

# SEAC

## Would You Like LTC/Critical Illness With That?

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1

## LTC/CI with...

- Individual life products continue to evolve
  - UL focus on flexibility and interest accumulations
  - Recent focus on enhanced lifetime guarantees
  - Backlash to rate wars, with new complementary coverages featuring living benefits
    - LTC riders
    - Critical illness coverage
    - Terminal illness benefits
- Annuity plans are similarly dynamic
  - Increasingly utilize special ancillary benefits such as GMDB or GMLB benefits
  - New benefit features emerging relative to LTC coverage

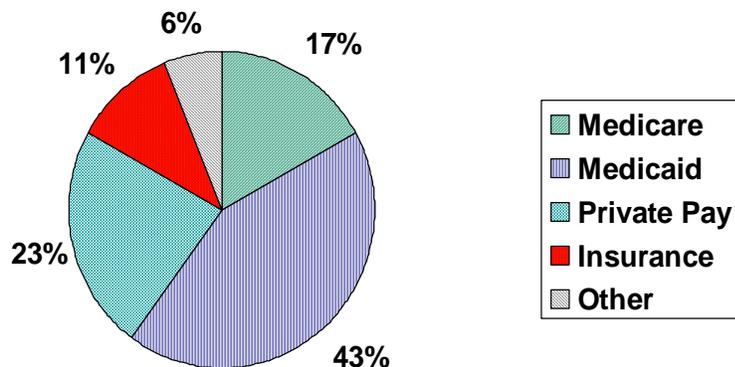
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## LTC/CI with...

- The U.S. population over age 65
  - Over 35 million
  - The number of LTCI policies in force in 2002 was 5.7 million, up from 800,000 in 1987
- A modest number of carriers offering stand-alone LTCI coverage - over 70% of LTCI in the top 10 companies
- Insurance industry experience with stand-alone long-term care insurance plans has not been totally favorable
  - A number of insurance companies have withdrawn due to morbidity risk, interest rate risk, and regulatory concerns

3

## LTC Funding Sources



- Average 2003 semi-private nursing home room costs - \$158 per day
- Average 2003 private nursing home room costs - \$181 per day

4

## LTC/CI with...

- Stand-alone LTCI Policy Characteristics
  - Policy benefits typically limited by daily or monthly maximums
  - Maximum benefit periods specified in years or dollars, and elimination periods commonly apply prior to benefit eligibility
  - Inflation protection must be offered as an option under the NAIC LTC Model Regulation requirements
  - Policies filed to comply with LTCI regulatory requirements may not feature premiums that are expected to increase by age above age 65
  - Rates typically guaranteed renewable
  - Lifetime level pay plans have been the common premium structure, but limited pay designs are increasingly being offered

5

## LTC/CI with...

- Over the last 15 years, there has been an expansion of alternatives to purchasing stand-alone LTCI coverage
- The insurance industry is increasingly offering combination products
  - Allow the industry to access a broader range of the population
  - Mitigate some of the risks for insurance companies
  - LTCI benefits can be provided via riders to fixed, variable, or equity indexed plans of various product lines
  - Different markets are accessed through these differing structures

6

## LTC/CI with...

- Many approaches reduce the cost of LTCI by accelerating the payment of other insurance coverage upon inception of qualified LTC services to the insured
- Consolidate the steps in the consumer's insurance purchasing decisions and reduce the insurance company's marketing costs
- With many designs, the ability to pre-fund the premiums for LTC insurance through another insurance vehicle is achieved, including single premium structures

7

## LTC/CI with...

- Critical illness insurance: the need
  - Increasing gaps in health and disability income coverage
    - Higher deductibles
    - Hospitals out of network
    - Managed care limiting treatment choices
    - Cost shifting from employers to employees
  - Health insurance covers the treatment of a critical illness, not the consequences
    - Continuing medications
    - Travel and related expenses
    - Loss of income not always covered by disability income
    - Loss of spousal income if spouse is providing care during recovery

