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Managing the Risks of the Long-Term Care Insurance Reinstatement Process

by Loretta Jacobs

As many long-term care (LTC) insurance blocks of business mature, new business management challenges are beginning to appear. One such emerging risk relates to the reinstatement process, which is the process by which a lapsed policy is reactivated and put back in the same position as it was before the lapse occurred. Since LTC insurance lapse rates have historically been low, insurers have not typically placed significant focus on the management and mitigation of the reinstatement risk exposure. However, a recent increase in litigation activity and regulatory scrutiny related to this process has led insurers to strengthen their risk management controls over it.

LTC insurance reinstatement requests primarily arise from one of three reasons, with only the first being specifically contemplated in LTC insurance regulation. First, a policy may be unintentionally lapsed because the policyholder is cognitively and/or functionally impaired at the time the premium billing notice is sent and is not reasonably capable of paying the bill. Second, a policy may be unintentionally lapsed for a variety of other reasons, including the policyholder claiming not to have received a billing notice, the insurer claiming never to have received monies the policyholder sent, or the policyholder submitting the premium to the insurer sometime after the end of the grace period. Finally, a policyholder who has voluntarily lapsed coverage may simply have a change of heart and request to reinstate the policy.

COGNITIVE AND/OR FUNCTIONAL IMPAIRMENT REINSTATEMENT SITUATIONS

The NAIC Model LTC Regulation, and essentially every state with explicit LTC regulations, recognizes the need to protect LTC insureds from unintentional lapses of their LTC policies when they most need them (i.e., when they are eligible for LTC insurance benefits). The robust protection against unintended lapse typically includes requiring an initial billing statement and a 30-day overdue billing notice to be mailed to the insured, plus a policyholder option to name at least one individual to receive a similar 30-day overdue billing notice alerting the named third party that the insured's premium is overdue and the policy is in danger of lapsing. Finally, termination of the policy cannot occur any earlier than at least 35 calendar days after the overdue notice(s) is(are) mailed.

Then, if the policyholder requests reinstatement of the policy within five months of termination and can demonstrate his or her condition would have qualified for LTC policy benefit eligibility on the termination date (i.e., that he or she was cognitively and/or functionally impaired in accordance with the definitions contained in the insured's policy) and pays all overdue premium, the policy is reinstated and treated as if it had never been out of force.

For purposes of this article, the reinstatement regulations of Florida and Washington will be analyzed and discussed. The reader may then consider the similarities and differences of these regulations to those of the other states.

Washington's reinstatement regulation states, "A long-term care insurance policy or certificate must include a provision for reinstatement of coverage in the event of lapse if the issuer is provided proof that the policyholder or certificate holder was cognitively impaired or had a loss of functional capacity ***before the grace period expired.*** Reinstatement must be available to the insured if requested ***within 5 months after lapse*** and may allow for the collection of past due premium if appropriate. The standard of proof of cognitive impairment or loss of functional capacity must not be more stringent than the benefit eligibility criteria for cognitive impairment or the loss of functional capacity contained in the policy or certificate."

Florida's reinstatement regulation states, "If a policy is canceled due to non-payment of premium, the policyholder is entitled to have the policy reinstated if, ***within a period of not less than 5 months after***

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Loretta Jacobs, FSA, MAAA, is a senior manager with Ernst & Young in Chicago, Ill. She can be reached at Loretta.Jacobs@ey.com.

the date of cancellation, the policyholder or any secondary addressee designated…demonstrates that the failure to pay the premium when due was unintentional and due to the policyholder's cognitive impairment, loss of functional capacity ***or continuous confinement in a hospital, skilled nursing facility, or assisted living facility for a period in excess of 60 days."*** The Florida regulation also states, "Notice of possible lapse in coverage due to nonpayment of premium shall be given by ***United States Postal Service proof of mailing or certified or registered mail to the policyholder and secondary designee*** at the address shown in the policy or the last known address provided to the insurer. Notice may not be given until 30 days after a premium is due and unpaid. Notice shall be deemed to have been given as of 5 days after the date of mailing."

Disputes Arising from the Five-Month Reinstatement Request Time Period

An issue that has arisen recently surrounds the interpretation of the date on which the allowable five-month time frame to request reinstatement begins. The state of Washington suspended one insurer's license to sell LTC policies for six months in 2011 because it interpreted the five-month time frame as beginning on the date the (unpaid) premium was initially due, not the date on which the lapse transaction occurred, 65 days later.

