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Voluntary Benefits

A Strategy for Capturing the Underserved Middle Market

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Can life insurers regain the lost middle market?

A 2010 LIMRA survey[1] revealed that life insurance ownership in the US was at its lowest point in 50 years. In 2011 LIMRA also reported that only 59 percent of adults owned either an individual or a group life policy, down from 70 percent in 1960[2]. This is despite the fact that 40 percent of LIMRA's survey respondents said they would have trouble meeting their basic living expenses if a primary wage earner in their household passed away. Astonishingly, all of this comes at a time when the cost of life insurance is at an all-time low.

Nowhere has this been more pronounced than in the middle market, defined as the 52 million households with annual incomes between $35,000 and $100,000[3]. Only 44 percent, or 23 million households, have life insurance[4]. This level of ownership is so low that even small improvements in insurers' effectiveness in this sector would yield significant returns. Yet, despite all of the debate and attention focused on this issue over many years, little progress has been made by the industry.

To be fair, middle-market formation has been slowing, discretionary income has been squeezed, and alternatives to life insurance as a saving vehicle have emerged. But, as life insurers grappled with the high cost of distribution and underwriting, they were forced to focus on the mass affluent and affluent markets, leaving the middle market underserved. Compounding the problem, in the '60s it used to be easy to find a life insurance agent, but today they are fewer and farther between.

Can life insurers recapture this lost ground? To date, most agent-driven, traditional carriers have not undertaken the top-to-bottom value chain realignment required to reach middle-market consumers efficiently and effectively. Nor have they developed products purpose-built for both the unique needs and more limited spending power of the middle market. Yet, some insurers are winning in this market – insurers like Aflac, Torchmark and Colonial Life, to name a few. For these carriers the workplace represents all if not most of their new sales. Why the workplace? As the oft-quoted bank robber, Willie Sutton, might have said: because that's where the middle market is!

With its lower distribution costs, the workplace is becoming increasingly compelling as a channel for reaching middle-market consumers. Notwithstanding the success of companies like those mentioned above that sell primarily through small businesses, the market is still in its infancy. Underscoring this opportunity, 80 percent of employees rate the workplace as a "very important" or "somewhat important" source of personal insurance and savings products[5]. And 75 percent of those who shop for life insurance in the workplace ultimately decide to buy[6].

In this report we will explore the marketplace that's come to be known as "voluntary benefits" – protection products bought by employees through the workplace at their expense. We'll look at the dynamics unique to this marketplace, what's on the horizon, and what it will take for life insurers to win.

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40
41

The Current Situation

Voluntary benefits is growing in importance. For employers, it's an easy way to enhance the company's benefits program without adding to their cost or unduly to their administrative burden. For employees, who are now part of a workforce that is increasingly diverse and multi-generational, the workplace is cited as a convenient, and often less costly, venue for fulfilling more of their financial needs. For life carriers, it is indeed becoming a strategy for capturing the underserved middle market and, notably, for growing sales of less capital-intensive protection products. For healthcare carriers, voluntary benefits is a source of new revenue at higher margins since it escapes the minimum loss ratio requirements of the Affordable Care Act (ACA). Benefit brokers, too, believe voluntary benefits sales will help them make up for the adverse effect of healthcare reform on their businesses.

A recent MetLife study[7] reinforced the increasing relevance of voluntary benefits. In 2012, 58 percent of employers made voluntary benefits a significant benefits strategy, up from 32 percent in 2010. The strongest growth was in smaller companies. In the same study, nearly 75 percent of employees said they value the ability to buy voluntary benefits at work. What's more, offering a variety of voluntary benefits doubled the power of the program to drive employee loyalty when compared to a program offering less choice.

Except for a handful of larger carriers, the voluntary benefits industry is very fragmented and sub-scale. Eastbridge Consulting's U.S. Worksite/ Voluntary 2012 Sales Report includes data on 65 competitors. In addition to life and healthcare carriers, the value chain includes distributors, service providers/TPAs, enrollment firms, and payroll companies.

