The Ingredients Needed to Perfect the GSI Recipe in the Lloyd's Market

By Laura Muka

Thirty years ago, when you baked a cake for a kid's birthday party, it was most likely from a box – just add oil, water, and maybe an egg. No heavy lifting required. But times, and people, have changed.

Today, the kid's birthday cake is now "pastry," and the recipe calls for eggs from cage-free chickens, oat flour, and ultra-filtered coconut oil – plus several substitutes and adjustments. In today's evolving marketplace, insurance can no longer just be from a box. Advisors need to make sure they can alter the ingredients in the recipe to fit their client's tastes.

For highly compensated professionals, one of the top items on today's insurance menu is high limit disability Guaranteed Standard Issue Plans, also known as GSI.

GSI is a process where underwriters utilize a conventional high limit disability product but create a program that allows it to be underwritten and distributed through the institutional buying power of a large corporation or partnership; typically, by asking very limited eligibility questions while not requiring medical evidence of insurability. Benefit departments of these companies often recognize that the highly compensated key employees of their firms are underinsured by the benefits offered in their basic group plan and, if available, any domestic supplemental individual disability insurance (IDI) program and seek to equalize benefits to help fill the gap for these key team members.

In the high limit disability space, the Lloyd's of London GSI market has been rapidly growing over the past decade, with a growth rate that far surpassed its fully underwritten brethren. By comparison, supplemental IDI coverage has existed for over 30 years in the domestic U.S. market and the recipe has been perfected throughout the years as the demand has grown to create a profitable market. And like the domestic market, the Lloyd's GSI market, though still in its infancy in the insurance world, is gaining experience by recognizing that adjustments will need to be made to create a sustainable and profitable market.

There are four key ingredients to a sustainable GSI disability product for the Lloyd's market:

1. **Pricing**
2. **Benefit Maximums**
3. **Contract Terms**
4. **Claims**

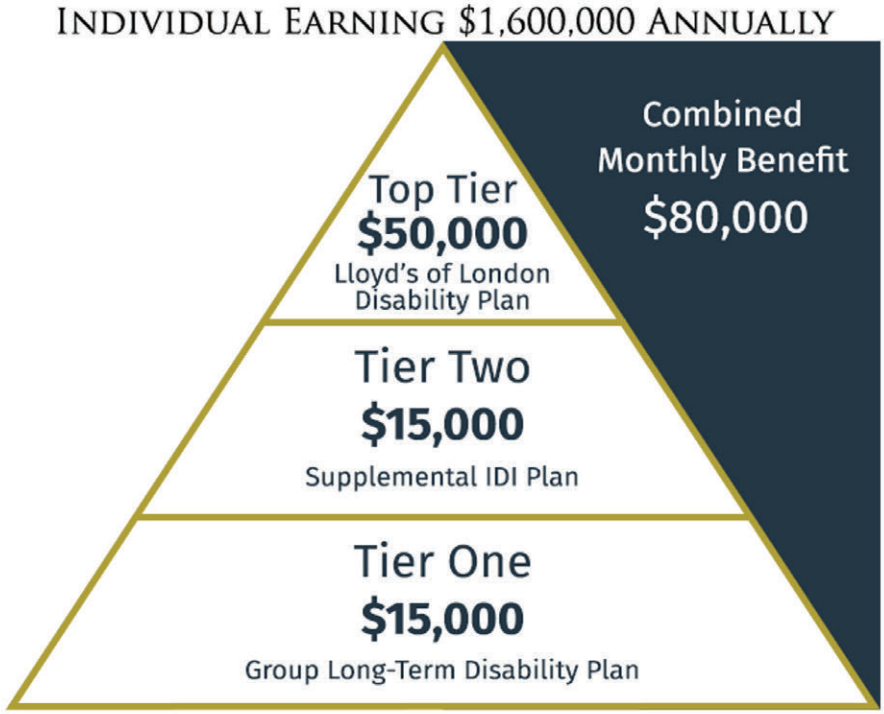
Getting the balance of these components, as well as other related variables, right over the years is what has driven some of the biggest U.S. disability providers in the country to write more GSI business than fully underwritten business. They realize that if the formula is right, they can save on underwriting costs (i.e., no expensive medical exams and lab tests) and collect premium for multiple lives under one list premium bill.

