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The Hidden Costs of Disability

It is understood in the world of Human Resources that the cost of "fringe" benefits is hidden--unintentionally, to be sure--from employees. It is less obvious, however, that a significant portion of the true costs of benefits are also hidden from the human resources and financial staffs who labor to purchase and administer the benefit programs.

Employers would probably relish the opportunity to understand better the true costs associated with benefits, but lack of time and resources to trace and analyze costs makes this extremely difficult. Additionally, employers are discovering that the administration of benefit plans is more complicated and confusing as new elements and mandates are added to the mix of programs. The combination of complexity of administration and today's leaner support staffs means that even large companies often find effective, comprehensive benefit plan administration to be only a distant goal.

Over the past 10-15 years, the focus of attention has been on controlling the ever-increasing costs of healthcare, primarily through a shift to "managed healthcare" via health maintenance organizations and employer coalitions. As the costs of

healthcare have stabilized, many firms have relaxed their management efforts on benefit issues. But there is a "hidden payroll" cost that is emerging under the banner of "disability," creating a strong incentive for employers to shift attention to this area.

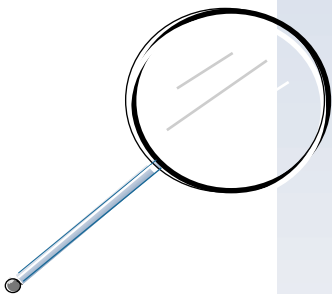
The annual costs associated with employee disabilities are estimated at over \$160 billion. Surveys done by large insurers and the Washington Business Group on Health place the cost of employee disabilities at 6-10% of payroll.

A study entitled *Managed Disability-Past, Present & Future* by Thomas R. Corcoran and Thomas E. Klett of Towers Perrin, reports disability costs as an even greater percent of payroll:

Sick leave	2.0% to 4.0%
Short-term Disability	0.5% to 1.2%
Long Term Disability	0.5% to 0.8%
Medical treatment of Disabilities	1.0% to 2.0%
Workers' Compensation	2.0% to 4.0%
Productivity loss	4.0% to 8.0%
Total	10.0% to 20.0%

Although some of the cost allocated to "disabilities" can be identified as workers' compensation, over

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P R E S I D E N T ' S M E S S A G E



VPA has made great strides toward meeting its goals for 1997 since our last address to you in the fall of 1996. In January, we successfully installed a fully-integrated disability benefit program for Charles Schwab Corporation, which for the first time, allows an employer to have a single-income protection plan for its employees nationwide. This innovative program provides for a single pretax employee contribution to the company's "Income Protection Plan," which provides all their short-term disability benefits that they would normally receive from many sources such as state disability insurance benefits (in CA, HI, NJ, and NY), salary continuation benefits that were previously paid by the employer, and short-term disability benefits that were previously provided by the employer when employees exhausted their salary continuation benefits.

This "single source program" allows Schwab employees to make a *single* toll-free phone call to VPA to apply for *all* of their income protection plan benefits. It also allows the attending physician to certify a patient's disability one time by calling the same toll-free number with the medical certification. This process speeds up the delivery of a single, fully-taxable disability benefit check to employees nationwide (the average time from the date of disability to the first benefit check payment is less than two weeks).

Whereas the previous multiple-source disability benefit system was confusing to employees, the new single-source system clearly explains what disability benefits are being paid to him or her and for what period of time. The reception of this integrated program by Schwab management and employees has been exceptional, and we anticipate that many of our current and future clients will be adopting this type of program in the coming years.

We are also pleased to announce that VPA has been selected to administer the disability retirement benefit program for the Louisiana State Employees' Retirement System (LASERS), which covers over 70,000 Louisiana State employees. VPA teamed with Genex Services to

provide a comprehensive disability management solution. We were particularly proud to be selected by LASERS as we were competing against several major insurance companies and managed-care companies for this contract. The LASERS contract is substantiation of VPA's commitment to expand its existing long-term disability administrative services on a nationwide basis for large, self-insured employers. We anticipate many more long-term disability administration contracts to be forthcoming for VPA.

VPA has also been selected as the short-term disability benefit plan administrator by Science Applications International Corporation (SAIC) for their 18,000 employees nationwide. This program includes the consolidation of self-insured, short-term disability programs with a self-insured supplemental short-term disability benefit plan and the company's salary continuation program. The consolidation will allow employees to receive their complete disability benefits on a more timely basis as well as providing better control over the duration of disability.

As we strive to market our unique "seamless" integrated disability benefit programs to new national clients, we strive even more to maintain our status as the premier provider of integrated disability benefit program administration in the United States. The ongoing enhancement of our proprietary "Disability Claims Management System" (DCMS) and constant upgrading of our staff's skills through acquisition of new employees as well as enhanced training programs for our existing employees, will enable us to not only serve our current clients in a manner consistent with VPA's reputation in the market place, but also provide us with the capability to service even more clients in the future.

