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Strategic Approaches to Help Make Long-Term Care Risks More Manageable

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As baby boomers enter their retirement and the U.S. population aging continues, there is a huge foreseeable need to address future financing of long-term care (LTC). This creates promising opportunities for insurance companies to provide consumers with solutions to help them better manage their chronic conditions. However, as we think about the current LTC insurance industry, not a month goes by where we don't hear news that another LTC carrier has had to take a substantial premium increase and/or a sizable hit to their balance sheet to cover future LTC liabilities. This has created negative publicity that unfortunately has dampened both carrier's and consumer's confidence in LTC insurance. As carriers' management recognize the demand for new and sustainable private LTC insurance solutions and continue to look at ideas, an important question remains as to what product characteristics will help address the risk and value issues associated with current LTC policies.

To help management better identify and evaluate new product ideas, this article seeks to apply lessons learned from our experience to the next generation of LTC products. It focuses on how new products should address having acceptable carrier risks and at the same time enhance the product's value to consumers to pave the way for broader acceptance.

In this article, we will reference several innovative LTC product ideas including: Combination products that add LTC riders to base life policies or base annuity policies; LifeStage Protection; LTC Retirement Approach e.g., Retirement Plus; Limited LTC coverage (short-term care and home health care (HHC)); and Medicare/LTC.

What will it take to build the next generation LTC products that will meet both the consumer and the carrier needs?

CARRIER AND PRODUCT RISK

The existing private LTC insurance is deemed to be a high-risk product from a carrier's perspective as its profitability is highly sensitive to changes to a few of the key risk factors such as investment return from asset portfolios, consumers' lapsing behavior and morbidity costs. The challenges of pricing products, the difficulty in getting rate increase approvals, and the complexity in managing the ongoing claims have inhibited carriers from recognizing potential losses in a timely fashion. Therefore, any new LTC product idea will only be appealing to carriers if it has lower risks both relative to the existing LTC products and at an acceptable level in the absolute.

We believe that new product offerings should have the ability to address the following key risk factors:

> New products should address having acceptable carrier risks and at the same time enhance the product's value to consumers to pave the way for broader acceptance.

Risk mitigation and management

The existing LTC product's profitability is volatile and is highly sensitive to the changes in key risk assumptions (morbidity, morbidity improvement, mortality, mortality improvement, lapses, interest rates, and expenses). A small negative change to one of these key assumptions could potentially require increasing reserves by 5x+ or 6x+ or reduce profits by close to half or more.

Some new product concepts are proving to be more attractive to carriers (e.g., combination products and possibly retirement plans that include built-in LTC protection) by employing what's known as "natural hedging" of risk. These products offer both morbidity and mortality protection and these different protections have different financial characteristics whose risks tend offset each other. For example, extended mortality tends to add risks for LTC policies (consumers staying alive longer represents more potential LTC claims), while it reduces the risks for the life insurance component of policies (consumers staying alive longer means the time of death benefit payout occurs further into the future allowing for the investment horizon to be extended).

In addition, the profit sensitivity to claim incidence and termination assumptions is significantly reduced as the insured uses

their own money to pay for LTC benefits and the company is at very little LTC risk.

Experience driven assumptions, corrective mechanics and risk prevention

Many existing LTC policies were priced with limited known information 20 or 30 years ago, when 8 to 12 percent interest rates were common, and lapse rate assumptions hovered around 8 to 10 percent. However, interest rates have dropped significantly and lapse rates have shown to be close to 0 percent. The experience for some key assumptions is starting to stabilize and become more conservative (e.g., how low can lapse rates be, given that carriers are using close to 0 percent lapse assumptions). Using conservative experienced based pricing assumptions to price new products naturally provides companies with an additional layer of assurance that the assumption volatility is being stabilized and mitigated.

In addition to having experience driven assumptions, it's important to have mechanics that would help mitigate risks to prevent the carriers from taking on an excessive amount of unhealthy risks. Such mechanics would allow correction if consumer behaviors turn out to be more adverse than expected. Some of these mechanics may include examples such as having the right level of underwriting protocols, a deferral period before one can be eligible for coverage or automatic enrollment requirements. Experience has shown that carriers who utilize comprehensive underwriting protocols have experienced up to 50 percent reductions in the claims relative to carriers who do not use them.

Some Medicare/LTC product concepts being considered would impose automatic enrollment requirements on the LTC component. This would help mitigate severe anti-selection risks. Also, this product could be proposed with annually renewable premiums. That way, if the product was somewhat underpriced in year one, it could be corrected on an annual basis as with health insurance plans.

Up until this point in the industry, carriers typically have not proactively managed their insured populations to with the idea of mitigating potential claims costs. Inclusion of some form of preventive health care or wellness benefits could help early detection of conditions that could lead to claim and allow insurers to help consumers take actions that could manage or mitigate those conditions and potentially minimize resulting claims as well.

Limits to upside risk exposure

Existing LTC products often provided lifetime coverage, very rich inflation benefits or cash as opposed to reimbursement benefits. Historically, companies had anticipated potential high benefit utilization by consumers when benefits are rich and loaded their base assumptions significantly. These rich benefit features were therefore priced significantly higher than the less rich benefit features (e.g., cash benefit is usually priced 50 to 70 percent higher). However, despite the loaded based assumptions, emerging experience still shows rich benefits have introduced a much higher than expected consumer anti-selection and utilization of benefits.

What's even more concerning is that the experience will likely continue to deteriorate as the average LTC insured reaches their peak age to claim.