With the passage of the ACA, healthcare carriers have become more focused on voluntary benefits. They have the potential of being formidable competitors. They see voluntary benefits as a natural and attractive adjacency, and are in a strong position to leverage their share-of-wallet with benefit brokers. They also have pricing and bundling advantages that the traditional voluntary benefits players do not. In fact, a majority of states require consumers to have medical coverage before they can apply for supplemental health benefits on a voluntary basis – further strengthening healthcare insurers' hand. Some healthcare carriers offer employers a discount on medical care coverage if their voluntary benefits are provided to employees.

The ACA and growing healthcare consumerism have caused healthcare insurers to quickly move to a B2C model and away from the time-honored employee benefits B2B model. As a result, their rapidly developing consumer marketing skills, powerful brands, single enrollment platform, consolidated billing, and scale make healthcare companies a disruptive force in the voluntary benefits marketplace.

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Market Dynamics

First, some basic facts. Voluntary benefits sales totaled $6.03 billion in 2012 and $5.48 billion in 2011[8] – an increase of 10 percent – in an environment of high unemployment. Group voluntary product sales represented 56 percent of total voluntary benefits sales in 2012, and are growing faster than the sale of individual products at the workplace[8]. Therefore, it's not surprising that benefit brokers are taking share from agents. In 2012, benefit brokers captured 56 percent of total sales, up from 55 percent in 2011 and 52 percent in 2010[8]. Large employers are more likely to prefer group products to individual products, and brokers to agents. Indeed, employers with more than 2,500 employees represented almost one-third of all voluntary benefit sales in 2011[9]. Agents continue to be most active in the small-employer marketplace.

Employee participation levels vary widely within market segments and by employer. They are influenced by a number of factors including:

- Employer commitment to the success of the offerings;
- Employee affinity to their employer;
- Demographics of the group;
- Communication and enrollment strategy and campaigns;
- Geographic dispersion of the employer; and
- Communication and enrollment frequency.

Participation levels are most influenced by the communication and enrollment strategy. Face-to-face enrollment meetings in a group setting (and the subsequent availability of one-on-one consultations) drive significantly higher participation levels. In the small and mid-sized employer marketplace, 35 to 40 percent is not unusual. In that environment, agents, benefit brokers, or per-diem enrollers who use a teaching approach see the best results. Employers especially value the opportunity these in-person meetings provide for promoting and explaining the core benefits program that serves as the foundation for a variety of voluntary benefits. This is a frequently used selling point by agents and benefit brokers.

For large employers with multiple locations, face-to-face enrollment meetings are often impractical and (when done) the experience is inconsistent from location to location. Online communications and enrollment, often supplemented with call center support, is the most common approach.

However, large employers today limit enrollment frequency and a carrier's ability to use sophisticated direct response marketing techniques. It's been difficult for carriers to overcome large employer concerns about "hard selling" and privacy. Instead, voluntary benefits are typically offered when employees enroll annually for their core benefits (or when new employees join a company), and participation rarely achieves double-digits. The inability to segment an employee population and access employees more frequently or as their needs change, significantly impairs the program's success.

Whether a program of voluntary benefits is subject to the Employee Retirement Income Security Act (ERISA) can also influence participation. Employers can have little involvement in non-ERISA plans if they choose to go down that path. Some argue that this leads to poorer participation. On the other hand, we believe it can give carriers more freedom to drive participation.

Maintaining ongoing employee participation is also a challenge. It's best addressed through payroll deduction, which makes for very sticky relationships relative to other billing approaches like credit cards or electronic funds transfers. Carriers also find it difficult to retain employees as clients after they have left their employer – even when products are portable on either an individual or group basis.

Group or Individual?

