PRINCIPLES OF RISK MANAGEMENT AND INSURANCE

CLASS NOTES

Chapter 20 Individual Health Insurance Coverages

Topics

- Health Care Problems in the US/Rwanda
- Individual Health Insurance Coverages
- Hospital-Surgical Insurance
- Major Medical Insurance
- Health Savings Accounts
- Long-term Care Insurance
- Disability-Income Insurance
- Individual Medical Expense Contractual Provisions
- Shopping for Health Insurance

Health Care Problems

- Problem 1: Rising Health Care Expenditures
  - Health care expenditures in the US have increased substantially over time and are outstripping the growth in the economy
  - Group health insurance premiums are rising faster than the rate of inflation
  - Factors affecting health care costs include:
    - Rising outpatient and inpatient costs
    - Rising cost of prescription drugs
    - Rising cost of physician services
- Problem 2: Many people do not have health insurance coverage
  - Groups with large number of uninsured include:
    - Foreign born
    - Hispanics, Blacks, and Asians
    - Young adults
    - Low income households
  - Many people are uninsured because the coverage is not affordable
  - Some people are denied coverage, or do not believe health insurance is needed
  - Many low income people who are eligible for Medicaid are not aware they are eligible
- Problem 3: Uneven Quality of Medical Care
  - The quality of medical care varies widely
  - There is a "quality gap" in the US; many people do not receive the most effective care
  - Many doctors are not following the recommended guidelines in treating common ailments
- Problem 4: Waste and Inefficiency

- The administrative costs of delivering health insurance benefits are excessively high

Individual Health Insurance Coverages

- Individual medical expense plans are purchased by:
  - People who are not employed
  - Retired workers
  - College students
- Common forms of individual coverage include:
  - Hospital-surgical insurance
  - Major medical insurance
  - Health savings accounts
  - Long-term care insurance
  - Disability-income insurance

Hospital-Surgical Insurance

- Hospital-surgical insurance plans cover routine medical expenses
  - Not designed to cover catastrophic losses
  - Maximum benefits per illness and lifetime aggregate limits are low
  - Most policies cover:
    - Hospital inpatient expenses
    - Miscellaneous hospital expenses, e.g., x-rays
    - Surgical expenses, covered two ways:
      - A scheduled approach, with a maximum per procedure
      - On the basis of reasonable and customary charges
    - Outpatient services, e.g., emergency treatment
    - Physicians' visits for nonsurgical treatment
  - These plans are not widely used

Major Medical Insurance

- Major medical insurance is designed to pay a high proportion of the covered expenses of a catastrophic illness or injury
- Plans are characterized by:
  - Broad coverage of reasonable medical expenses
  - High maximum limits
  - A benefit period, or length of time for which benefits are paid after a deductible is satisfied
  - A deductible (typically calendar year)
    - A calendar-year deductible is an aggregate deductible that has to be satisfied only once during the calendar year
    - A family deductible specifies that medical expenses for all family members are accumulated to satisfy the deductible
    - Under a common-accident provision, only one deductible has to be satisfied if two or more family members are injured in a common accident
  - A coinsurance provision requires the insured to pay a certain percentage (typically 20-25 %) of eligible medical expenses in excess of the deductible

        - Purpose is to reduce premiums and prevent overutilization of policy benefits
    - The insured's total out-of-pocket spending is limited by a stop-loss limit, after which the insurer pays 100% of eligible expenses
    - Common exclusions include cosmetic surgery and expenses covered by workers compensation
    - Plans may have internal limits for some types of expenses
    - Some plans have incorporated elements of managed care

Health Savings Accounts

- A health savings account (HSA) is a tax exempt account established exclusively for the purpose of paying qualified medical expenses
    - The beneficiary must be covered under a high-deductible health plan to cover catastrophic medical bills
    - The account holder can withdraw money from the HSA tax-free for medical costs
    - Contributions and annual out-of-pocket expenses are subject to maximum limits
    - An HSA investment account in a qualified plan received favorable tax treatment
        - Participants pay premiums with before-tax dollars
        - Investment earnings accumulate tax-free
    - Proponents argue that HSAs can help keep health care costs down because consumers will be more sensitive to costs, will avoid unnecessary services, and will shop around
    - Critics argue that HSAs will encourage insureds to forego preventative care

Long Term Care Insurance

    - In a qualified plan, a benefit trigger must be met to receive benefits. Either,
        - The insured is unable to perform a certain number of activities of daily living (ADLs), or
        - The insured needs substantial supervision to be protected against threats to health and safety because of a severe cognitive impairment
    - Since inflation can erode the real purchasing power of the daily benefit, some plans offer automatic benefit increases
    - Policies are guaranteed renewable
    - Coverage is expensive
    - Most insurers offer optional nonforfeiture benefits, which provide benefits if the insured lapses the policy
        - Under a return of premium benefit, the policyholder receives a cash payment
        - Under a shortened benefit period option, coverage continues but the benefit period or maximum dollar amount is reduced
    - Long-term insurance that meets certain requirements receives favorable income tax treatment
        - Premiums are deductible under certain conditions

