Medicare Supplement and the Market Opportunity

by Steve Woods, Gen Re, Portland

Wouldn’t it be nice to be in a business selling an insurance product where your potential customer base is going to increase by 10,000 people a day, on average, for the next 16 years? Well, this market exists today, and it is called Medicare Supplement Insurance, or Medigap, or even Med Supp.

In order to fully comprehend the value and opportunity that Medicare Supplement presents, you first need to understand the current Medicare system and the choices that individuals are provided with when they turn age 65. This article will give you an overview of current Medicare options and how a Medicare Supplement policy can provide additional benefits to those who enroll in “Original Medicare.”

Medicare Eligibility

Everyone has heard of Medicare, which is the government-run healthcare plan that is made available to most people age 65 and older, people under 65 with certain disabilities, and people with end-stage renal disease. When an individual becomes eligible for Medicare, he or she is given two options on how to receive coverage. Most people are probably familiar with the traditional Medicare offering which is also referred to as “Original Medicare.” This plan is made up of Part A and Part B. Part A covers inpatient hospital care and some expenses for skilled nursing facilities and is provided to people at no charge, assuming they have paid Medicare taxes while working. Part B covers doctors’ and other healthcare providers’ services, outpatient care and

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I believe that one of the biggest issues facing the life insurance industry is the lack of growth. It is the result of many challenges, such as:

- Low interest rates
- Lack of middle market penetration
- Aging (antiquated?) distribution
- Tax threats

However, there are still many opportunities for growth, and this issue of The Bulletin highlights a few of these.

Our lead article gives an overview of Medicare Supplement. This is a product in high demand by senior citizens, and with the aging of the Baby Boomers it is a great opportunity for growth. While current sales volumes are dominated by a few large players, there is also a lot of room for small to mid-sized carriers to participate, and Gen Re offers the ability for these companies to get into this market on a turn-key basis.

We are also seeing many life insurers trying to grow sales through the use of Living Benefit Riders. Some of these designs have been around for many years, but we are now seeing a number of new twists. Check out Joe Atamaniuk’s article on page 6 for more information.

In my list above, I mention aging (and possibly antiquated) distribution systems as being a barrier to growth. In Stacy Varney’s article on page 8, one of the technology trends she notes is the use of social media to change the way our industry markets to customers. I saw an example of this at the ACLI’s Executive Roundtable in January where one of the keynote speakers was Clara Shih, Chairman and CEO of HearSaySocial.com. HearSay’s focus in the insurance industry is to empower agents to efficiently and successfully use social media to attract prospects, retain customers and grow business.

Happy Spring—growth is in the air. I hope you enjoy this edition of The Bulletin.

Best regards,

Steve Mannik
President
General Re Life Corporation

“Growth is never by mere chance; it is the result of forces working together.”
– James Cash Penney
preventative services. There is a premium for Part B that ranges from $104.90 up to $335.70 per month and is based on an individual’s prior two years of income.

The other option individuals are given is to purchase a Medicare Advantage plan, or Part C. A Medicare Advantage plan is technically still Medicare, but the plans are run by private insurers and may be similar to an HMO or PPO plan. Since private insurers manage these plans, the plans vary and have no standardization. In addition, premiums for a Medicare Advantage plan can be similar to Original Medicare Part B or they can be substantially higher, depending on the benefits that are offered. For the purpose of this article, all you need to know about Medicare Advantage is that it is available as an option when someone becomes eligible for Medicare. If an individual chooses a Medicare Advantage plan over Original Medicare, he or she is not eligible for a Medicare Supplement policy.

The final piece of Medicare is Part D, Prescription Drug Coverage. With original Medicare, Part D is not included but may be purchased for an additional monthly premium. If you purchase a Medicare Advantage plan, the prescription drug coverage may or may not be included. If Part D is not part of your plan you are able to purchase it separately.
**Medicare Supplement Overview**

If a person has chosen the Original Medicare option, he or she is also eligible to purchase a Medicare Supplement plan. Medicare Supplement, Medigap or Med Supp is private health insurance that supplements Original Medicare and helps an individual pay the coinsurance, copayments and/or deductibles not covered by Medicare. Medicare Supplement is regulated by the federal government through the Center for Medicaid and Medicare Services (CMS) and requires insurers to only sell standardized plans, which means they include the same benefits and features, regardless of the company a consumer purchases the coverage through.