In the beginning there were "worksite" carriers, whose retail focus led to products being developed and delivered on an individual chassis. These insurers competed primarily in the small-business marketplace. Underwriting was performed on a simplified basis, premium rates were locked in at issue, and commissions were heaped (i.e. high in the first year, lower thereafter). Enrollment was conducted face-to-face in employee meetings at the workplace.

Then along came the "voluntary" players – group insurers typically in the business of providing employee benefits to mid-sized and large employers. Products were sold on a group basis with guaranteed issue, lower initial premium rates, and level commissions. Enrollment was rarely face-to-face.

Today, these distinctions have become less relevant as the marketplace coalesces around the "voluntary" opportunity. While, as mentioned earlier, the sale of group products is larger and growing faster than individual products, it's getting harder to tell the difference between them without actually looking at the contract. Guaranteed issue is often available on an individual platform. Group carriers promote face-to-face enrollment for certain markets. Flat commissions are paid by some carriers for individual products. Even ERISA doesn't distinguish between group and individual products sold in a group setting.

There can be instances where individual products offer consumers more value. Medical underwriting (even on a simplified basis), benefit provisions that build in value over time, return of premium, and true portability are features of individual products that often benefit consumers. In addition, employers can switch group carriers, which can be disruptive for covered individuals. That said, what matters most today for employers and benefit brokers alike are simple and affordable products and the services and support offered by the carrier – not the platform used for filing.

Looking Forward

The ACA will undoubtedly stimulate the voluntary benefits marketplace. Most employers consider healthcare coverage as only one component of a thoughtfully designed and tightly integrated program of employee benefits. And, because it's the most costly component, it often has a second-order effect, a ripple effect, on other employee benefits. In this section, we will explore several of those potential scenarios and their impact on voluntary benefits.

Some research as well as industry pundits have predicted that the ACA will induce certain employers to terminate their healthcare coverage for employees, and that this will dampen employer interest in providing any benefits including voluntary benefits. Why not just let employees purchase their own individual healthcare coverage through the public exchanges? After all, the employer penalty for not offering coverage is less than the cost of providing coverage.

Yet, what this reasoning fails to consider is that it is often less expensive to provide healthcare coverage than to pay the higher salary that employees would require of an employer that drops healthcare coverage. For the same reason, employers with fewer than 50 employees that provide healthcare coverage today will likely continue to do so in 2015 even though they are not subject to the mandate and penalty. In general, we believe employers that today make the business case that benefits are an important component of an employee's compensation will continue to provide healthcare and other protection-oriented benefits following the onset of the ACA. Employers have the option of using a public exchange as their vehicle for providing healthcare coverage. However, the public exchange risk pool is likely to be more expensive than the risk pool for employees.

That said, the ACA may drive up healthcare costs for certain employers. If that happens, those costs will almost certainly be passed on to employees in the form of higher contributions – not a good thing for employees' propensity to purchase voluntary benefits. On the other hand, we believe that the emergence and likely proliferation of private healthcare exchanges (prompted by the ACA, but not legislated) will stimulate a marketplace for not only healthcare, but increasingly for other employee benefits as well.

Moreover, the public exchanges may also become a marketplace for other benefits through a provision of the ACA known as the Small Business Health Options Program (SHOP). The SHOP consolidates the buying power of small businesses to offer more affordable healthcare coverage. Public exchanges may see the sale of other employee benefits (especially those that provide supplemental healthcare coverage) as an attractive adjacency, and they are not restricted from doing so. Private and public exchanges are good news for voluntary benefit players. But, competing in an environment where employees can choose among a number of providers is uncharted territory for most voluntary benefit insurers. It will require a whole host of new capabilities and skills.

There's also the so-called Cadillac tax, which penalizes companies that offer high-end healthcare coverage to their employees. According to the New York Times[10], "companies hoping to avoid the tax are beginning to scale back the more generous health benefits they have traditionally offered and look for ways to bring down the overall cost of care." The tax doesn't kick in until 2018, but it seems employers are already taking action. Likely remedies include higher deductibles, co-pays, and co-insurance – all leading to higher out-of-pocket expenses for employees.

