to taking out his own disability cover. If possible, any documentation given to the insured when joining a scheme should contain a warning of the possible consequences of over insurance.

If all this fails, claims will have to be reduced at claim stage. All offices involved will share the reduction, and they will follow the maximum benefit of the most lenient of them. It is essential that all offices co-operate in this, and that no office tries to get some marketing advantage by ignoring the dangers of excessive benefits.

The policy document should state clearly the practice that the office will adopt in the event that an aggregated claim benefit exceeds the allowable maximum. The manner of calculation should also be specified.

A capital disability benefit will very often be an acceleration of a death benefit, and in these cases the amount by which the disability claim is reduced will continue as a death benefit and be paid on death.

Where lump sum disability benefits are involved, exceptional extra expenses, such as initial (not ongoing) rehabilitation costs and costs of adaptations to housing and transport can be deducted from the capital amount before finding the capital amount's equivalent income. However, it must be stressed that only additional expenses actually incurred by the insured should be treated like this.

Any benefits arising from claims under what have been called non-income replacement benefits should be taken into account. Once again one can ignore these benefits to the extent that they cover expenses actually incurred by the claimant.

From what goes before it should be clear that it is the total benefit payable from all sources that is important. The insurer should be entitled to receive full information from the claimant about other sources of income and capital payments, either currently or possible payments in the future.

Appendix A

75% of the first R25000 monthly earnings

plus

60% of the next R20000

plus

50% of the balance

with an overall maximum benefit of R50000

Appendix B

The following factors will be used to convert a lump sum benefit to its equivalent monthly income benefit at the underwriting stage:

Up to and including age 50:	120
Over age 50, and up to and including age 55:	100
Over age 55:	100 reduced by 10 for each year over age 55