Lloyd's of London Coverholders have adopted this same model to make additional benefits available over and above what can be underwritten in the domestic market. Here's an example:

A large Boston based consulting firm currently has a Group Plan that covers 60% of an employee's income up to $15,000 per month of disability benefits – this covers up to $300,000 of income. They also have in place a domestic IDI plan that covers 60% of income up to an additional $15,000 per month for those consultants earning in excess of $300,000. The combination of these two plans covers all consultants earning up to $600,000 annually. With over 50 consultants earning between $600,000 and $1,600,000 annually, their biggest rainmakers were in many cases woefully underinsured by their existing plan. To equalize the benefit shortfall and provide a similar plan design to the rank and file, a third layer of protection was installed with Lloyd's to dramatically enhance the plan for the top paid consultants.

Pricing

Pricing must be acceptable to the buyer based on the perceived risk and in reasonable line with the cost of domestic IDI. From the market/carrier side, enough properly underwritten coverage must be placed to pay claims and administrative



expenses — yet still have enough left over to deliver a reasonable underwriting profit. Initially, a Lloyd's premium may have been less than what was offered in the domestic market, based on the facts that the Lloyd's product had a shorter policy term and can come with a pre-existing conditions limitation. However, our consulting firm example highlights a key difference between the Lloyd's GSI market and the Domestic GSI market, mainly that the domestic market will always have more lives to cover. They will be covering the employees earning between $300,000 and $600,000, as well as those earning north of $600,000. In most organizations, there will be far more in this group than in the group earning in excess of $600,000.

It's important to remember that in the domestic market, retail pricing is discounted in the GSI program based on the number of lives, clearly a factor that goes into the rate development for a Lloyd's GSI program.

Lloyd's contracts will need to adjust premiums to recognize that its plans will include fewer participants and may require more premium to create enough volume to support the cost of sustaining the programs over time.

Benefit Maximums

An IDI plan will typically not exceed $15,000 of monthly benefit. If a claim is paid, it will pay that benefit for the benefit period, which can be either to age 65 or 67.

However, Lloyd's benefits are structured differently and are issued as a 60- or 120-month benefit and can be followed by a lump sum that is paid at the conclusion of the monthly benefits. Since their inception, Lloyd's GSI benefits have reached what can be defined as irrationally exuberant levels. As an advisor, be wary of new plans that offer monthly benefits of $100,000-plus and lump sum benefits up to $10,000,000. This is an area that will require significant course correction.

It is inconceivable that a market can support the premium required to pay and then reserve enough to sustain even one claim that could result in a payout of $22,000,000-plus. Plans are being modified at renewal to bring them into a more sustainable position.

Contract Terms

A typical contract term for a domestic IDI plan would be to age 67. That means that unless the policy owner cancels or fails to pay the premium, the IDI policy will continue until the individual reaches age 67 without any premium change unless the benefit amount changes.

Lloyd's prohibits contract terms longer than five years (less one day). So, to continue coverage the contract must be renewed at the end of the contract term. This will typically result in premium increase because the participant is five years older.

If the experience is less than expected, the Lloyd's provider can change the contract terms, e.g., increase the rate, shorten the benefit period, or reduce the maximum GSI benefit. In the most extreme cases, the provider can decide not to renew the contract at all.

Because claims experience has been higher than anticipated, there has been a shift in the market whereby contract terms are being held to shorter terms, especially in voluntary plan designs. We expect these changes will continue to evolve as the market seeks profitability and sustainability. At this juncture, the business is either too immature or being adjusted to reflect normalized claims experience.

Claims

Claims are to be expected. However, the claims cannot outpace the cost of providing the benefit. As previously mentioned, there must be enough premium collected to cover the claims, administrative costs and still leave room for underwriters of this class to make a profit.

So what is the right recipe? The answer may be changes to all the ingredients in a short period of time to be sure the Lloyd's GSI market can experience the same success as the domestic market in the U.S. Your best clients have become foodies when it comes to determining their insurance needs, and they entrust you, The Master Pastry Chef, to know what it will take to satisfy their palate. Make sure you get that five-star rating. IJ

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