This again is good news for voluntary benefit insurers that, we believe, will find a growing appetite for supplemental healthcare offerings. Aflac's 2013 WorkForces Report[11] reinforces the tremendous need: 45 percent of workers say they have less than $1,000 to pay for out-of-pocket medical and illness expenses, while 25 percent have less than $500.

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What It Will Take to Win

Taken together, the following five actions will put tomorrow's most able voluntary benefits players on the path to success:

1. Develop a clear and concise segment, channel, and positioning strategy;
2. Offer a broad portfolio of benefit solutions that meet multiple employee needs in the segment(s) targeted;
3. Make it easy and seamless for employers;
4. Re-imagine, simplify, and personalize the shopping and ongoing customer service experience for employees; and,
5. Allow employees to enroll at any time.

Develop a clear and focused strategy

Each employer market segment behaves uniquely, requiring different strategies, capabilities, and competencies. Carriers often sub-optimize their voluntary benefits value proposition, resources, and investments in an attempt to be all things to all employers. Carriers need to identify their most leverageable assets, and develop a clear and focused segment, channel, and positioning strategy around them. Pursuing an employer with 5,000 employees sounds exciting. However, if your focus has been small businesses and you distribute primarily through agents, it's likely you will compromise your overall effort. Carriers need to recognize what they do best and stay focused.

Offer a broad portfolio

According to MetLife[7], 47 percent of employers that currently offer voluntary benefits say they are likely to increase the number of products offered in the next two years. That's because employee interest in receiving more voluntary benefits through their employer continues to grow. From the same MetLife study, "62 percent of surveyed employees report they are interested in having their employer provide a wider array of voluntary benefits than is currently offered." It should also be noted that the majority of employers (and brokers) prefer to obtain voluntary benefits from their healthcare or group insurance carrier.

Taking all of these factors together, it means that having a broad portfolio of voluntary products will be a competitive advantage, and lead to deeper relationships with employers and employees alike. Carriers should also consider alliances to fill product gaps and to facilitate speed-to-market. In addition, they should explore offering non-traditional voluntary benefits as a means of heightening employee interest and for competitive differentiation. Auto and homeowners insurance would be one example; group legal, a second. On-site financial education on a variety of topics could be another.

Make it easy and seamless for employers

Carriers that can combine product, enrollment, billing, and administration into a single, seamless package will be rewarded. For that critical first sale to employers, we believe this will be a source of sustainable competitive advantage.

That said, employers and brokers are often skeptical that one carrier can be excellent at every component of a bundled, end-to-end solution. Bundles offer great advantages, but there is a concern they come at a price. Today, most voluntary benefits carriers that offer a bundled solution will unbundle their offering. That is more apt to happen with larger employers in their sometimes misguided quest for best-of-breed. That practice may continue. Furthermore, healthcare exchanges may make unbundling a matter of course, if indeed they become marketplaces for a broad set of employee benefits.

Be that as it may, we believe a piecemeal approach will increasingly become sub-optimal as forward-thinking carriers transform their capabilities and offerings. Selectively swapping out a component or product from one organization for one from another will disrupt the employee experience of the bundle as a whole in ways that are difficult to anticipate or even more difficult to correct. However, it raises the bar for carriers to continuously pursue and create best-in-class componentry.

Re-imagine, simplify, and personalize the employee experience

Employee benefits are a very personal business: real people with real differences. That explains why today's education-based, face-to-face enrollment meetings at the workplace and the subsequent one-on-one meetings with employees yield significantly better participation results than self-enrollment approaches. Self-enrollment is certainly more efficient (and almost always required for large, geographically dispersed employers), but not nearly as effective as face-to-face.

