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Conflicting Perspectives on LTC Rate Increases

by Larry J. Pfannerstill

Guaranteed Renewable with level premiums anticipated for the life of the policy. Those are provisions included in almost every individual long-term care (LTC) policy contract sold since the early stages of the product. However, it's become common for companies in the industry to recognize that the original anticipation of level premiums throughout the life of the policy cannot always be maintained. Premium rate increases on LTC products have become more common and have brought increased scrutiny to the industry by agents, regulators, current policyholders and potential purchasers.

There has been relatively little discussion of rate increases in trade publications, although everyone involved in the LTC industry is aware that this practice is occurring. So, let's acknowledge the elephant in the room by examining the different viewpoints of three stakeholders in a LTC insurance contract; the insurance company that issued the policy, the policyholder that purchased the policy, and the insurance department that approved and continues to regulate the policy. Each of these stakeholders has very different, and often conflicting, opinions on the appropriateness of rate increases on individual LTC policies. One thing I believe each party would agree on is that when the policy was issued, none of them anticipated that premium rates would increase in the future.

JOE THE POLICYHOLDER

Joe purchased his individual LTC policy back in 1999 at age 60. He was in good health at the time and was issued at a preferred rate. (The insurance company had no underwriting restrictions regarding unique middle names). Joe's comprehensive policy benefits included compound inflation and carried an unlimited, or lifetime benefit maximum. He bought top-of-the-line coverage available at the time and considered himself a responsible person for purchasing coverage for his long-term care needs.

It's now 2009, and just after his 70th birthday, Joe received a notice that his premiums were increasing by 25 percent on the next renewal date. The following thoughts randomly cross his mind:

- I thought the premiums were level for life. Now the insurance company says it can raise my rates! I'm complaining to the insurance commissioner.
- What do I have to show for the 10 years of premiums I paid without collecting any benefits?
- I'm on a fixed income while everything I purchase keeps getting more expensive each year. I'm not sure I can afford to keep paying these premiums.
- The company is offering not to increase my premiums if I reduce my lifetime benefits down to five years. Is that still a valuable benefit to cover my needs?

Joe's situation is hardly unique. Seniors who bought policies years ago are generally less healthy and unlikely to qualify, or even find comparable benefits in the market at a price similar to what they are paying. It's difficult not to feel a level of remorse for policyholders in this tough situation.

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THE DEPARTMENT OF INSURANCE

Protection of the policyholders in their respective state is the utmost priority of the Commissioner of Insurance. Their department is responsible for monitoring the practices of insurance companies to ensure that the companies are compliant with the regulations of the state that were established in the interest of all Joe T. Policyholders. The regulations, in most cases, are based on the National Association of Insurance Commissioners (NAIC) model regulations but with state specific modifications. Joe's policy was issued prior to the state's adoption of the NAIC Rate Stabilization Model Regulation. Therefore, the regulations governing rate increases are likely the same regulations that were used as guidance when the Department originally approved the policy form for sale. These regulations rely on minimum loss ratio standards to prove that proposed premiums are reasonable in relation to benefits.

There is a wide variation of interpretations by states in granting a rate increase based on those regulations. However, there is often additional information the department is forced to consider in the process of evaluating a rate increase filing. For example, Joe's complaint to the insurance commissioner will likely not be the first if the department has approved rate increases on other LTC companies. Based on my discussions with regulators on rate increases filings, most departments are keenly aware of the policyholder complaints that will be generated by a rate increase on LTC policies. This is even more of a significant concern in those cases where the policy form has been granted an increase in the past. Along with policyholder complaints, increased scrutiny on the industry from the media and higher levels of government, including federal, have influences on whether or not rate increase filings are approved. These influences have become more intense over the past few years as the number of companies filing for rate adjustments has increased.

In some states, the maximum percentage increase that can be approved is now limited by regulation. This limitation is viewed by regulators as a method to protect the policyholders from excessive rate increases. If Joe's policy was issued in one of these states, his increase in any one year will be less than or equal to the regulated maximum, but he may receive further increases in subsequent years. The regulations in other states give the commissioner discretionary power to limit rate increases "if the proposed increase is deemed excessive." In summary, the department governing Joe's policy now has multiple factors it must consider when deciding on the appropriate future rate levels, besides the actuarial justification submitted in the rate increase filing. This has been very plainly explained to me in discussions with staff at the department of several states.

THE COMPANY

Looking in a rear view mirror, the industry as a whole did not price appropriately for the risks accepted in the early stages of LTC products. The products were evolving and there was little historical data on which to base assumptions. Right around the turn of the century, companies began to realize that pricing assumptions were not being realized, and the profits were not emerging as expected. Benefit designs were changed, new issue premiums increased and there was a general improvement in risk management through advancements in underwriting selection. This left many companies with an older block of business that was performing below expectations. There are different strategies employed by companies to regain profitability on older LTC policies. Some companies use experience on better performing segments of their business—LTC or other product lines—to offset losses on older LTC policy blocks. Others have used extensive claim management programs to delay or mitigate the need for premium increases. However, the most prudent management decision for some companies was to exercise the contractual provision of the guaranteed renewable

product and increase premiums. Unfortunately for Joe, his company may have tried other options, but they still ultimately increased premiums.