Since the coverage is the same from carrier to carrier, cost is the main differentiator. Even though the coverage is standardized, there are 10 different plans from which to choose and that offer differing levels of coverage. This coverage ranges from the basics, Plan A, to covering almost all out of pocket expenses with first dollar coverage, Plan F, which is by far the most popular plan.

**Enrollment Scenarios**

There are three ways an individual can apply for a Medicare Supplement policy. The first is during an open enrollment period that lasts for six months and starts the first day of the month in which the applicant is age 65 and enrolled in Original Medicare Part B. The advantage of applying during the open enrollment period is that applicants are not subject to medical underwriting and cannot receive an adverse underwriting decision because of a pre-existing condition. If an individual applies for Medicare Supplement insurance after the open enrollment period concludes, the insurance carrier to whom he or she is applying can medically underwrite the individual and possibly decline the person for coverage.

In a third enrollment scenario, an individual would be eligible for guaranteed issue, even though he or she is outside of the open enrollment period. This involves moving from a Medicare Advantage plan to a Medicare Supplement plan within a defined period or coming off other, non-Medicare health insurance.

**Value of Medicare Supplement**

As you can see, Medicare Supplement coverage brings significant value to the policyholder. Beyond the obvious direct financial benefits, it allows seniors to budget better for medical costs and avoids the confusion and difficulty of handling complex medical bills. This is especially important for seniors who are on a fixed budget.

As you can imagine, when you have a product that is valued by the consumer, and its consumer base is growing daily by an average of 10,000 people, a product such as Medicare Supplement is sure to gain a lot of attention from the insurance market. It’s hard to miss the advertisements, both on television and in print from AARP (UnitedHealthcare) or Humana—two of the largest carriers selling Medicare Supplement today. However, there are actually 285 carriers currently in the market, with 175 of these carriers selling new business. Throughout 2014, a minimum of 10 new carriers are poised to enter the market and with many more considering entrance.

As popular as this plan is with consumers, and despite the positive, long-range demographic conditions, some concerns and questions are being raised in Washington. We are living in a time where big government programs are being questioned and people are searching for ways to cut the budget as well as raise new revenues. Even though Medicare Supplement is not a government-funded program, some believe that certain Medicare Supplement plans are too rich and the first dollar coverage is inflating the utilization rate of Original Medicare.

In September 2013 the Government Accountability Office (GAO) delivered a report to the Senate outlining its findings on utilization rates of Original Medicare and showing rates both with and without a Medicare Supplement policy in place. In this study, the utilization was significantly higher when a Medicare Supplement policy was in place. These findings, along with other studies, have led to a number of recommendations from legislators in Washington. Some of the most popular are the elimination of first-dollar coverage, introducing cost sharing and taxing Medicare Supplement premiums. The White House has actually taken this one step further in the President’s 2015 budget and included a surcharge on Part B premiums for those that purchase near first-dollar Medicare Supplement coverage.
In Summary
As mentioned previously, the number of people age 65 and older will continue to grow and expand the market for Medicare and Medicare-related products. In 2012 there were 10.5 million people with Medicare Supplement policies. That number is expected to grow to 13 million in 2017 and 16.6 million in 2022. With that level of projected growth and the profitability the product is currently showing, Medicare Supplement should continue to attract new carriers. It seems that the size of the market will support additional carriers; however, when price is the major differentiator, turning Medicare Supplement into a commodity product—and managing to the lowest price in the market—would not be beneficial in the long-term and could negatively impact carriers as well as consumers.

As a leader in the Medicare Supplement reinsurance market, Gen Re is committed to this business. We plan to build on our successes with new and improved capabilities that address the reinsurance needs of carriers in the Medicare Supplement market today and those planning to enter the market in the future.

Endnotes
2,3 The Future of Medicare Supplement, 3rd Annual Market Projection, CSG Actuarial.
Living benefit riders, or accelerated death benefit riders (ABR), have been prevalent in the life insurance arena for many years and as the industry searches for ways to attract new customers, their use has intensified. With increased use comes the need for expanded analysis of their risks versus benefits. Before delving into the design, marketing and current state of these three different types of riders, let’s begin with definitions.

**Terminal Illness Rider**
This rider has been around the industry since the late 1980s. It’s designed to allow policyholders to accelerate a portion, or the entire face amount, of their policies when the insured is diagnosed with a terminal illness with a life expectancy of “X” months, typically 12 or 24. The purpose of this rider is to provide an early payment of the death benefit to assist in medical costs prior to death.