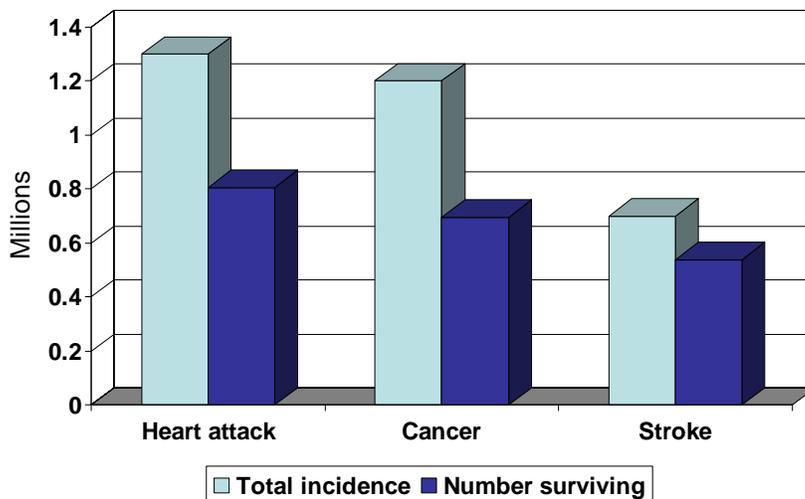
8

## LTC/CI with...

- Critical illness: the market
  - Primarily worksite marketing, some individual and group sales
  - Focus has been low to middle income markets, with increasing attention to middle to upper income markets
- CI: the design
  - Covered conditions, benefit amounts, multiple pay-outs
    - Typically lump sum benefits for cancer, stroke, heart attack, major organ transplant, or kidney failure
    - Pay-outs may vary by age, or by level of severity
  - Waiting periods, survival period, pre-existing conditions
  - Rate structure, renewability, rate guarantees
    - High probability of claim can make coverage expensive
    - Stand-alone versus additional benefit to life policy which accelerates death benefits

9

## Critical Illness - Incidence and Survivorship



10

**LTC/CI with...**  
**Key Structural Considerations in Designing a  
Combination LTC Plan**

- Will LTCI benefits be independent of the base plan, or will they represent an acceleration of base policy benefits?
  - If payment of the LTCI benefit reduces the life face amount, the cost of the LTCI benefit is the cost of acceleration of payment of the life insurance benefit assumed to be paid
  - Results in a substantial reduction to the cost of LTCI benefits offered
  - Increasingly common to see independent LTCI riders offered and sold together with an accelerated benefit rider
  - Challenges of providing accelerated benefit structures to term plans that normally are expected to expire prior to ages where LTC needs are the greatest

11

**LTC/CI with...**  
**Key Structural Considerations in Designing a  
Combination LTC Plan**

- Will the LTCI coverage be filed in compliance with LTCI health requirements, or as a de minimus add-on to the base plan?
  - The NAIC Accelerated Benefit Model Regulation allows for the addition of accelerated benefits to a life product
  - The NAIC Long-Term Care Insurance Model Act includes provisions governing combination policies
  - Life insurance policies that include long-term care insurance benefits funded by a reduction in death benefits need not meet loss ratio requirements
  - The policy is not subject to the same rate increase disclosure and pricing requirements as a stand-alone LTCI policy when the long-term care insurance benefits are incidental to the life policy

12

**LTC/CI with...**  
**Key Structural Considerations in Designing a  
Combination LTC Plan**

- What is the charge structure for the LTCI benefit?
  - If the coverage is structured to comply with all terms and requirements of stand-alone LTCI coverage, the cost must be level for all years beyond age 65
  - Not a natural fit relative to term product ultimate premium scales
  - If the LTCI benefit is configured as a “de minimus add-on to base coverage,” charges for the benefit could be based on a base plan cost of insurance (COI) set-forward, basis points fees on account values, a level premium, or other variations

13

**LTC/CI with...**  
**Key Design Considerations for  
Combination Plans**

- How is the LTCI benefit to be structured in light of policyholder taxation issues?
  - HIPAA provides for favorable tax treatment of premiums and benefits for tax qualified (TQ) LTCI
  - Not clear whether benefits from nonqualified LTCI designs are tax-free, although it is clear that premiums are not deductible
  - Independent LTCI riders on life policies are not treated as “qualified additional benefits” under section 7702
    - Charges withdrawn from the life insurance account values are treated as distributions

