THE FUTURE OF LONG TERM CARE INSURANCE: BOOM OR BUST?

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Introduction

- “If I had known I was going to live this long, I would have taken better care of myself.”
  - Mark Twain, Eubie Blake, Mickey Mantle, George Burns, et. al.

- “I hope I die before I get old.”
  - Pete Townshend of “The Who”, “My Generation”
Emergence of LTCI

- Insurance coverage created to meet the needs of an aging population
- LTCI product design an “accident of history”
LTC – Boom or Bust?

- Market Potential
- Bumps in the Road
- Trends in Product Design
- Regulatory Reforms Underway
Market Potential

United States: 2000

Population (in millions)

Source: U.S. Census Bureau, International Data Base.
# Market Potential

<table>
<thead>
<tr>
<th>Ages</th>
<th>Total Population (U.S. census)</th>
<th>Affordability*</th>
<th>Penetration**</th>
<th>Est. Available Market</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt; 25</td>
<td>99,437,266</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>25-44</td>
<td>85,040,251</td>
<td>42,500,000</td>
<td>900,000</td>
<td>41,600,000</td>
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<tr>
<td>45-64</td>
<td>61,952,636</td>
<td>31,000,000</td>
<td>1,600,000</td>
<td>29,400,000</td>
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<tr>
<td>65+</td>
<td>34,991,753</td>
<td>17,500,000</td>
<td>3,500,000</td>
<td>14,000,000</td>
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<tr>
<td>Total</td>
<td>281,421,906</td>
<td>91,000,000</td>
<td>6,000,000</td>
<td>85,000,000</td>
</tr>
</tbody>
</table>

* Affordability 50% (estimated)

** Penetration <1% ages 25-44, 2.5% ages 45-64, 10% ages 65+ (estimated)
Market Potential

Conclusion:

- Huge untapped market for LTC insurance
- Insurance industry should strive to meet the need through all channels
  - LTC Policies
  - LTC Riders on Life/Annuities
  - New LTC designs for the future
  - Other solutions (e.g. reverse mortgages)
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Bumps in the Road

- Low market penetration
- Declining interest rates
- Lower than expected lapse rates
- Large rate increases
- Class action lawsuits
- Criticism of Industry
Bumps in the Road

- **Low Market Penetration**
  - due to denial of need and lack of awareness

- **Declining interest rates**
  - reduces product profitability
  - not a good basis to request rate increases
Bumps in the Road

- **Lower than expected lapse rates**
  - First modern LTC products were priced with a 5% or higher ultimate voluntary lapse rate assumption
  - Today most actuaries use no more than a 2% ultimate lapse rate assumption
  - Actual mortality also lower than expected
Bumps in the Road

- Large rate increases on existing block of business – driven by:
  - higher-than-expected persistency
  - higher-than-expected morbidity
  - poor underwriting
Bumps in the Road

- Class Action Lawsuits
- High-profile reports and articles criticizing the industry, such as:
  - 1999 Conning & Co. study – “Long-Term Care Insurance, Baby Boom or Bust”
  - Consumer Reports
Conundrum facing the insurance industry:

Having a product that is perceived as too expensive by the public, yet is chronically under-priced.
LTC – Boom or Bust?

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Trends in Product Design

- **Original Nursing Home Product**
  - Covered Skilled Nursing Facility (SNF) stays based on 3-day prior hospital stay
  - No coverage for Assisted Living Facility (ALF), Home Health Care (HHC)
Trends in Product Design

- **Early Product Innovations**
  - Activities of Daily Living (ADL) and Cognitive Impairment Benefit Triggers
  - Inflation Protection (required to offer)
  - Nonforfeiture Benefit (required to offer, not sold in practice)
Early Product Innovations (cont.)
- HHC/Adult Day Care coverage
- Homemaker/Chore services
- Caregiver training
- ALF and other residential care
- Spousal discounts
Trends in Product Design

- More Recent Product Innovations
  - Tax Qualified (HIPAA)
  - Alternative Care
  - Care Coordination
  - Equipment Benefits
  - Pool of money policy maximums
  - Monthly/Weekly Benefits
Trends in Product Design

- More Recent Product Innovations (cont.)
  - Preferred discounts / more underwriting classes
  - Return of premium
  - Single lifetime elimination period
  - Premium waiver for HHC as well as in Facility
Trends in Product Design

- More Recent Product Innovations (cont.)
  - Spousal premium waiver
  - Lifetime waiver of premium for survivorship
  - Shared Care
  - International coverage
  - Limited pay / Accelerated pay
Trends in Product Design

Current Trends

- Shift away from stand-alone coverages such as Home Care only
- Carriers selling only Tax Qualified
- More conservative pricing assumptions
- Higher spousal discounts
- Better coverage for informal care
Current Trends (cont.)

- Elimination of options perceived to be too risky
  - single pay
  - some carriers may withdraw unlimited benefit plans
- More sales through work site
- Shift toward larger carriers marketing product
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Regulatory Reforms Underway

- NAIC rate stabilization regulations (adopted in half the states)
- LTC Active Life Reserves – policy termination rates based on mortality and lapse rates subject to limitations
  - Existing NAIC model
  - New NAIC model (2005)
- Risk Based Capital Formula Change
- Tax reforms (e.g. allow LTCI premiums to be above the line tax deduction)
Regulatory Reforms Underway

- **Contract reserves – Existing Model (Jan 1997) termination rates:**
  - Policy Years 1-4: 80% of Voluntary Lapse Rate, or 8% if less
  - Policy Years 5+: 100% of Voluntary Lapse Rate, or 4% if less
  - Mortality: 1983 Group Annuity Mortality Table without projection
Contract reserves – **New Model** (Jan 2005)

- **Policy Year 1:** 80% of Voluntary Lapse Rate, or 6% if less
- **Policy Years 2-4:** 80% of Voluntary Lapse Rate, or 4% if less
- **Policy Years 5+:** 100% of Voluntary Lapse Rate, or 2% if less (Group insurance exception, use 3% instead of 2%)
- **Mortality:** 1994 Group Annuity Mortality Static Table
Regulatory Reforms Underway

- **Risk Based Capital (RBC)**
  - Changes currently under consideration
    - Formula shift from percent of premium to percent of incurred claims
    - Better tie to risk
    - New formula would reduce capital requirements for new entrants
Conclusion – the Future of LTCI

- Better education of the public is critical for success
- Currently most buyers have had personal experience with LTC – if not, less likely to purchase
- Encourage regulatory reform to allow for new benefit designs
- LTCI Industry cannot repeat past mistakes