**Critical Illness Rider**
The concept of Critical Illness insurance has been around since the mid-1980s, originating in South Africa. The goal is to provide a benefit to insureds who survive a critical illness event, such as heart attack, cancer, stroke, renal failure or major organ transplant. These events, known as triggers, can include many other ailments than the five mentioned above. This coverage can be issued as a standalone policy, but for our discussion, we address its use as a rider to a life contract. Upon the insured receiving a diagnosis with one of the pre-defined triggers, the insurance company accelerates a portion or the entire face amount of the policy. The amount accelerated often depends upon the severity of the event.

**Chronic Illness Rider**
This is a relatively new rider concept, but the benefit itself has been around for many years in the form of Long Term Care (LTC) insurance. The Chronic Illness rider is a modified version of LTC insurance, which addresses either the insured’s inability to perform activities of daily living (ADL) without assistance from another person, or the insured’s cognitive impairments. ADLs include bathing, continence, dressing, eating, toileting and transferring. If the insured is unable to perform two or more ADLs, he or she would be considered chronically ill and eligible for the benefit. The rider benefit is not dependent on the cost of care, but on a stated figure up to the total face amount of the policy. The payment can be made in a lump sum, annual or monthly installments.

**Benefit Structure Designs**
There are various benefit structure designs for each type of rider.

**Terminal Illness Rider**
There usually is no charge for this rider. It is included on all Individual Life policies issued and many companies offer this rider on in-force policies. Since this acceleration rider is simply a short-term advancement of the death benefit, the discount factor is typically relegated to the time value of money. The company discounts the death benefit at some pre-determined interest rate. If the insurance company defines the terminal illness as greater than, let’s say, 12 months, the company may also factor in the value of lost premium revenue.

**Critical Illness and Chronic Illness Riders**
For both the Critical Illness and Chronic Illness Riders, the calculation of benefits becomes more complex. Three different structures are used to determine the impact of the acceleration related to the face amount of the policy.

1. **The most common structure is a discounted or “no-charge” method.** In this version of the accelerating rider, no additional premium is collected at the time of issue, but if a claim is filed for the benefit, an “actuarial” discounting of the face amount would be applied for the amount being accelerated. In this methodology, the company either re-underwrites the policy or employs a standard industry table to determine the life expectancy of the insured, based upon the severity of the impairment.

   To determine the accelerated amount, typically the company calculates the premium lost due to acceleration and the time value of money for the early benefit payout. For example, if the insured requests to accelerate $50,000, the face amount may be reduced by $80,000 due to this “actuarial” discounting. Since the policy face amount has been reduced, the future required premium would also be reduced as the policy is now smaller.

2. **The second acceleration method is the lien approach.** This could also be classified as an enhanced policy loan. Under this method, the amount accelerated plus interest is held as a lien against the death benefit of the policy. In this design, the policyholder continues to pay the full premium. The cost is the interest associated with the lien. The lien and interest would reduce the
amount of cash value available for surrender or loan as well as the death benefit.

3. The third method charges the policyholder an explicit additional premium at the time the rider is issued. In this calculation, the death benefit is reduced by the amount of the requested acceleration on a one-for-one basis. No actuarial discounting or interest charge is associated with this method.

Each method discussed above references lump sum acceleration payments. However, the Chronic Illness Rider frequently is paid out in monthly installments, with those payments being tax-free, up to a limit stipulated by the Internal Revenue Code (IRC). Anything paid above this amount is treated as ordinary income. For the monthly payouts, IRC 7702B(d)(4) currently stipulates the maximum per diem benefit payable is $320 per day, or $116,800 per year.

The Terminal Illness Rider is usually offered on all policies, whereas the Chronic and Critical Illness Riders are offered on standard or better risks. Often, a supplemental questionnaire is required to assess the additional risk.

In the more common form of the issuance of these riders, the discounted or no-charge method, the riders are added to the base life policy at no additional charge. This “no-charge” rider design has experienced success in marketing to the middle market. The applicant sees this as a way to receive added benefits for no additional cost. This is the case unless the insured files a claim for the benefit.

Some recent statistics show that less than half of the policyholders eligible for the rider benefit claim it. The reasons behind the low claim figures could be the insured’s reluctance to reduce the death benefit of the policy or he or she feels the discounted amount offered is unacceptable.

This is where a potential problem can arise. The original sales illustration presented to the applicant describes that filing a claim for the living benefit would reduce the death benefit in a greater proportion than the amount requested; in reality, however, this fact can be overlooked or misinterpreted. In an instance where the insured disagrees with the discounted offer made by the company, either due to the assessment of the severity of the impairment or the final offer, the dispute could potentially lead to a lawsuit.

