State of the Long-term Care Insurance Industry

Vincent L. Bodnar, Chief Actuary LTCG
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Agenda

• What made LTCi successful in the early days?
• What happened to traditional LTCi?
• Attitudes of a new buyer generation
• Are hybrid products the answer?
• What else can we do?
Funding of LTC Expenses

- US spending on LTC was $239 billion in 2014
- 63% was funded by two social programs:
  - Medicare: Limited post-acute care
  - Medicaid: Once assets are spent down
- 20% from direct out of pocket spending
  - Most represents asset spend-down
- Only 3% from private LTC insurance
  - 7 million insureds out of 86 million age 55+

The Need for Private LTC Insurance

- Asset spend-down most common funding scheme
  - Savings are first exhausted or moved via loopholes
  - Migration to public welfare (Medicaid) afterwards
- Strain on social program funding
  - Medicaid's mission is to provide a safety net to the poor
  - Not meant to fund lack of LTC planning for the middle class
- Clear need for individual financial planning / private insurance
  - Demographics result in an unsustainable burden on public resources
  - Preserve assets / legacy funding
  - Higher quality of care when privately funded
Consumer Attitudes

• Biggest fears about retirement\(^1\):
  – 11%: Will have too much debt
  – 18%: Won't be able to afford daily expenses
  – 23%: Exhaust savings
  – 28%: High medical (LTC) expenses

• Most are aware of Medicaid as a safety net, but worry that it won’t allow an acceptable lifestyle

\(^1\)Source: Bankrate.com Money Pulse Survey, Feb. 18, 2015

Consumer Attitudes

• Private financing of LTC is strongly preferred\(^1\)
  – 59% agree that individuals should be responsible
  – 66% agree that owning private LTC insurance would give them peace of mind
  – 51% don’t trust the government to run an LTC insurance plan

• Knowledge of LTC costs and risks is relatively low\(^1\)
  – Most greatly underestimate the chance of needing LTC
  – 20% can correctly estimate costs in their state
  – 44% have “other priorities” for money other than LTC insurance

\(^1\)Source: 2014 Survey of Long-Term Care Awareness and Planning, U.S. Dept. of HHS
Unique Distribution Challenges

• Example of a product that is “sold not bought”
• Lack of awareness of risk and gaps in coverage
• Unfamiliar product features
• Expensive
• Broad distribution channels did not push
  – Lack of understanding of product; discomfort selling
  – Already successful selling other products

How the Industry Responded

• We answered this challenge with specialty distribution
  – Agents that are trained to sell LTC almost exclusively
• Small distribution pockets produced a majority of sales
  – Initial specialists were captive
  – Independent specialists later emerged and dwarfed captives
• Agents were trained to:
  – Patiently sit with customer leads – often several hours
  – Educate customers about risks and complex products
  – Have rational responses to premium amounts
• Specialists often worked with broader distribution to chase
  leads they encountered (split commissions or referral fees)
Specialists: Key to Success

- Of the 177 carriers that entered the LTCI market
  - 74 sold less than 1,000 policies
  - Only 56 sold 10,000 or more

- Most carriers did not train or access trained distribution and exited the market early

- Carriers that used specialists saw large sales volumes

- Key to understanding how we succeeded and how we might reenergize the market

Sales Volumes

- Early success! 20%+ growth during the 1990s
- Short-lived: Sales began to decline in 2001
  (after netting out 2002-2003 FEP enrollment)

Source 1999 – 2015 Broker World Surveys
What Caused the Crash of Traditional LTCI?

Reason 1: LTCI’s design makes it a very risky product
- Level premium pre-funds an increasing cost
- Four forces contribute to increasing claim costs:
  - Older people more likely to need long-term care
  - Wear-off of underwriting effect
  - Benefits increase for policies with inflation protection
  - Married people becoming widows and widowers (which have higher costs)

Reason 2: Environmental developments
- Very low lapse and mortality rates
  - LTCI’s pre-funding nature makes it lapse supported
  - Early pricing assumptions of 4% turned out to be almost zero
  - Mortality rates are lower than annuitant mortality tables
- Unforeseen drop in interest rates
  - LTCI’s pre-funding nature makes it very sensitive to interest rates
  - Early assumptions of 5%-8% turned out to be 2%-4%
- Emergence of assisted living facilities (“ALFs”)
  - Immaterial care delivery sector when early products were priced
  - Expensive ALF stays are not embedded in early pricing data
  - Almost half of current confinements now occur in ALFs
What Caused the Crash of Traditional LTCI?

