

Enabling Best Care: How Pet Insurance Can Help

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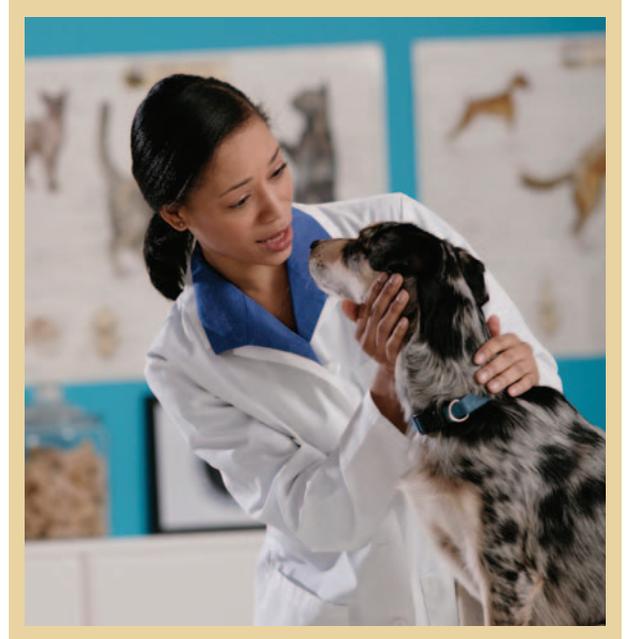
Proceedings from a seminar conducted at the 2010 Western Veterinary Conference. The CE-credit seminar is available online at dvm360.com/ev.

Insurance exists because bad things happen, even to those who mitigate risks. But for insurance to make sense, the risk of loss has to be both reasonably likely and possibly significant. Obvious risks such as property loss or damage, early death, auto accidents and so forth have been long insured.

The first record of insurance dates to the Chinese and Babylonians who insured cargo by borrowing to ship goods and paying off the loans once they received payment. An extra premium on the interest rate covered the loans if the cargo was lost, stolen or destroyed. Greeks and Romans are credited with the first life and health insurance: aristocrats pooled their money; if one of the pool members died or became disabled, the pool cared for his family.

Commercial insurance companies—the first to offer coverage to the public sprang up after the great London fire in 1666. Around this same time, sailing vessels began to be insured by the Lloyds of London syndicates which still exist today.

English insurance concepts were imported to the American colonies. Benjamin Franklin, who founded a fire insurance company in the 1750s, was the first to underwrite risks, choosing not to insure high-risk buildings or charging higher premiums for higher risk situations. Through the insurance mechanism, he also encouraged safer building codes.



The Evolution of Human Healthcare Insurance in the U.S.

Health insurance in the U.S. emerged in the 1920s. The first policies were fee-for-service or indemnity insurance, a contract between the insured and their insurance company. Covered persons paid the medical bill and then submitted the paid bill to the insurance company for reimbursement. Because costs for procedures varied among geographic areas, the insurance company paid a fixed amount called “usual and customary” charges. The insurance company also decided which services and procedures would be covered. Any costs not covered were paid by the insured person.

Currently, every pet insurance company in the U.S. market uses the indemnity insurance model.

Health insurance began to change in the 1940s. Severe labor shortages and wage and price controls as a result of World War II limited employers from

increasing wages. To compete for the limited number of people available for hire, employers began to offer benefits to employees and their families, among them employer-paid health insurance. The federal government saw the advantage of supporting and enticing the system to continue, and created tax incentives for both businesses and consumers.

In the 1950s and 1960s, the government revisited the rapidly developing employer-sponsored system, realizing that it omitted two very important groups: the low income and the elderly. Medicare was created to offer medical coverage for retirees and Medicaid to support medical insurance coverage of low income families and the disabled.

However, by the 1980s it was evident that the healthcare insurance system—which included private insurance plans, employer or group plans and government-sponsored programs—had major problems:

- Employer-paid insurance masked the true cost of healthcare to employees
- Access to insurance was still poor for the under-employed, the partially employed and those who fall into low income categories
- There were no incentives to contain medical costs
- Rapidly escalating costs were a burden to many insurance companies

To exert some control, managed care was invented, defined as “External control over clinical decisions of patients and their providers concerning the treatment of given medical conditions.” Today, managed care is the predominant form of human health insurance.

Could these same societal and economic pressures happen to veterinary medicine? Not likely, as employers and the government will not pay for pet health insurance. While many companies offer pet insurance in their selection of benefits, they are not paying for any part of coverage but only allowing pet insurance premiums to pass through their employees’ paychecks. And the likelihood of the federal government creating a Medicare or Medicaid

system for pets is also extremely low.

What can we learn from the evolution of human dental insurance? To begin with, it is a much younger form, having started in the 1960s as indemnity insurance but taken one step further: dentists could file claims directly with insurance companies on behalf of the patient. In the 1990s the first dental managed care

contracts emerged, initiated by labor unions who wanted constituents covered, but at the same time, costs controlled.

The American Dental Association responded proactively to these new managed care contracts, engaging in research and educational programs for dentists. ADA research found that the older form of indemnity insurance had the best benefit, increasing both the utilization of dental services and practice revenue.

The Creation and Evolution of Pet Insurance

Interestingly, pet insurance has been around as long as human health insurance, having started in Sweden in 1890. Today, about 50% of Swedish pets—mostly dogs—are insured. After more than a century of insuring pets and achieving 50% penetration, it is noteworthy that the Swedish pet insurance companies have not moved to managed care.