In the lien approach, interest is added annually to the amount of lien, which over time could cause this amount to exceed the policy’s death benefit and result in a lapse of coverage.

The additional premium variation of these riders avoids some of the potential problems. The change in policyholder behavior can impact the base policy. It also presents a sales challenge due to the increased cost.

**In Summary**

Living benefit riders are one option for life insurance providers to increase sales, either in existing markets or in the ever-elusive middle markets. These extremely popular riders have various potential risks associated with them—making pricing, underwriting controls and additional analysis necessary to assess the living benefits. These riders have a great potential to successfully serve a broad market, but the risk should carefully be weighed.

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### About the Author

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### More on Life Riders

With a No Cost Rider all costs are handled through a backend charge to policyholders who elect the benefit (i.e., the policyholder is paid the present value of expected death claims, minus present value of missed premiums, and possibly minus a fee). Cathy Bierschbach, Chief Pricing Actuary, Individual Products, wrote an article in 2012 entitled, “A ‘No Cost’ Rider? Really?” To read it, visit genre.com and enter the article title in our search bar.
Trends To Watch in the Life and Health Insurance Industry

by Stacy Varney, Gen Re, Portland

Franklin (Tad) Montross, Chairman, President and CEO at Gen Re, recently wrote an article entitled “The Playing Field” (published in March 2014). In this article Tad talked about several key trends that impacted the Property & Casualty and Life & Health industries in 2013 and are expected to continue to do so in 2014. Tad references some specific Life & Health trends that our experts are monitoring and that you can learn more about below.

Aging
The demographic shift we are experiencing in the U.S. is having a huge impact on the demand for our products and services. Today about 12% of our population is over the age of 65. By 2050 that number will be 20%. Aging not only has an effect on medical and other benefit costs but also on consumer spending, and is a significant factor in the pricing of our products. Jena Breece, Pricing Actuary for Group & Specialty Products, wrote an article in the last Bulletin publication entitled “Aging and Interest Rates—The Impact on Long Term Disability Profit.”

Technology
Advancements in technology have improved many aspects of our daily lives as well as our business environment. Social media and mobility have changed the way we market and interact with customers and each other. However, technology has also brought new challenges to our businesses, including cyber crimes. Read more about cyber crimes targeting healthcare delivery systems.

Decision Analytics
Also referred to as predictive analytics or data mining, decision analytics has become prevalent in the insurance business. We create 2.5 quintillion bytes of data every day; 90% of the world’s data has been generated in just the past two years. In 2020 there will be 35 zettabytes of shared data. To give you an idea of how large this is, one zettabyte equates to the same volume as the entire Great Wall of China. Companies are hoping to mine this data to better understand their clients’ needs and better underwrite risks. Gen Re recently conducted a survey on this subject called the “Predictive Modeling Industry Survey” to life insurers. You can read our Summary Report.

Regulatory Environment
In addition to state versus federal regulations, our industry is now challenged with global regulations and financial reporting. Risk management practices and non-insurance company entities, such as banks, will impact the competitive landscape and compliance issues of our industry. Our research into the ERM Practices of Life & Health insurers provided insights into how companies have prepared for the changing regulatory environment in which we operate. See our recent blog post on this topic.

On behalf of my colleagues at Gen Re, we look forward to helping you and your company address these and other risk management issues—and if you haven’t read Tad’s thought-provoking article, I encourage you to do so. Read Now.

About the Author
Stacy Varney is Vice President, Marketing and Account Management and is responsible for the leadership of client account management and new business development for Group LTD, Group Life and AD&D, Individual Disability and Medicare Supplement products. She can be reached at 207 347 4612 or stacy.varney@genre.com.
Below is a summary of the Life, Disability and Health industry and consortium surveys the Gen Re Research Center is releasing in the first half of 2014. Surveys are listed by category and in the order of publication date.

Full reports are available only to participating companies. Some market surveys have short report summaries on genre.com.

If you would like to learn more about our Research Center, or about participating in any of these surveys, please contact Marcy Updike at mupdike@genre.com.