Reason 2: Environmental developments

- Regulators resist large rate increases (>25%)
- Often cannot offset losses completely, resulting in reserve corrections
- Creates uncertainty for distribution and potential new customers

What Caused the Crash of Traditional LTCI?

Reason 3: Carrier exits

- 7 out of top 10 carriers writing at LTCI’s zenith have exited
- Affects distribution’s confidence in industry’s commitment to LTCI

Source 2002 and 2015 Broker World Surveys

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What Caused the Crash of Traditional LTCI?

Reason 4: High new business premium rates
LTCI premiums have climbed above a middle income price point

![Average Market Premium - 3 Year Benefit Period with BIO](chart)

PA hearing consumer question: “Is LTCI only for the 1%?”

Source: 2002-2015 Broker World Surveys

What Caused the Crash of Traditional LTCI?

- Reason 5: The target market’s generation “turned over”
- We were trying to sell a 30 year-old product to a new crowd
WWII Generation

- Born 1900-1924
- Also called “G.I.” or “Greatest” Generation
- Endured the Great Depression and won World War II
- Value self-sacrifice
- Average of 2.4 children
- Low divorce rate: 20%
- Saved as much as they could
- Believed in traditional insurance products and trusted their agents
- Currently age 91+

The Silent Generation

- Born 1925-1944
- Born into a time of crisis: Great Depression and WWII
- Younger members grew up in the 50s
- Compliant; honored their elders and loyal to old institutions
- Average of 3.3 children
- Wanted a different childhood for their kids
- Learned how to save from parents
- Currently aged 71-91
Baby Boomers

- Born 1945-1964
- Also called the “Me” Generation
- Grew up with, but rejected their parents’ traditional ways
- Average of 2.0 children
- 40%+ divorce rate
- Redefined retirement
- More likely to view insurance products as investments
- Currently aged 51-71

Generation X

- Born 1965-1980
- The MTV Generation
- Grew up during prosperous times
- First generation of divorced parents
- First to use PCs
- Average of 2.0 children
- High rate of single parenting
- “Helicopter Parents”
- Out-earned parents, but saved less
- Don’t believe that Social Security will be there for them
- Currently aged 35-51
**Generation Turnover**

LTCl Issues by Generation and Average Issue Age by Year

Source: 2003-2011 SOA Long Term Care Intercompany Experience Study and AHIP: Who Buys Long-Term Care Insurance in 2010-2011

**Buyer Statistics**

- Lower Issue age in 2010
- Baby Boomers working longer than the Silent Generation

Source: AHIP: Who Buys Long-Term Care Insurance in 2010-2011
Buyer Statistics

Income of Individual LTCI Buyers

- Inflation partially accounts for shift (71%)
- Rest likely driven by big drop in retiree purchasers

Source: AHIP: Who Buys Long-Term Care Insurance in 2010-2011

Buyer Statistics

Education Level of Individual LTCI Buyers

Boomers are more likely than Silents to have college degrees

Source: AHIP: Who Buys Long-Term Care Insurance in 2010-2011
Buyer Statistics

Reason for Buying LTCI

Motivations shifted to preserving assets and lifestyle

Source: AHIP: Who Buys Long-Term Care Insurance in 2010-2011

Transition to Hybrid Products

New Premium by Calendar Year ($millions)

- Shift to hybrids correlates to shift to Boomers as purchasers
- Important to note that much of hybrid premium is single pay

Sources: 2001-2014 Broker World Surveys and LIMRA’s Individual Life Combo Products Annual Reviews
Hybrid Product Sales

Hybrid products comprised 12% of new life insurance premium issued in 2014.

100,000 policies and $2.4 bn issued in 2014

Compared to 130,000 policies and $330m in the Traditional LTC market.

Carriers are entering the hybrid LTC market as opposed to continued exits in the Traditional LTC market.

