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BENEFITS

It's time for a rethink around LTD coverage for older employees

Plans that only pay benefits for workers under 65 could face age-discrimination claims

By Jeremy Bell

Employers and unions should re-think long-term disability (LTD) benefits for employees over age 65 because a common provision — only paying benefits to those younger than 65 — may be susceptible to age-discrimination claims. Sponsors and unions should proactively consider plan options to avoid reacting later.

Many health and welfare benefits, as well as defined benefit (DB) pensions, have elements of age discrimination — in favour of older workers. For example:

Likelihood of death increases with age: With a fixed-death benefit, a 64-year-old receives about 10 times the value a 25-year-old would from a group life plan.

Drug usage increases with age: Again, employees around age 65 will get about 10 times the value from an extended health plan, largely through drug coverage, compared to a 25-year-old employee.

The value of DB pensions increases similarly over time: Credit for a 25-year-old is worth far less than credit for a 65-year-old. The 25-year-old needs to wait 40 years before she starts to receive the pension. This waiting time means the pension credit is five to 10 times more valuable for the older employee than the younger one.

The value of LTD benefits increases over time, but only to a point: Older employees are more likely to become disabled and more likely to stay disabled. For employees aged 55 to 59, the cost of one year of standard LTD coverage — based on the expected value an insurance company would be required to pay — is about 10 times that for employees aged 25 to 29.

Put these factors together and employees approaching retirement — even those doing the same job at the same salary — will receive thousands of dollars more value each year through many benefit plans than those at the beginning of their careers.

Much of this type of discrimination is accepted because the benefits are defined and all employees have the same access to benefits, regardless of age. The value difference occurs because of how employees of different ages interact with the same benefit provisions.

The vast majority of LTD plans limit coverage so benefits are not paid after age 65. Benefits in payment cease at age 65 and benefits do not commence for anyone who becomes disabled after age 65.

There are many reasons why someone may want, or need, to receive income benefits after age 65. They may not have sufficient financial assets or pension income to simply retire at 65. Younger colleagues doing the same job would be eligible for significant income replacement on disability.

This type of discrimination is more difficult to justify than many of those discussed above. The benefit is non-existent for employees older than 65 and very low for those approaching 65.

Justification for age limit

Presumably, employers require some valid justification for the age 65 limit. To some extent, the limit has been around for so long and is so commonplace, many employers have not considered that justification.

Arguments in support of the age 65 limit include:

- It's standard in the industry.
- Canada Pension Plan (CPP) disability benefits are payable to 65.
- Pensions generally provide for normal retirement at 65.
- There is limited or no ability to purchase LTD insurance extending beyond 65.
- Insurance companies have developed offerings around this age limit.
- There is a societal contract for employment and retirement built around retirement at 65.
- The cost of increasing the age limit would be prohibitive.
- An increased age limit would result in similar age discrimination cases.

If the age limit was removed, there would be a host of administrative issues in determining how long LTD coverage would continue for each person.

Some of these arguments can be dismissed fairly easily, such as the lack of a marketplace for insurance products. The market is thin and expensive as a result of limited demand, but the insurance industry is capable of insuring earnings in case of disability for those past age 65.

Weakened justification

Some arguments, though, have more merit. The justification for an age 65 limit on LTD benefits has become weaker in recent years, given that:

- People are living longer and are healthier in their later years. In 1961, the Canadian life expectancy at birth was 68.4 years for males and 74.3 years for females. In 2011, the life expectancy at birth was 79.3 years for males and 83.6 years for females, according to Statistics Canada.
- More Canadians are working beyond age 65 — 24 per cent of people 65 to 70 are still working, up from 11 per cent in 2000, according to the government.
- DB pension plan coverage has decreased. In 1992, 38 per cent of Canadian workers were covered by a DB plan. In 2008, 29 per cent were covered by such a plan, according to Statistics Canada. For the 71 per cent of workers without a DB pension plan, the employment-pension link to an age 65 retirement date is weak and oftentimes non-existent.
- Mandatory retirement rules — those allowing employers and unions to compel retirement at age 65 — have been essentially eliminated.
- In the federal budget in 2012, the eligibility age for Old Age Security (OAS) was increased from 65 to 67. This change is being implemented gradually, reaching full implementation by 2029.
- Some workers' compensation schemes, in British Columbia for example, are now providing limited income replacement starting after 65 and extending beyond 65.

Putting it together

The age 65 limit is extremely convenient for the group benefit industry — it is easy to apply and it limits liability and thus employer and employee costs.

For a significant majority of participants, existing LTD plans effectively replace income over working lives: In other words, the plans do what they are supposed to do.

But the policy does not serve those over age 65 at all. It invalidates their need for employment income in spite of the strong indicator that many still require employment income — they are still working. Because of demographics, workforce participation, mandatory retirement removal and OAS changes, the age 65 limit has started to look arbitrary and, thus, susceptible to renewed challenges.

The age 65 limit may remain in place for some time. Inevitably, though, it will change. There will come a time when enough people are working past 65 that it will be impossible to continue to deem their income unnecessary.

There are many implications to removing the age limit but the cost, regardless of who bears it, could be significant. Employers and unions would be wise to consider possible implications for their plans.

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