Electronic brochures, websites, and on-line newsletters and decision support tools fail to recognize that employees aren't just buyers – they have evolved into connected consumers. They're connected to social networks. They're connected to like-minded consumers. They're connected to brands. That means they also have the potential to be a carrier's advertisers. Today's consumers have more opportunities than ever before to express their likes, dislikes, and recommendations.

What's more, technology is finally at a point where consumers can be treated like individuals. Replicating a face-to-face experience on a self-enrollment platform is now possible. This concept of mass personalization will enable forward-thinking carriers to infuse every employee interaction with greater engagement and intimacy. In addition, the experience must allow employees to navigate seamlessly among a portfolio of channels (i.e. digital, call center, etc.), depending on the employee's needs and preferences at any given time.

Allow employees to enroll at any time

Linking voluntary benefit enrollment to the annual enrollment for core benefits is a double-edged sword. On the one hand it ensures visibility and provides a window during which employees must act. On the other hand, healthcare sticker shock may dampen employee enthusiasm for voluntary benefits. Moreover, employee needs do not always coincide with an annual, one-time enrollment period. We believe the path to higher participation levels lies in allowing employees to enroll at any time. It would transform what is today often a very static marketing process into one that becomes a direct-to-consumer opportunity for carriers – which itself would require a transformation of most life insurers' marketing departments.

From employers, concerns about "hard selling" will undoubtedly arise. But, we believe the ability to offer employees a highly personal, educational, and engaging shopping experience will begin to address those concerns. From carriers, concerns about anti-selection, where applicable, will arise, but can be easily overcome by requiring evidence of insurability (four or five knock-out questions). Better yet, evidence of a life event change will accomplish the same goal and be viewed as being more consumer-friendly.

A Powerful Growth Engine – for Those That Transform

How will your voluntary benefits business take shape? For all of the reasons we've discussed, voluntary benefits has the potential of being a meaningful growth engine for life carriers. In addition, we believe the workplace is the most efficient and effective channel for accessing the underserved middle market. Employees are enthusiastic about the opportunity to purchase financial services products through the workplace, and tell us they want more.

Winners will transform the employee experience. The technology now exists to do that. But merely investing in consumer marketing, creative, and digital capabilities will not be enough. The path to success will necessitate a top-to-bottom value chain realignment. Operational excellence and putting employees at the center of everything will be of paramount importance. For those break-away carriers the rewards will be significant.

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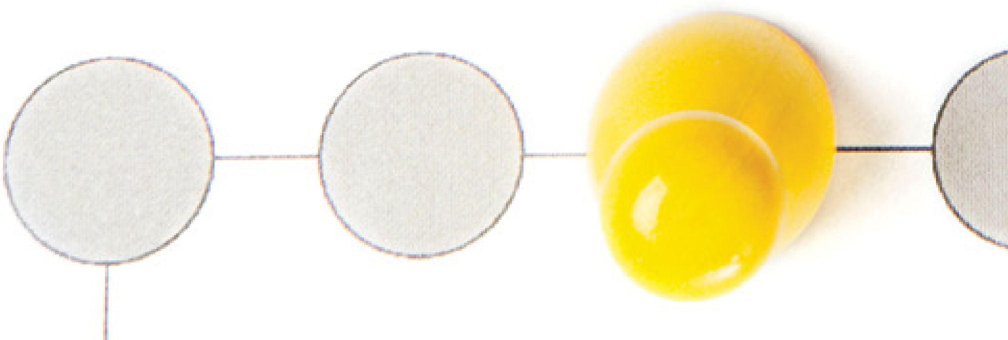