To the extent that other jurisdictions follow Washington's lead, there are implications for insurers. Clearly, all insureds must be provided at least 7.13 months (equal to regulatory minimum of five months plus at least an additional 65 calendar days) after the last day coverage was paid for to request reinstatement. In addition, if for some reason an insurer delays terminating a policy beyond the required minimum 65 day time frame from the original premium due date, the five-month time clock only starts on this latter date. For instance, if a carrier has a system outage and does not lapse any policies for a day, a week, or some other time frame, this extra time the policy has remained in force does not count toward the five-month reinstatement request time period.

Disputes Arising from Demonstration of Cognitive or Functional Impairment

Another source of dispute in the cognitive and functional impairment reinstatement process is the requirement to prove that cognitive or functional impairment began before the grace period expired. Most states include language requiring that the evaluation standard of cognitive or functional impairment be no more stringent than that used to adjudicate claims under the policy. These standards usually involve review of medical records and the results of formal cognitive testing performed on or before the lapse transaction date.

However, insureds may not have formal cognitive testing documented in their medical records and so even those insureds who truly have Alzheimer's or another eligible cognitive impairment (as proven by cognitive testing performed at a later date) cannot clearly demonstrate such impairment in the medical records dated before the expiration of the policy's grace period. In these cases, reinstatement is not required by law. Alternatively, an individual may have had cognitive testing performed before the grace period ended, but the results of the testing do not indicate a ***severe*** cognitive impairment as required by the insured's LTC policy. While a modest cognitive impairment may have contributed in some way to the insured's alleged unintentional lapse of his or her policy, this level of impairment would not entitle the insured to have his or her policy reinstated.

Of course, state regulations are worded to permit insurers to utilize less stringent standards for evalu-

ation of impairment for purposes of reinstatement of coverage than for benefit eligibility determination for claims submitted on in-force policies, but it is unlikely that carriers would employ such a procedure in practice.

An interesting side note to this issue is the inclusion by the state of Florida of the phrase permitting reinstatement as long as the insured has been ***continuously confined*** in an Assisted Living Facility for at least 60 consecutive days. This is problematic for insurers because simply being confined in an assisted living facility does not mean the insured is eligible for LTC insurance benefits. In fact, the term assisted living facility applies to a broad range of entities; many such facilities may actually be independent senior living apartments and serve as the primary residence of insureds who are neither functionally nor cognitively impaired. The inclusion of this phrase in the Florida law significantly broadens the reinstatement right for coverage that was allegedly terminated unintentionally.

OTHER REINSTATEMENT REQUESTS

Many situations arise in everyday policy administration where a policy is unintentionally terminated and the customer wants to put the policy back in force when the termination is discovered.

Allegations of Premium Billing and Collection Processing Errors

A common complaint insurers hear is that the customer simply did not receive his or her billing notice or lapse warning or that a third party did not receive the lapse warning. It is unclear how often coverage is reinstated without investigation or management involvement when an insured maintains he simply did not receive his mail. Insurers would be wise to keep a record of all such reinstatement activity and may be surprised to find how often allegations of billing errors occur. To the extent that this activity is more frequent and exposes the insurer to more risk than it prefers, alternative management of the billing and collection process may be in order. For instance, an insurer who is reinstating a policyholder for a second or third time due to alleged lack of receipt of mail may wish to condition the reinstatement on future billing by automatic bank withdrawal.

Alternatively, an insurer may choose to investigate alleged billing errors in detail, rather than simply accepting the customer's word that an error occurred. If the insurer finds no evidence of any mishandling, it may deny automatic reinstatement but as a good faith policyholder service, may offer these individuals the opportunity to reinstate coverage by providing satisfactory evidence of good health. With mature blocks of business, it is unlikely that more than half of the applicants will be able to satisfy the underwriting criteria, but offering some means by which an individual may reinstate coverage may be viewed more favorably by state regulators or other outside third parties who may end up reviewing these situations than simply denying the request on the basis of not finding errors in the billing process.