Hybrid Product Appeal

Customers:
- Easy to understand: Access to a pot of money (death benefit)
- Cost effective: Add-on premiums are generally less than stand-alone
- Equity exists in base product’s account value

Carriers:
- Mitigated risks:
  - Exposure limited to life policy net amount at risk
  - Insured's equity in base coverage acts like a "co-pay"
  - Low mortality offsets life insurance risk
- Easy to distribute:
  - “Add-on” to the base policy sale; can be sold by broad distribution
Are Hybrids the Answer?
Still gaps that can be filled…

Customers:
- Not always interested in combining with life insurance
- Simplified purchase
- Modular solutions
- Flexibility of benefits as care delivery evolves

Carriers:
- “Better box” or eliminate long-term environmental risks:
  - Interest rates
  - Declining mortality rates
  - Disability incidence
  - Evolving care delivery

Future Changes in Care Delivery
Who Will Need LTC & Available Resources

- Generation receiving care will start to flip to Baby Boomers
- Ratio of caregivers to care receivers will drop dramatically
- Both will drive changes in care delivery

Source: US Census Bureau 2015 Projection Population
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Generational Comparison – Baby Boomers

- **Life Expectancy at Birth**
  - Silents: 56
  - Boomers: 68
  - Gen X: 71
  - Mills: 73

- **Health Risks by Generation**
  - Hypertension
  - Hypercholesterolemia
  - Diabetes
  - Obesity

Boomers will live longer, but are generally less healthy

Source: CDC National Center for Health Statistics and The Journal of the American Medical Association

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Current Care Landscape

- **Who:**
  - Recipients: Silents
  - Informal caregivers: Boomers
  - Formal caregivers: GenXers
- **Generational dynamic:**
  - Silents accept how things are
  - Do not want to burden children
  - Children are busy and mobile
  - Will endure social isolation
  - Low tech, inefficient health system
- **Where:**
  - At home
  - Assisted living facilities
  - Nursing homes

Emerging Care Landscape

- **Who:**
  - Recipients: Boomers
  - Informal caregivers: GenXers
  - Formal caregivers: Millennials
- **Generational dynamic:**
  - Boomers will demand change
  - Will not expect help from children
  - Will not tolerate isolation
  - Will want to keep their toys
- **Not “Where” but “How”:**
  - Emerging tech deployed
  - At home via “smart homes”
  - More efficient, less labor intensive
  - Lifestyle preservation “places”
  - Amenities, mobility, social interaction
What are We Trying to Insure?

A closer look at persons that need care….

• Averages for persons aged 80+
  – Net worth: $275,000 including $135,000 of home equity
  – Annual income: $22,000
• Average annual nursing home cost: $81,000
• Average income shortfall ~ $60,000
• Average time to exhaust assets:
  – Out of cash in about 2 years
  – Burn through home equity in another 2 years
• Many panic and begin Medicaid planning

Isn’t this really a lifestyle preservation risk?

What if We Focus on Lifestyle Preservation?

At the point of needing care…

• Care Annuity (UK version of LTC insurance)
  – Underwritten SPIA issued to newly disabled persons
  – Health conditions result in higher monthly benefit payments than traditional SPIAs
    • 2 year life expectancy for nursing home entrants
    • $120,000 gets you $60,000 per year for life instead of $12,000
  – Removes longevity risk for the annuitant
  – Means that people just need to have enough assets to fund an average stay for persons with similar health conditions
  – Most 80+ year-olds have enough assets to do this

Two U.S. carriers currently sell this product
What if We Really Changed Our Thinking?

From selling pre-defined benefits to contribution-based products?

- Deferred annuities that are designated to fund Care Annuities
  - Lump sums or periodic deposits
- Simple, modular and flexible for the customer
  - Put in what you can when you can
  - Stop whenever you want; if you don’t use it, you keep it
- Elimination of long-term environmental risks for the carrier
  - Only need to price for longevity of cohorts as they become disabled

If we could only change some laws…

- Pre-tax contributions that are not taxed if used for LTC?
- “Term LTC” insurance while account builds up?
- Lever-up account balance if LTC is needed?

Signs of Hope

- Regulators / legislatures are receptive
  - Increased understanding of legacy block issues
  - Increasing pressure to solve the Medicaid LTC crisis
  - Understand the need for new solutions
  - Asking for industry input: What laws should we change?
- Carriers are evaluating market entry (and re-entry)
  - See an opportunity for an "against the grain" play
  - Want to sell a new value proposition
  - Looking for ways to distribute new product concepts
- Will someone from outside the industry leapfrog us?