- Per diem benefits are subject to daily limits

Disability-Income Insurance

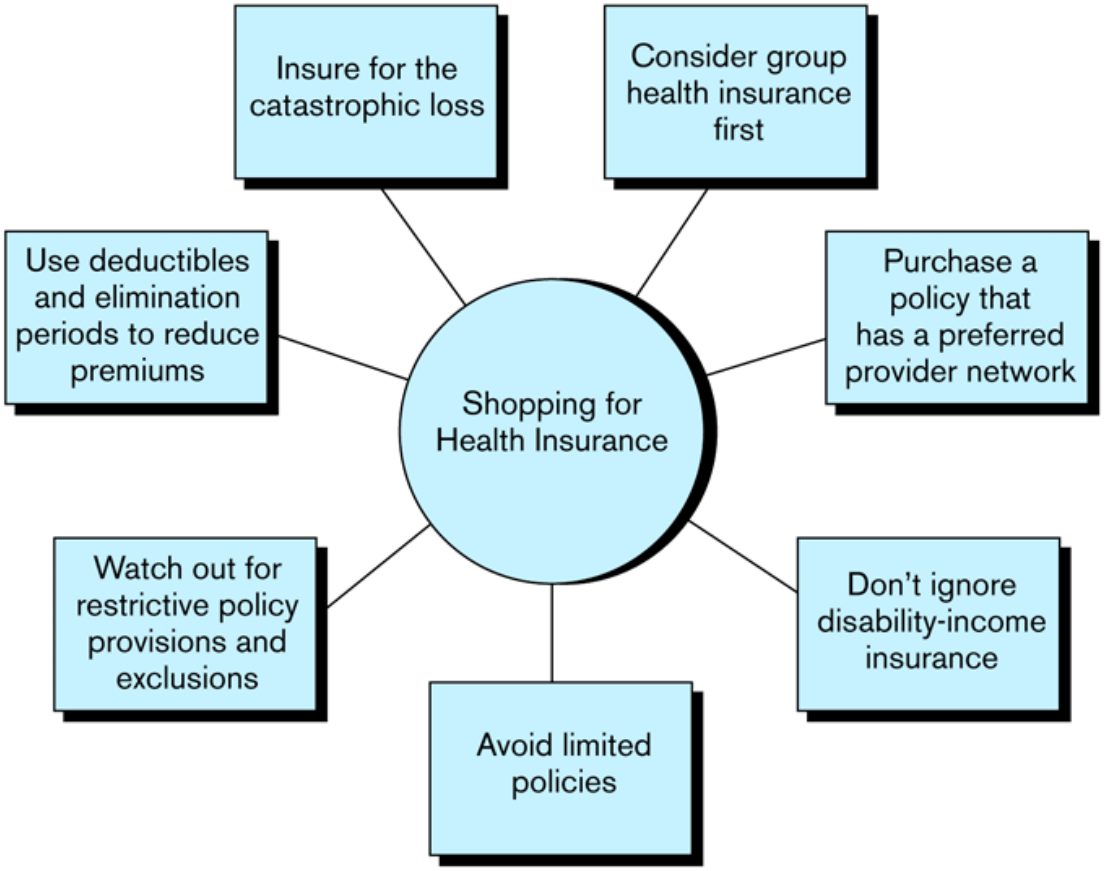
- The financial impact of total disability on present savings, assets, and ability to earn an income can be devastating
- Disability-income insurance provides income payments when the insured is unable to work because of sickness or injury
  - Income payments are typically limited to 60-80% of gross earnings
- The four most common definitions of total disability are:
  - Inability to perform all duties of the insured's occupation
  - Inability to perform the duties of any occupation for which the insured is reasonably fitted by education, training, and experience
  - Inability to perform the duties of any gainful occupation
  - Loss-of-income test, i.e., your income is reduced as a result of sickness or accident
  - Most insurers use a combination of 1 & 2
  - Partial disability is defined as the inability of the insured to perform one or more important duties of his or her occupation
  - Some policies offer partial disability benefits
    - Usually, partial disability benefits must follow total disability
    - The partial disability benefits are paid at a reduced rate for a shorter period
  - Residual disability means a pro rata disability benefit is paid to an insured whose earned income is reduced because of an accident or sickness
    - The typical provision has a time and duties test that considers both income and occupation
  - The benefit period is the length of time that disability payments are payable after the elimination period is met
    - Most disabilities have durations of less than two years
  - Individual policies normally contain an elimination period, during which time benefits are not paid
    - The typical elimination period is 30 days
  - A waiver-of-premium provision allows for future premiums to be waived as long as the insured remains disabled
  - Policies typically include a rehabilitation provision

Individual Medical Expense Contractual Provisions

- Some common contractual provisions address the renewability of the policy
  - Under an optionally renewable policy, the insurer has the right to terminate a policy on any anniversary date
  - A "nonrenewable for stated reasons only" provision allows the insurer to terminate coverage only for certain reasons
  - A guaranteed renewable policy is one in which the insurer guarantees to renew the policy to some stated age
    - Premiums can be increased for the underwriting class

  - Under a noncancellable policy, the insurer guarantees renewal of the policy to some stated age
    - Premiums cannot be increased during that period
- To control adverse selection, individual policies usually contain some type of preexisting-conditions clause
  - The clause limits coverage for a physical or mental condition for which the insured received treatment prior to the effective date of the policy
  - Some states limit these exclusion periods, e.g., for 12 months
- Some contractual provisions address claims:
  - Under a notice of claims provision, the insured must give written notice to the insurer within 20 days after a covered loss occurs
  - Under a claim forms provision, the insurer is required to send the insured a claim form within 15 days
  - Under the proof-of-loss provision, the insured must send written proof of loss to the insurer within 90 days
- The grace period is a 31-day period after the premium due date to pay an overdue premium
- The reinstatement provision permits the insured to reinstate a lapsed policy, subject to payment of premiums and a 10-day waiting period for sickness
- The time limit on certain defenses states that after the policy has been in force for two years, the insurer cannot void the policy or deny a claim on the basis of misstatements in the application, except for fraudulent misstatements

Guidelines for Health Insurance Shoppers



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