14

**LTC/CI with...**  
**Underwriting and Claims Considerations for**  
**LTCI Riders**

- Additional underwriting may be needed for LTCI riders attached to life base plans
  - The life application often a starting point, with a supplemental application providing additional information necessary to evaluate risks critical to LTCI
  - Requirements increase dramatically at higher issue ages, but are less important if the LTCI benefits are an acceleration (i.e., reduction) of base plan benefits

15

**LTC/CI with...**  
**Underwriting and Claims Considerations for**  
**LTCI Riders**

- With an annuity base plan
  - Little or no underwriting involved, and even more likely that additional underwriting requirements will be needed with an LTCI rider
  - With de minimus LTCI benefits, not critical
  - With more substantial LTCI benefits, there is a greater need to require further underwriting
- Specialized claims administration capabilities are generally required for LTCI
  - With accelerated benefits, the value of the LTCI benefits is greatly reduced

16

## **LTC/CI with... Marketing and Compensation**

- With the addition of LTCI to a life or annuity base product, product complexity is increased
  - Agent training required, and licensing requirements - new HIPAA Medical Authorization Regulations went into effect April 14, 2003
  - Thus, even more forms are needed
- A stand-alone LTCI sale is often a multiple visit sale
  - If the LTCI benefit is an acceleration feature with minor costs, it will not merit the same attention as an independent benefit
- Commissions may be asset based, a function of base plan COI rates, or expressed as percentages of target rider premiums

17

## **LTC/CI with... Pricing, Reserving, and Company Taxation Considerations**

- Pricing of LTCI riders requires a range of assumptions including persistency, interest rates, mortality, morbidity incidence and severity, expenses, capital requirements, and taxes
- De minimus benefits are often crudely sized, and if below a certain threshold, a modest charge or no charge is utilized
  - Should be examined by age, as seemingly modest benefits can be expensive at older ages
  - More comprehensive benefits require more scrutiny

18

## **LTC/CI with... Sample Products**

- Company A offers a range of riders covering LTCI
  - One plan uses several annuity base plans, with a rider (not designed to be sold as LTCI) offered to policyholders under age 80 at no cost
  - The rider features an increase to penalty free withdrawals in the event that LTC services are needed
  - Yet another rider features an extension of benefits
- A rider attached to a group variable annuity policy has also been offered by this company for several years
  - The cost for the rider is a portion of the initial premium
  - Features a 7-year deferral period
- The company also offers an accelerated benefit rider on universal life plans

19

## **LTC/CI with... Sample Products**

- Company B
  - This plan features a series of TQ LTCI riders attached to a fixed, single premium annuity
  - Under the first rider, the daily benefit equals the account value at the time of claim divided by 730, payable monthly
  - The first two years of reimbursable LTC service are paid via distribution of account values, with waiver of surrender charges
  - The next two years are covered via a second rider, as independent benefits
  - Another two years of benefits optionally covered via a third rider
  - Costs range from 60 to 300 basis points annually on account values, based on issue age (e.g., the age 70 cost is 140 basis points)
  - Inflation benefit purchases are available annually, up to 5%, but require additional single premium

20

## **LTC/CI with... Sample Products**

- **Company C offers an Annuitization Option Rider**
  - Long-term care insurance rider on an immediate annuity
    - The rider may be elected with life contingent options
  - Annuity payments increased if annuitant is disabled
    - Claims cannot be made until annuity payments have been received for at least 2 years
    - Increased payments continue as long as disability lasts
  - The increased annuity payment is a constant percentage of the basic annuity payment
    - The increase equals 30% for partial disability defined as the inability to perform at least 2 ADLs, & 60% for total disability, defined as the inability to perform at least 5 ADLs

21

## **LTC/CI with... Summary**

- There is a growing need for LTC/CI insurance
  - But there are a variety of considerations within the industry regarding the challenges of stand-alone LTCL, and the need for CI is evolving
  - The number of alternative structures providing a combination of LTCL and CI coverage is increasing
- There will be several challenges to successfully pursuing these combination plans
  - Need to assure that the customer understands the product
  - Marketing, underwriting, claims, and taxation issues must be carefully assessed
  - Pricing of these plans requires careful analysis
- Despite the challenges, continued and substantial expansion with creative combination product designs can be expected

22