LTC Rate Increases: Exploring Alternatives

By Nolan B. Tully, Sandra K. Jones and Jessica E. Loesing

As issues surrounding the cost of long-term care for Americans becomes the focus of the industry, premium rate increases have historically been necessary to maintain the financial integrity of most blocks of stand-alone long-term care insurance (LTCI) business. In conjunction with those rate increases, insurers have offered (and regulators have approved) an evolving menu of rate increase mitigation options for policyholders who do not wish to or otherwise cannot afford to pay the increased rate. Recently, we have seen new and innovative alternatives proposed by industry participants. There is a growing recognition that insureds should be educated about the nature of their existing coverage and presented with a variety of options in the alternative to paying the approved rate increase amount. In the past few months alone, insurers are offering, and regulators are approving (and sometimes even requesting), an even wider variety of options, such as modifying existing coverage, reducing available benefits, or taking a reduced paid-up policy, policy buyouts and even "hybrid" policy buyouts.

Rate increase litigation also remains prevalent. Providing alternative options to a premium rate increase can serve to reduce the risk of litigation by: (1) satisfying the need of insureds to feel heard and attended to, as an individual, rather than as a group of policies, and (2) diminishing a common perception that the insurer is callously seeking more premium for the same coverage—particularly for those who might misinterpret the underlying reasons for the increased rates. These dynamics warrant consideration of how best to present mitigation options to insureds and what mitigation options to propose. Some of those options are explored below.

While no option is a panacea for all (and some of them come with risks of their own), we believe that consideration of a wider variety of rate increase mitigation options present an opportunity for insureds who are otherwise subject to a rate increase to customize and tailor their coverage. Doing so will allow adaptation to their budgets, care needs and changing health, and can simultaneously present an opportunity for insurers to solidify the financial footing of blocks of their business.

CASH BUYOUTS FOR POLICY SURRENDER

Historically, insurers have turned to policy buyouts in one-off scenarios—usually related to litigation or policyholder fraud. Recently, companies have started to consider policy buyouts as potential options available to insureds at the time of a rate increase. At least two insurers have actually sought approval for these options, and one of them—Penn Treaty Network America Insurance Co. (in liquidation)—received broad favorable regulatory response. Although Penn Treaty's rate increase was in conjunction with a liquidation, making it unusual and unique, it is worth noting that regulators were willing, for the first time, to consider some "out of the box" mitigation options. While buyout options present some anti-selection and litigation risk of their own, they also offer a potential benefit to insureds to liquidate an otherwise illiquid asset, while allowing insurers the potential to reduce exposure to in-force long-term care insurance policies. The description and presentation of the offer and the disclosures accompanying must be well-thought out and drafted, creating a viable path toward including buyouts at the table of possible alternatives to an otherwise "take it or leave it" rate increase.

1035 EXCHANGES

In the long-term care insurance context, 1035 exchanges are not always available—or otherwise thought of as a viable option. Exchanges are more palatable to those insureds who anticipate long-term care needs but do not want to maintain the coverage under current policies for a number of reasons. With a 1035 exchange option, insurers might offer insureds an exchange of their policy for an annuity with various payout options. Thus, if the insured does not end up needing long-term care in the future, the use of the funds is left to the insured's own discretion. Regardless of how the insured ultimately uses the annuity, his or her premium dollars have possibly multiplied through investment. This sort of arrangement may also serve to ameliorate regulatory concerns about future care costs, while at the same time limiting a perceived paternalistic control over policyholders' finances by insurance companies.

REDUCTION OF COVERAGE OPTIONS

Rather than require an insured to pay increased premiums and keep his or her benefits the same, a company may offer its insureds several choices of policy benefits that will either maintain their current premium, result in a lower premium rate increase or even result in a premium decrease. This reduction in "face value" of a policy can occur through several mechanisms, including a reduction in overall lifetime benefits, a reduction in the daily benefit amount, a reduction in types of coverage or benefit offered under the policy, or a reduction or elimination of inflation protection. Having myriad options allows policyholders the ability to consider the trade-off between having reduced coverage and paying less premium. This is especially helpful to an insured who might have a better grasp on their health status but is worried about their current or near-term finances. For example, reducing coverage from unlimited lifetime benefits to a set term of years can substantially reduce the premium for some policyholders, yet allows policyholders to feel "covered." In any case, a reduction in coverage allows the insured to keep his or her policy place at a more sustainable and "personalized" cost.