Recently, short-term care and HHC only coverage have gained sales momentum and attention. Short-term care policies provide insureds with up to one year of coverage. While these policies will not completely cover all of insured's LTC needs, they do provide comprehensive coverage to help cover the chronic care needs, especially if that care is delivered in the less expensive home setting. By limiting the maximum amount of benefit a company could potentially be exposed to, these types of products significantly reduce carrier risks.

BALANCING CARRIER RISK AND CONSUMER VALUE

The LTC industry has often proceeded under the assumption that actions to mitigate carrier risk will carry with them the unintended consequences of higher premiums and premium uncertainty and that in turn will lead to low perceived consumer value. The dramatically lower sales that we have recently seen with traditional LTC products suggests both a very dangerous downward spiral and the need for the industry to think differently about our LTC product offering. It turns out that different thinking may result in the opportunity to both enhance consumer value AND mitigate carrier risk.

While the number one reason that consumers state for not purchasing LTC, in study after study, is that the products are not affordable, we believe that the problem isn't just price. It's that consumers aren't convinced that the current LTC product benefits provide sufficient consumer value to justify the price and the long-term financial commitment required to maintain coverage.

In recent qualitative research conducted for the State of Minnesota, consumers stated: "I know I am going to die, but I don't know if I am going to need LTC. What happens if I pay premiums for years, but end up not needing LTC or die before I use it." These type of comments reflect the uncertainty that consumers feel regarding the value of the traditional LTC product.

But there are product development strategies that have the potential to increase the value of the LTC product offering without necessarily adding substantially to either carrier or consumer costs

New Combinations

As noted above, the recent success seen with products that combine life or annuity with LTC **mitigate carrier risks**, but in addition provide significantly **enhanced consumer value and increase consumer appeal**. In recent quantitative research conducted by the LTC Think Tank, when consumers were exposed to both the LifeStage Protection concept (combing term life coverage during working years with LTC later in life) and the Retirement Plus concept (adding a built-in LTC benefit to their Retirement savings account), they reacted very positively to the idea of multiple product benefits in one product offering. The research indicated that both product concepts' projected trial scores were well above those typically seen in financial services products and both concepts were deemed to have significant market potential.

Creative opportunities to add consumer value by combining/adding benefits to LTC can go beyond these two ideas to include additional product benefits for other family members and caregivers, as well as adding healthy living benefits to the product.

More Health/Less LTC

Often we think of LTC events as an inevitable result of aging. But there is new medical thinking that 50 percent or more of the chronic conditions that are responsible for LTC claims are controllable by changes in lifestyle—better eating, more exercising, stress reduction, better sleeping, etc. There is even thinking by leading medical experts that many of these lifestyle changes can strengthen the brain to the point where it can ward off or mitigate dementia. A product offering with a benefit of "helping you stay younger, longer" will have broader consumer appeal than "helping you protect your assets." And, if the "healthier living" results in lower frequency and duration of claims that could mean that what we and consumers currently deem "adequate" protection could be significantly lower and less expensive in the future.

At the recent ILTCI conference, the session entitled "Guiding Insureds to Healthier Futures" explored both new medical protocols that can help consumers lead healthier lives, but also the kinds of incentives that can be offered to encourage them to undertake them. Carriers would do well to consider the positive potential of incentivizing healthy aging behaviors with the goal of mitigating those chronic conditions that are

Figure 1
Stay at Home Costs and Savings versus Nursing Home Care

Care Site	Average Daily Claim $s HHC	Average Daily Claim $s NH	Stay at Home Daily Difference	Monthly Savings at Home	Months to Pay Back $1,000 Investment
$100 available DMB	$85	$97	$12	$365	2.7
$150 available DMB	$114	$137	$23	$700	1.4
$200 available DMB	$131	$165	$34	$1,034	1.0
$250 available DMB	$151	$212	$61	$1,855	0.5
$300 available DMB	$158	$242	$84	$2,555	0.4

precursors to LTC claims, even for those insureds who have not yet reached claim status.

Encourage and support care at home

The vast majority of seniors want to stay in their own homes for as long as possible. The fear of going to a nursing home to receive care is one of the biggest fears that seniors have, as evidenced by the not infrequent promises enacted by parents from their children to do everything so they won't have to go to a nursing home. Developing new offerings that provide support for technologies and support services to enable people to safely stay at home longer-**even before they are on claim**, has the potential for a major win/win. It keeps people where they want to be for as long as possible, has the potential to keep people out of the institutional settings they want to avoid and most importantly is typically significantly lower in cost. Figure 1 is derived from Society of Actuaries claims experience data and suggests that monthly care savings realized by remaining at home versus going into a nursing home can range from over $300 per month to well over $2,500 per month depending on the available Daily Maximum Benefit.

Given the level of potential savings, carriers should consider use of technologies like emergency medical response systems, medication management and even tele-health programs for current claimants, insureds and older family members to provide the support that can enable consumers to remain healthier and in their own homes for longer.

Add Now Benefits

The LTC industry has, for years, investigated the idea of more "now" benefits. It's time to renew considerations for adding NOW benefits to LTC products so that consumers can realize some benefits today without the need to wait 20, 30 or 40 years, if then, to benefit from the product. In the current environment, consumers are increasingly focused on the short term. They have a difficult time emotionally justifying expenditures that have high uncertainty associated with them, even when logic might say they should. Providing tangible benefits that they can access sooner rather than later can add significantly to the consumer perception of value for LTC offerings.

CONCLUSION

Two of the main problem areas for existing LTC product are the risks that it represents for insurance carriers and its failure, to date, to address consumer value issues. A successful next generation LTC product needs to address a significant portion of both the carrier risks and consumer value issues. With a careful design of LTC product solutions, that include both risk mitigation and consumer value adds, version 2.0 of LTC protection products can and should be able to be managed profitably. ■

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