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The Suitability Solution for Long-Term Care Insurance

by Denise M. Michaud and Steven G. Stauss

Insurance guru Ben Feldman taught us, "If you don't have a process, you have a big problem."

Well, we see a problem in the long-term care insurance industry because we don't have a standard process. The majority of agents and advisors, who sell a variety of products, are often at a loss for what to do with LTCI. Long-term care insurance hasn't been around long enough and sold widely enough for the industry to have established a sales methodology and suitability standards.

This presents a big problem for insurers, agents and our clients with potentially costly consequences. Insurers lose money through 'wasted' underwriting, application effort and policy modifications. Agents lose time making unsuccessful sales calls or through clients not taking their policies. For the clients, the consequences of poorly designed policies can be devastating.

How, then, do agents today go about designing and selling LTCI policies? From what we observe, they commonly use one of four methods. We call these: (1) the "statistics-say" method, (2) the "big umbrella" method, (3) the "finger-in-the-wind" method, (4) and the "you're-too-poor-to-afford-it, or too-rich-to-need-it" methods. We'll briefly describe each.

1. The statistics-say method

Agent: Well, the average nursing home stay is 2.5[1] years, so three years of coverage should be just fine.

If the agent is going to use a statistic, this is the wrong one. It only looks at nursing home stays, when the vast majority of people receive their care at home (as many as 80 percent). In addition, the 2.5 year figure is based on all stays in nursing homes, including one-to-two week recovery periods from hospitalization, and not just long-term stays for chronic conditions.

Besides, do your clients want their long-term care plans to be defined by a statistic? The agent should be asking what matters to the client and should get to know what sort of person they are. This information will help the agent design a policy that respects their client's humanity and reflects their individuality.

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1) MetLife and American Health Care Association.

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Certainly it is important to look at statistics to get a frame of reference, and statistics are critical to actuarial studies. But if you had a chronic illness, what role would a statistic play? Would it really matter? What would matter? This is what the agent needs to focus on.

2. The big umbrella method

Agent: The cost of care is $200 per day, so you need to have a $200 Daily Benefit with Lifetime Benefit Period coverage.

The agent is 'playing it safe' by attempting to provide a large amount of coverage for the maximum coverage period. This is not a bad strategy in principle, but it doesn't take into account the client's preferences and financial capacities. What if the premium is more than the client can afford or exceeds their "premium tolerance"? What if the client can't afford lifetime coverage, but could afford a shorter period at $200 a day? Maybe the client has some assets that could enable her to partially self-insure (like a medical insurance co-payment).

3. The finger-in-the-wind method

Agent: Let's see. Four or five years should be enough. Lifetime coverage is too much; no one will need care that long.

This sounds like a 'wild guess.' Clients deserve more than that. Furthermore, the agent is exposing himself to possible liability charges later because the agent doesn't have a clear method for arriving at their recommendation.

4. The you're-too-poor-to-afford-it or too-rich-to-need-it method

Agent: Your assets are under $30,000 so you can't afford long-term care insurance. You should just plan on Medicaid.

This isn't helpful or hopeful. In some cases, we may find an alternative solution for this person. If we ignore this request for help, aren't we violating the core of our ethics: caring and service? (Later in this article we show how to construct a policy for someone with assets less than $30,000.)

Agent: Your assets are over $1 million so you don't need long-term care insurance; you can easily self-insure.

This is a broad statement. We cannot conclude the client doesn't need insurance if we don't know what their plans and commitments are for their money. Many wealthy clients *want* to transfer their risk even though they could afford to self-insure.

Most people we know want to protect their hard-earned money against catastrophe. They show this by buying insurance on their homes, cars and health.

With these methods the agent is directing the client without systematically considering their needs, values and financial capacities. At some point, the client may question the purpose and value of their policy because it has no relationship to their circumstances.

We would like to describe a system for producing defensible coverage recommendations for our clients. This is a system that we have developed and refined over 13 years of full-time LTCI sales and that also draws upon Denise's five years of experience as a cost analyst at a major insurer.

Using this system, we have built a large and trusting population of clients who keep their policies in force and refer many of their friends. We call it the *Suitability Solution*. In 2004, we were invited by the California Department of Health Services to teach the Suitability Solution at their annual agents' seminar in Sacramento. Our company now regularly teaches the Suitability Solution as a registered continuing education course in California.

The cornerstone of the Suitability Solution is a process that incorporates human factors: client values, concerns and goals—with financial factors: income, expenses and assets. These factors are applied to the policy components to tailor a policy that is suitable for the client.

Throughout the process we keep the end in mind: The policy must help the client realize their vision of their care and it must make use of their financial strategies. However, clients rarely have a clear vision of what they want or a clear understanding of their financials. It is our responsibility to help draw them out.