DROPPING A RIDER OR TWO

More recently, the idea of allowing insureds to "sell back" or "trade in" particularly "rich" riders has become another option to satisfy insureds and insurers alike. This scenario—which is a hybrid of a buyout and a reduction of benefits—allows an insured to drop an expensive rider that he or she might no longer need or want in exchange for maintaining a stable premium. Even better is that, for policies with multiple riders, insureds may be able to go back to the company and trade in riders multiple times without impacting his or her overall basic coverage under the policy. For example, insurers can offer to buy out riders at a multiple of the premiums paid on the rider over the lifetime of the policy, ultimately returning the entirety of the premium dollars paid on the rider to the insured. Alternatively, if a rider provides a specific benefit, the rider itself can be "separated" from the policy and placed into paid-up status while the policy remains active and intact. This option may also prove to be more palatable from a regulatory standpoint, as it allows insureds to retain coverage but drop additional benefits, years or other "rider" protections that might not be necessary any longer.

More recently, the idea of allowing insureds to "sell back" or "trade in" particularly "rich" riders has become another option. ...

REGULATORY APPROVAL

Whether or not regulatory approval is obtained (or required) will dictate the breadth and depth of any rate increase mitigation option. In light of those (and other) concerns, the National Association of Insurance Commissioners Executive Committee formed a Long-Term Care Insurance (EX) Task Force earlier this year. The task force has set goals to establish national standards for reviewing and approving rate increase requests, as well as "identify[ing] options to provide consumers choice regarding modifications to long-term care insurance contract benefits where policies are no longer affordable due to rate increases."[1] The task force will deliver a proposal on these topics to the Executive Committee by the 2020 Fall National Meeting.

ACTUARIAL CONCERNS

The risk of adverse selection often ranks as a carrier's highest concern in connection with consumer alternatives to rate increases. From an actuarial perspective, both regulators and insurers have legitimate concern about the effect that rate increases and consumer alternatives will have on the remaining in-force blocks, compared to assumptions set at pricing. These concerns, along with the problems of pricing the alternatives, often pose the biggest hurdle in offering a buyout or other alternative to a rate increase.

The most obvious adverse selection concern relates to health: Will healthy insureds allow their policies to lapse, opt for a buyout or otherwise remove themselves from the risk pool, leaving an insured population that no longer reflects the general population? On the other hand, adverse selection is multi-faceted and other anti-selection concerns exist in the consumer alternative domain. For example, individuals that are terminally ill or otherwise have a short life expectancy may cash out their policies in exchange for funds needed now. These individuals may ultimately receive a cash payment from the company in exchange for liquidation of a policy that they were never going to use. But adverse selection can also result in retaining healthier insureds; the most financially secure insureds are also the ones most likely to keep their policy in force even in the face of a significant rate increase. These insureds also typically enjoy the best access to health care and opportunities to age in place, leaving healthier insureds in the pool at the highest rates of coverage. These unpredictable effects of a rate increase require carriers to rely heavily on their actuarial teams.

LITIGATION RISK

Litigation risk remains prominent in the realm of premium rate increases. Although courts have strongly found in favor of insurers concerning the right to raise premium, subject to regulatory approval, that has not stopped creative plaintiffs' attorneys from filing class action lawsuits attacking rate increases. The "filed rate doctrine" is a formidable defense available to insurers in many jurisdictions. Recently, however, rather than questioning the insurers' contractual right to raise premiums, newer vintage class actions have relied on marketing materials or unusual policy or rider language as a way to collaterally attack the rate increase. These new and creative theories of recovery are likely to extend to insureds who claim to be harmed by their "choice" of rate increase mitigation option, especially to the extent a certain option might not work out as expected financially. Likewise, family members that later discover the insured has chosen a particular option and disagree with that choice will be a hotbed of litigation. Disclosure language, unambiguous presentation of all options available, and clear and consistent documentation of the insured's election(s) are key elements of mitigating this risk. Other options are worthy of consideration as well—such as requesting (or even requiring) that the insured consult with an attorney or financial adviser or requiring sign off by a secondary/tertiary designee.

CONCLUSION

In sum, rate increases involve an inherent risk factor—and have for many years. Insurers can get creative toward mitigating these risks by (1) working closely with regulators to gain approval of the programs they intend to implement, including some of the alternatives proposed in this article, (2) carefully documenting the actuarial calculations and conclusions underlying the program that is ultimately offered to the market, and (3) meticulously crafting language in its rate increase offerings to insureds that are clear, lack "legalese" and are unequivocal in the messages conveyed. As the industry continues to respond to the marketplace, the financial climate and the needs of society, we believe that customizing policies will become commonplace and will benefit insureds and insurers alike. ■

Nolan B. Tully is a partner at Drinker Biddle & Reath. He can be reached at *Nolan.Tully@dbr.com.*

Sandra K. Jones is counsel at Drinker Biddle & Reath. She can be reached at *Sandra.Jones@dbr.com.*

Jessica E. Loesing is an associate at Drinker Biddle & Reath. She can be reached at *Jessica.Loesing@dbr.com.*

ENDNOTE

1 National Association of Insurance Commissioners. Long-Term Care Insurance (EX) Task Force. Accessed Oct. 29, 2019. *https://naic-cms.org/cmte_ex_ltci_tf.htm.*