Industry Surveys

2014 U.S. Group Disability & Group Term Life Market Survey
This survey tracks new sales and inforce results for 2013 Total Group (Traditional/Basic and Employee-Paid combined) for LTD, STD, Term Life and AD&D. The report includes an in-depth business analysis focusing on metrics such as client growth, premium per life, and the percent of employee-paid business. Additional analysis captures industry lapse and renewal rates for LTD and Term Life. The full report is available to participating companies only. A short summary is provided on our website.

Release Date: April 2014

2014 U.S. Individual Disability Income Market Survey
This survey tracks 2013 sales and in-force results for Guaranteed Renewable (GR), Non-Cancelable (Non-Can), Buy-Sell and Guaranteed Standard Issue (GSI) products. The final report details growth trends and also includes premium per policy and benefit amount per policy. The full report is available to participating companies only. A short summary is provided on our website.

Release Date: April 2014

2013 U.S. Group Term Life Profit Study
This study provides an assessment of the profitability of Group Term Life for 2013. Analysis in this survey explores the relationship between expenses, NII, earned premium and incurred loss ratios. The final report shows aggregate industry results. Individual company results are kept confidential. The full report is available to participating companies only.

Release Date: May 2014

2013 U.S. Group Disability Profit Study
This study provides an assessment of the profitability for LTD and STD products, and explores the relationship between expenses, NII, earned premium and incurred loss ratios. The final report shows aggregate industry results for 2013. Individual company results are kept confidential. The full report is available to participating companies only.

Release Date: May 2014

U.S. Medicare Supplement Market Survey
This survey tracks the overall size of the Medicare Supplement market for 2013, as well as which products are being marketed and to whom related sales efforts are being directed. In addition this survey covers key performance metrics such as lapse rates and claim trends. Results of the survey will be shown in aggregate to ensure participating company responses are kept confidential. The full report is available to participating companies only.

Release Date: May 2014
People News

> Keith Brown joined Gen Re as Chief Life Underwriter and Vice President, Risk Management for Individual Products.

> John Najarian, Chief Underwriter, has recently been named Vice President, Underwriting Research & Development for Group & Specialty Products.

> Jennifer Daigle has assumed leadership of the Group & Specialty division’s underwriting department as Vice President, Underwriting.

> Joshua Wolf joined the Individual Life pricing team in October 2013.

> Joe Iannetti, Senior Underwriter and Second Vice President, was named Group Life Committee Co-Chair for the GUAA Conference to be held in San Francisco May 18–22.

> John Palascak joined the Pricing team for Group & Specialty Products.

> Andrew Jenkins, AVP, Actuary, has received his FSA designation and joined the SOA Group Life Experience Committee. Jena Breece, Pricing Actuary and Second Vice President for Group & Specialty Products, has joined the Group Disability Experience Committee. Cathy Bierschbach, Chief Pricing Actuary for Individual Products, is on the Reinsurance Section Council for the SOA.

To discuss how Gen Re can help you with your reinsurance needs, please contact one of our marketing heads:

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> Marcy Updike, VP, Market Research, has joined the New England Market Research Board.

External Articles

> The September 2013 edition of On The Risk magazine contained articles by Joan Timpano, Individual Life Underwriter and Assistant Vice President, who wrote “Risk Assessment of Crohn Disease,” and Laura Vecchione, Medical Director and Second Vice President, who wrote on “Peripheral Artery Disease.” Both of these articles are available to read on genre.com.

> Jena Breece, Pricing Actuary and Second Vice President for Group & Specialty Products, wrote an article published in Best’s Review December 2013 edition called “Hitting the Mark.” The article discussed how long term disability writers need to incorporate workforce aging and low interest rates into their pricing.

Industry Events

> Sally Dodge, Claims Manager, spoke last October at the International Claim Association Annual Meeting in Chicago on “The Lead Dancer—The Claims Analyst’s ‘Dance Space.’”

> Steve Woods, Senior Account Executive, spoke at the Southeastern Actuaries Conference Fall Meeting last November in Atlanta on the topic of “Voluntary Worksite Perspectives.” At the same meeting, Steve Rowley, Senior Account Executive, spoke on “Living Benefit Riders and Specialty Health Products Around the World.”

> Adela de Loizaga Carney, Medical Director, spoke last October at the Northeast Home Office Underwriters Meeting in Leominster, Massachusetts on “Mitral Valve Disorders—Echocardiography Findings and Assessment.”

> At the Texas Wide Underwriting Conference in San Antonio last October, Michael Clift, Underwriting Manager, spoke on “The Mountain Climbing Risk,” and Cecil Ramotar, Senior Medical Underwriting Specialist, spoke on “Auto Racing.”