As noted earlier, the Florida regulation requires that lapse warning notices to policyholders and third-party designees be mailed by U.S. Postal Service proof of mailing or certified or registered mail. Presumably, the reason for this requirement is to reduce or eliminate the number of disputes arising from alleged failure of the U.S. Postal Service to deliver required notices. However, the additional costs of mailing these notices by certified or registered mail are likely prohibitive for insurers with large blocks of business in Florida. While U.S. Postal Service proof of mailing is reasonably cost efficient, it does not provide evidence of ***receipt*** by the customer or third party, but rather simply provides evidence that the insurer ***mailed*** the notice(s). Carriers may wish to consider the possibility of mailing lapse warnings via certified or registered mail for older and/or longer duration policyholders and the less expensive U.S. Postal Service proof of mailing for the remaining policyholders.

In addition, to the extent that the root cause of alleged non-receipt of billing notices is due to the notices being inadvertently discarded as "junk" mail by the recipients, insurers may wish to review their billing packages for effectiveness. For instance, adding a bolded "Important Insurance Information Enclosed" message on the envelope may be an inexpensive yet effective way to reduce the possibility that these important lapse warning notices will be discarded without being opened.

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Premiums Arrive Late

A common problem that insurers face is whether to reinstate policies when premiums arrive shortly after the end of the grace period. Carriers may routinely provide an additional "internal grace period" of up to two days in the event that the 35th day following the mailing of a lapse warning falls on a Saturday, Sunday or holiday. But what happens if the 35th day after a lapse warning was mailed falls on a regular business day and the premium arrives the following day? When is a premium finally "too late" to allow the policy to be automatically reinstated? These are questions LTC carriers have to answer for themselves.

A key component to successful management of an LTC insurance operation is development and implementation of a comprehensive risk management strategy.

A separate emerging issue facing LTC insurers in the reinstatement management process relates to required health insurance policy reinstatement language that also appears in LTC policies. For example, the Florida health insurance reinstatement provision states, "Reinstatement: If the renewal premium is not paid before the grace period ends, the policy will lapse. ***Later acceptance of the premium by the insurer,*** or by an agent authorized to accept payment without requiring an application for reinstatement, ***will reinstate this policy…"***

LTC insurers typically process premiums through a bank "lock box" process. Directly billed LTC insurance premiums are mailed to a post office box that essentially is a banking facility. As soon as the premium is received at the lock box, it is deposited into the insurer's bank account. The insurer's accounting team subsequently reconciles the premium receipts to its active policyholder list, and discovers that premiums have been received on a terminated policy. The insurer then refunds this premium to the lapsed policyholder by ***issuing a new check.***

Attorneys for terminated policyholders may suggest to their clients to mail premiums to the insurer and then file suit claiming that the insurer has "accepted" the premium because it deposited the money in its bank account without issuing a "conditional receipt" and therefore the policy has been reinstated, even if the insurer issued a refund check within a short period of time, such as a week or two weeks. To the extent successful, this path to reinstatement exposes the insurer to significant adverse selection and should be managed. Insurers may wish to research with their banking facility partner whether it is feasible to alter the process to eliminate certain checks from being directly deposited, and instead held in abeyance for up to 24 hours while being researched. Such checks could be directly returned un-cashed to the lapsed policyholders and the insurer would be less vulnerable to the argument that it had "accepted" the premium.

CONCLUSION

A key component to successful management of an LTC insurance operation is development and implementation of a comprehensive risk management strategy. Procedures to address the risks of the reinstatement process should be incorporated into such a comprehensive risk management plan. Carriers may wish to consider establishing a Senior Management Reinstatement Review Committee composed of underwriting, claims, actuarial, legal, compliance and policy administration personnel who would be charged with not only evaluating reinstatement requests but also with reviewing the various premium billing and collection processes used by the company to determine if there are ways to alter them to mitigate the reinstatement risk exposure (without exposing the carrier to other risks). Of course, as carriers begin to formulate risk management protocols to address reinstatement and other emerging LTC insurance business risks, it may be valuable to discuss the plans with internal or external risk management professionals and/or Sarbanes-Oxley compliance staff to gain additional perspectives and insights.

Note: *This is an abridged version of "Managing the Risks of the Long-Term Care Insurance Reinstatement Process." The article, in its entirety, is available online at* http://www.soa.org/ltc. ■