Pet insurance began in the United Kingdom after World War II. Pet insurance companies reached 30% penetration, primarily because companies could pay

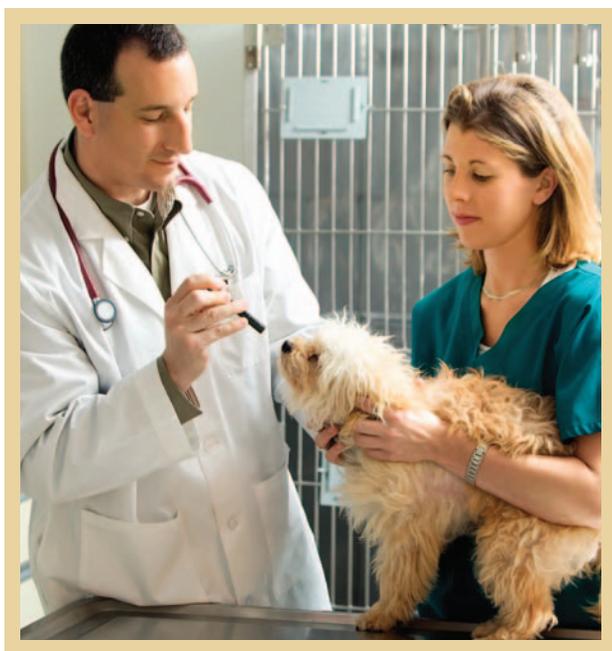


veterinarians a commission for selling pet insurance to their clients. In the U.S. any person selling insurance must be licensed. The U.K. enacted similar regulation a few years ago; the impact on pet health insurance remains to be seen.

VPI® insured the first pet in the U.S. in 1982 and is one of about a dozen companies offering pet health insurance in the U.S. Currently, only one percent of U.S. pet owners have pet insurance coverage. Some studies have suggested that as many as 14% of pet owners could be “reasonable or good prospects.” This percentage is likely high as pet insurance is not subject to the same societal and governmental forces as human medicine:

- Not likely that employers will pay insurance premiums for employees’ pets
- The market for similar “optional” insurance products like renter’s insurance remains low
- Only highly bonded pet owners will consider pet insurance

Because pet insurance cannot grow to the same levels as human health insurance, the companies behind them will never become powerful enough to control veterinary pricing. Veterinary medicine will never become the managed care world of human health.



Pet Insurance: Consumer Perception and Policy Structure

Insurance has evolved along with society. Early forms of insurance were limited to commerce and wealthy individuals. As middle class societies emerged especially after the Industrial Revolution—personal insurance such as homeowners, auto, life and health evolved and have grown rapidly.

As society has grown wealthier and the classic family structure has receded due to mobility, pets have become more important. The human-animal bond has strengthened and the value of pets increased. Accordingly, pet owners are willing to spend more to keep their pets happy and healthy. This trend drives increases in the “stop treatment” amount, making pet insurance a more compelling value proposition.

A recent study shows that the typical pet owner perceives that a \$40 pet insurance policy should only cost about \$20. Veterinarians also experience this value perception gap. We believe it exists because:

- People don’t believe anything bad will happen to their pet
- Pet owners do not understand the cost and sophistication of veterinary care. For example, they believe cancer treatment for dogs should be cheap because “He’s only a dog”
- They know that economical euthanasia is a legal option
- They compare pet insurance to their own health insurance without recognizing that their employer is heavily subsidizing the premium

Because of the perception gap, pet insurance companies must manufacture products that fit the premium that people are willing to pay.

Pet insurance companies offer two fundamental policy structures: the traditional percentage-of-invoice subject to usual and customary limits, and a benefit schedule model.

The benefit schedule is effective at directly tying the benefit paid to the premium charged. It does not attempt to mirror what veterinarians charge for various procedures but is loosely based on the

relative sophistication of procedures. The premium is calculated based on the benefit offered times the projected frequency of pets having those respective procedures.

The percentage-of-invoice model is limited to usual and customary charges—an amount the insurance company deems as reasonable based on average charges in a particular geographic region. All companies exclude pre-existing conditions as they are not insurable risks. In order to keep premiums low, many companies exclude hereditary conditions; others cover hereditary conditions and some partially cover them. These policy structures may also include:

- Lifetime coverage limits. In other words, a condition is paid in the year it was diagnosed, but in succeeding years is not covered
- Limits on what will be paid out over the life of a pet for biological systems (e.g., cardiovascular)
- The facility to increase premiums based on individual claim history or to cancel a policy due to claim history

Client Considerations in Pet Insurance

There are three things that clients should consider when thinking about pet insurance. First is the monthly premium, followed by reimbursement

levels. The two go hand-in-hand, because the higher the premium, the higher the reimbursement that can be paid. Third is the financial strength and longevity of the insurance company, coupled with its responsiveness.

Buying pet insurance is a personal decision. Clients should ask of themselves:

- What's my financial situation? Can I afford the premiums? Can I afford a large, unexpected veterinary bill? Am I a good saver?
- How strong is the bond to my pet? Am I willing to go into debt to save my pet?
- What's my tolerance for taking a risk with the health of my pet?

Only the pet owner can answer these questions. Pet insurance is not right for every client, but as clients look to their veterinarian for advice on pet insurance, practitioners can encourage them to take these questions seriously.

Pet insurance enables best care by assuring the owner that their pet's healthcare will never be compromised. Practitioners and veterinary practices can benefit as well, as outlined in the 2009 NCVEI white paper "A Veterinarian's Guide to Pet Health Insurance." The report is available for download at www.ncvei.org.

The CE-accredited webinar *Enabling Best Care: How Pet Insurance Can Help* is available free of charge to veterinarians and staff online at dvm360.com/ev.



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