As mentioned in the prior section, there is a wide range between states on the level of acceptance or reluctance on granting rate increases. From the viewpoint of a company that is operating in several states, this can be frustrating for several reasons including the following:

- The company has a contractual right to increase premiums to cover the cost of benefits covered by the policy. As a business, they have a right to earn a profit.
- Insurers have taken on increased and unforeseen risks as long-term care services have evolved since the policies were first issued. An example is the increased use of assisted living facilities.
- Denial of actuarially justified rate increases shifts additional risk to the company without compensation.
- More states are disapproving or severely limiting increases based on seemingly political arguments.

The management teams at companies I am familiar with did not take the decision to increasing premiums rates lightly. They reviewed other financial options, claim management alternatives, and also considered the impact of increases on the policyholders as well as the reputation of the company. I suspect the same decision process goes on in other companies before rate increases are filed.

Companies typically offer alternatives to reduce or eliminate the increase in rates. In Joe's case, the company is offering him the opportunity to continue paying the same premium by reducing the maximum lifetime benefit to five years. This option my also require approval by the state if there is a new rate schedule for the five-year benefit option or other elections. The policyholder has the right to change benefits at any time, but presenting different options to manage the premium level is helpful to all parties at the time of a rate increase. Such a compromise reduces the level of frustration of the policyholder, helps avoid complaints to the department, and reduces the ultimate risk of the company.

Recently, some states are taking additional steps in the interest of protecting their policyholders. Some are requiring the company to offer a paid up benefit if the policyholder lapses, in order for the state to approve a rate increase. This is similar in concept to the NAIC contingent non-forfeiture model, but the implementation is achieved by compromise, rather than by regulation. One state requires that the company offer to roll the policyholder over to a newer product with comparable benefits, that is subject the Rate Stabilization Regulation, commonly referred to as an MAE (Moderately Adverse Experience) regulation. In both scenarios, the company is being required to offer additional benefits and potentially assume greater risk without additional compensation.

MY ADVICE FOR JOE AND OTHERS

In Joe's situation, my advice would be to accept the reduction in the maximum benefit period (or adjust other benefit options) and maintain the current premium level. The five-year benefit is still a valuable long-term care benefit. He will have much greater benefits by maintaining the premiums he has been able to afford in the past, and presumably in the future, than he would by letting the policy lapse and taking the paid up option. However, Joe should be mindful that additional premium increases could happen in the future. The value of 25 percent could be an indication that a higher percentage was originally requested but the full amount was not approved. There may be some indication in the renewal letter he received. There may be additional information on the practices of the company regarding rate increases on other forms. Information can be found on most states' Department of Insurance Web sites. The California Web site below includes all approved rate increases on LTC policies in any state.

http://www.insurance.ca.gov/0100-consumers/0060-information-guides/0050-health/ltc-rate-history-guide/index.cfm

Joe's scenario is an example of the rate increase actions that are actually occurring in the LTC market with policies priced prior to the introduction of MAE regulation. In many states, compromises are made in order to gain approval of some level of rate increase, which is usually less than the percentage requested and justified from the viewpoint of the insurer. These compromises may not be in the best long-term interest of the current or future policyholders as they may eventually lead to the need for even higher ultimate rate increases.

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Departments of Insurance must continue to protect their policyholders from abusive practices but also recognize the need to keep LTC companies viable in order to pay future LTC benefits, and approve appropriate premium increases in a timely fashion.

Without some correction, it is easy to visualize the direct progression of the following steps:

1. An insurer unintentionally issuing an underpriced LTC policy.
2. Departments denying, delaying or limiting the needed rate increase.
3. Failure and liquidation of the company.
4. Policyholder benefits being reduced to the limits of each states' guarantee fund.
5. Increased cost to all taxpayers as more long-term care costs are paid by the general funds of each state through Medicaid benefits.

Granted, this is a "doom and gloom" scenario, but it is still a *plausible* scenario. If the private LTC market is to survive, each stakeholder must do their part to support that survival. Companies must first use appropriate, responsible pricing assumptions and effectively monitor their experience. Then, if unforeseen events occur that are beyond "moderately adverse," the company should file rate increases as soon as possible to control the amount of increase needed. Departments of Insurance must continue to protect their policyholders from abusive practices but also recognize the need to keep LTC companies viable in order to pay future LTC benefits, and approve appropriate premium increases in a timely fashion. Blanket denial of rate increases will hurt both the companies and policyholders in the long run.

The industry is challenged with finding a solution to the financial losses attributable to the pricing mistakes of the past. With the current regulatory structure, the options are limited. Unfortunately for all the Joe T. Policyholders, the LTC uninsured population, and the LTC industry, I expect that it will take the failure of one or more LTC companies to gain the attention of our regulators that the current structure is not working. At that time, we in the LTC industry must take up the cause to educate and steer any change in an appropriate direction.

The intent of this article is to spark discussion within the LTC industry regarding rate increases. The opinions expressed or implied, are solely my own based on eight years of filing rate increases for different LTC companies and periodic discussions with staff members at several Departments of Insurance. The opinions are not intended to reflect those of my associates or the companies which I have assisted. ■