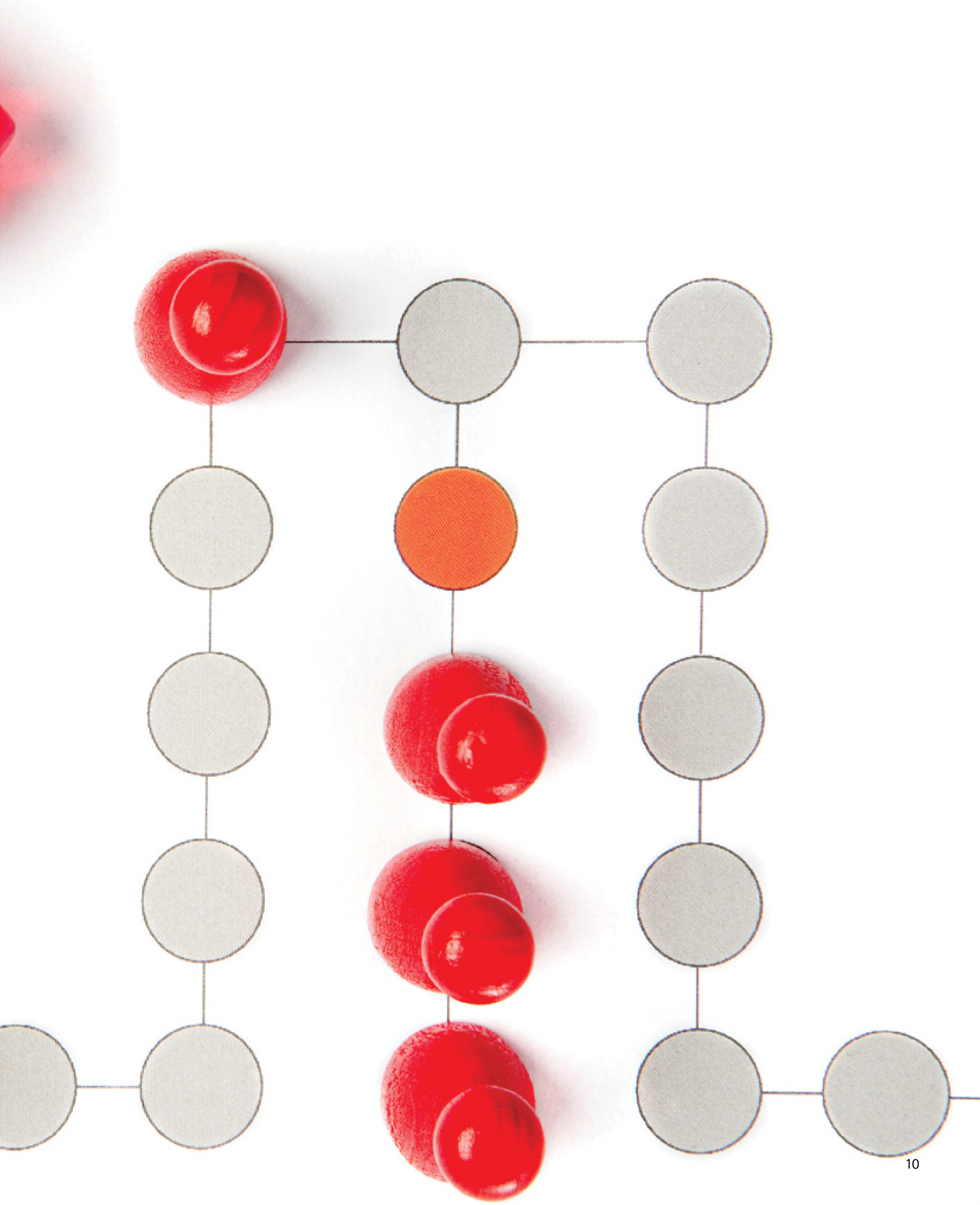

Accreditation

The author of this report is Bob Sollmann, who is a Managing Director in Accenture's Insurance Management Consulting practice. Before joining Accenture at the beginning of 2013, he was a senior industry executive for a Fortune 50 global life insurer, and led its group insurance business, global M&A, Retirement Strategies Group, and the U.S. retail and workplace annuity businesses during his tenure.

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