The Suitability Solution comprises three main steps:

1) Interview
2) Analysis and design
3) Presentation and agreement

Interview

The interview is best done face-to-face. The objective is twofold:

1) To identify the client's values, concerns and goals as they relate to long-term care, and
2) To get a measure of their finances and help them develop a financial strategy for their long-term care.

You arrive at this information by having them consider how their life would change if they needed care today. This exercise helps them identify what is important for them in their present lifestyle and what would be required to preserve those things if they ever needed care. We use a set of focused questions about human factors (values, concern, goals) and financial factors (income, expenses, assets, obligations) during the interview.

Analysis and Design

Back at the office, you analyze the information gathered in the interview. You develop a strategy, establish a premium cap, develop several feasible configurations, and test the configurations against the premium cap and against client values, concerns and goals. The result may be one or more recommended policy designs.

Presentation and Agreement

When you reconvene with the client, you review the policy design(s) and show how they satisfy their values, concerns, goals and financial strategies. Together, you complete the application with confidence the policy design is suitable.

Case Studies

We now look at two case studies to see how the Suitability Solution can be applied to clients with different personal goals and financial situations. Both are real-life cases. The first one, "Penelope Penniless," is about a client most agents would feel they couldn't help because of her limited income and assets. The second case, "Lori Legacy," presents a typical middle-class senior who has more than sufficient disposable income available to pay a premium.

Penelope Penniless

Interview

We interview Penelope and learn the following. She is 65 years old, has no family, and is in excellent health. She has no assets and rents a room in the house owned by her church friend, Naomi. She supplements her $1,667/month Social Security with income from a part-time job. She has $200 in monthly discretionary income, not counting her job. Naomi and the rest of her church community have reassured Penelope that she can count on them for help and support. It is very important to Penelope to remain close to her church friends, as they are her family.

Penelope is a proud and independent woman and has told us she will not accept care from her friends because she does not want to burden anyone. Further, she is unwilling to interfere with Naomi's lifestyle by having caregivers come into Naomi's home. She has already decided she will apply for Medicaid and enter the nearest facility with a Medicaid bed.

However, when Penelope needs care, there may not be any local facilities with available Medicaid beds. She could be placed hours away from her friends. Our challenge is to help her with this problem.

Analysis and Design

Our strategy is to make sure that Penelope is placed in a nursing home in her community.

Penelope needs to move into a nursing home—as a private pay patient. Paying privately will increase her choice of facilities and improve her odds of staying in the community.

Using the NAIC guidelines of 7 percent of Adjusted Gross Income (AGI), we calculate a premium cap of $117/month. This is comfortably less than her $200 in discretionary income. To

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determine design policy alternatives, we look at four primary components: Daily Benefit, Elimination Period, Inflation Option, and Benefit Period.

The cost of a semi-private room in a nursing home in her area is $200/day. Penelope's Social Security income would pay for about $55 per day. However, because her income only increases by 2 percent per year, the amount she would be able to contribute will diminish over the years. To be safe, we will select a daily benefit of $200.

Her Social Security is sufficient to pay for only eight days of care, so we have to choose a 0-day elimination period.

The inflation option needs to be 5 percent compound since she is a healthy age 65 and is likely to live well into her 80s.

Coverage	Initial premium	20% added after 10 years	Another 20% added after 20 years
Facility-only 1 year	$108	$130	$156
Premium Cap Source of money: Soc Sec increases @2% per year	$117	$140	$167

Penelope's Policy: The Suitable Solution

Type of Policy:	Facility-Only
Elimination Period	Zero Days
Daily Benefit	$200
Inflation Factor	5% Compound
Benefit Period	One Year
Maximum Lifetime Benefit	$73,000

We can do quotes for various benefit periods. However, it is clear she won't be able to afford a very long period, so let's start with one year.

The table on page six shows the premium for the above policy design. We project at least two premium increases and make sure that the money that is available to pay the premium can keep up with these potential premium changes.

Presentation and Agreement

Together with Penelope, we review our recommendation against her values, concerns and goals.

Does the policy meet her values? *Remain independent and self-sufficient, not be a burden to others*

She does not want to burden her friends with managing her care, so we make certain the policy includes a care manager provision. The Facility Only policy is affordable and gives her a period of independence and self-sufficiency.

Does the policy address her concerns? *Becoming an imposition, being vulnerable because she has no financial resources.*

Penelope goes into a Medicaid eligible nursing facility as a private pay patient and with a care plan in place. She imposes on no one. In California, nursing homes only need to see one year of financing for admittance. After the benefits in the policy have been exhausted, Penelope will apply for Medicaid. The nursing home must allow her to stayon as a Medicaid patient (California law). During the year she is a private pay patient, Penelope will have the opportunity to use her income at her discretion, perhaps donating money to her church.