I wish to thank all of our current clients who renewed their service agreements with VPA for 1997 and beyond, and I wish to assure you that your confidence in VPA will continue to be rewarded with the highest possible level of service available.

Jack Bredehorn

CLIENT PROFILE



Hewlett-Packard

Hewlett-Packard has always outsourced the administration of their Self-Insured State Disability Insurance (SDI) plans and their Short Term Disability and Long Term Disability benefit plans. In 1991 they selected VPA, Inc. from among several potential vendors, at least in part, because they were impressed with VPA's systems' capabilities. According to Marilyn Howard, Manager of Hewlett-Packard's Disability Service Center (DSC), "we wanted to upgrade our processes, and VPA had the people and the technical support to do it." At that time, each Hewlett-Packard division coordinated their disability claims with VPA. In 1993, Hewlett-Packard centralized the internal disability administration with the creation of the DSC. This consolidation also allowed for the electronic transfer of data between VPA and Hewlett-Packard. Hewlett-Packard also supported full coordination between VPA and their Workers' Compensation carriers in order to streamline and insure integration of those benefits. VPA now has on-line access to all Hewlett-Packard's Workers' Compensation information.

Currently, Hewlett-Packard employees use an automated telephone system or an on-line computerized notification system to alert Hewlett-Packard of a disability. Both systems generate personalized claim packets which are mailed to the employee. Each morning, Hewlett-Packard provides an electronic file to VPA with

the necessary demographic information (name, address, salary, last day worked, etc.) for each employee who has notified Hewlett-Packard of a disability during the prior 24 hours. Employees forward their completed claim forms directly to VPA for processing. The physicians are offered the option of telephoning in their information or completing a form. Twice each month, VPA electronically transfers data to the Hewlett-Packard Payment Service Center for processing. This allows payments to disabled employees to be generated by Hewlett-Packard, continuing direct deposit and allowing convenient maintenance of standard payroll deductions. Ms. Howard believes the system is working well. "We have teams at Hewlett-Packard and VPA that work very, very, closely so the system runs smoothly."

The latest project for the Hewlett-Packard/VPA team is a return to work program which focuses on changing the way disabled employees view themselves. Returning disabled employees to work as quickly as possible through the use of a support network and job accommodation are a part of the proactive stance taken by Hewlett-Packard. Hewlett-Packard's Occupational Health Nurses and VPA's Return to Work Coordinator work closely with disabled employees, outlining restrictions and encouraging a return to modified duty or part-time hours as soon as medically possible. While the program is still "a work in process," according to Ms. Howard, employees are responding and returning to work sooner. This program, as well as the overall duration management of the disability plans has allowed Hewlett-Packard to *reduce* disability benefits costs to *less than 1% of payroll*.



John Gernert

Finance Executive Joins VPA as its Vice President of Finance

Calabasas, Ca - VPA Inc., the largest independent self-insurance disability administrator in the United States, announced that John Gernert, has joined the firm as its Vice President of Finance.

Gernert, a certified public accountant, will be in charge of handling the financial aspects of VPA as the company continues its accelerated growth.

He brings a wealth of financial and managerial knowledge to VPA from his previous company, System Property Development Company, where he was its treasurer and corporate secretary.

During the past 15 years, Gernert has worked for many large companies, including: System Parking, Inc. and Affiliates, where he was treasurer, and Arthur Young and Company, where he was a senior auditor.

Educated at Loyola Marymount University in Los Angeles, Gernert is a director of the Ernst and Young Alumni Association, past director of Downtown Properties Owners Association in Los Angeles and a former steering committee member of the Central City Association of Los Angeles.



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Vice President
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Hidden Costs

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half of the cost belongs under the heading of discretionary benefits. Sick pay, salary continuation, short-term disability benefits--items that were previously considered insignificant or lumped into "payroll" costs--are becoming increasingly costly, and an increase of disability conditions due to aging of the working population and to new types of disabilities, means that companies must carefully examine the future of their disability programs.

Companies are now beginning to consider outsourcing the management of these programs as a win for hard pressed human resource staffs and, very importantly, a win for the disabled employee who receives a high level of attention and guidance as enlightened plan administrators focus on abilities, coordination of effective treatment plans and recovery strategies.

A classic example of this process was reported in *Investor's Business Daily* in an article by Janet Purdy Levieux. The article highlights the efforts of Hewlett-Packard which began over a

decade ago to gain control of the disability costs for the approximately 8% of its 60,000 employees who suffer some disability each year. First the company self-insured its disability coverages (including replacing state-mandated disability programs with private plans where possible) and placed program administration with one administrator (VPA).

Next the company focused on incentives to get employees back to work by eliminating areas of abuse in the sick leave and vacation programs. Finally, the external, single source administration structure was matched to a centralized, in-house team devoted to assisting disabled employees and coordinating the application of disability program provisions and requirements. The process works. According to the article, "disability represents 1% of payroll at Hewlett-Packard, well below similar costs at other firms."

The process takes careful analysis and planning followed by consistent professional management. The financial results and especially the improved outcomes for disabled employees makes the effort important to a company's continued success.