Does the policy meet her goals? *Stay in the community.*

She will be able to go into a nursing home in her community as a private pay patient, arranging to stay there when she eventually goes on Medicaid. Being closeby, her friends would be able visit her easily and often.

Lori Legacy

Interview

From the interview we have learned the following. Lori is age 62 and in excellent health. She owns a condominium worth $300,000 and has $100,000 invested conservatively and earning 5 percent. Her income consists of Social Security and a small pension. Both are indexed to the cost of living. Her monthly expenses are minimal, and she has about $750 left over at the end of the month. She has a well-to-do son who lives locally, but the relationship is strained. Her daughter is a financially struggling single mother; she has offered to be her caregiver if needed, but lives out-of-state.

We also find out that Lori:

a) Will not impose on, or live with her son or daughter, if she needs care.
b) Wants to receive care at home, but will go into a nursing home if necessary.
c) Wants to leave her condo to her daughter.
d) Would like to leave her remaining cash to her son, if possible.
e) Will not pay more than $350 per month for her policy.

Analysis and Design

Our strategy is to make certain that she can receive care in her condo, will not burden her family and will be able to leave her condo to her daughter when she dies.

Lori has given us a premium cap of $350. We want to shelter her condo, ideally. Her living expenses are covered by her pension and Social Security and should keep up with cost of living increases. Since the income from her $100,000 investment is not needed for living expenses, we will consider using a portion of it to pay an elimination period.

To design policy alternatives, we start with a daily benefit of $200. For $200, she can hire a live-in for 8-10 hours of hourly care at today's rates. Lori is still relatively young, so we include a 5 percent compound inflation rider. She wants to stay at home, but her health could decline and require her to go into a nursing facility, so we opt for comprehensive coverage. We will treat these three factors—daily benefit, inflation rider and policy type—as constants and will vary the other components to try to get Lori the maximum coverage within her premium tolerance. We will factor in two 20 percent premium increases.

To ensure Lori is not a burden on her family, we only examine policies that include a care management feature.

The following table on page 8 shows several policy configurations generated using illustration software from a well-known insurer. (In our full analysis we examine four to six insurers.)

Presentation and Agreement

Together with Lori we review our recommendation against her values, concerns and goals.

Does the policy meet her values? *Remain independent, self-sufficient, not burden others*

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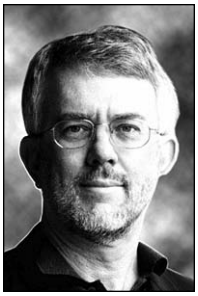
The cornerstone of the Suitability Solution is a process that incorporates human factors: client values, concerns and goals...

Benefit Period	Initial Premium	20% added after 10 years	Another 20% added after 20 years
4 years; 30-day EP	$372	$446	$536
4 years; 60-day EP	$341	$409	$491
5 years; 30-day EP	$417	$500	4601
5 years; 60-day EP	$381	$457	$549
Premium cap (2% inflation) ("Stretch" alternative	$350 ($381)	$418 ($464)	$510 ($566)

Denise M. Michaud, CLTC, is a co-founder of The Center for Long-Term Care Planning and is a licensed LTCI broker.

Lori's Policy: The Suitable Solution

Type of Policy	Comprehensive
Elimination Period	60 Days
Daily Benefit	$200
Benefit Period	Four Years (5 Years)
Lifetime Maximum Benefit	$292,000 ($365,000)
Inflation	5% Compound



Steven G. Stauss is a co-founder of The Center for Long-Term Care Planning and is a licensed LTCI broker.

With this policy, Lori will not need to burden others with the research and provision of care services. She will maintain her independence and self-sufficiency. Although Lori's stated premium tolerance is $350/month, we explore with her the possibility of "stretching" a bit in order to purchase a five-year benefit period.

Does the policy address her concerns? Stay home as long as possible, keep her home.

It gives her the security of knowing that she has the financing for four or five years of home care without using her home's equity. If she needs care longer than four years, Lori will move into a nursing home under Medicaid.

Does the policy meet her goals? *Passing her home on to her daughter, keeping the premium within her stated amount.*

Although Lori would need to "spend-down" her $100,000 before becoming eligible under Medicaid, the home is exempt. Lori can gift the home to her daughter before she dies (California rules). We keep the premium low by having Lori self-insure two months of her care (60-day elimination period).

Conclusion

The process we have described can be used by agents to improve the suitability of the policies they sell. This will result in better service to our clients and increased client confidence in our professionalism. Insurers should see a decline in money lost to underwriting effort wasted on poor-quality applications and policy modifications.

In the end, agents should also see an increase in their referral stream. ❋