Southeastern Regulators Association Conference

Long-Term Care Session

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Qualifications and Limitations

- The information contained in this presentation is for discussion purposes only and should not to be relied on by its recipients
- The data contained in this presentation are for illustrative purposes only. Actual results for any specific situation might differ
- This presentation is intended for state regulators attending the 2013 Southeastern Regulators Association Conference

Long-Term Care is a Complex Product

- Pricing is on a lifetime basis (level premium, increasing age curve), and major factors affect the rates:
  - Morbidity - made up of: frequency (probability of starting a claim), continuance curves (probability of person staying on claim – determines length of claim), and utilization (average cost per service and number/mix of services)
  - Lapse and mortality – determines how many people get to durations when claims are high
  - Investment income – determines how much money is made on large reserves that are accumulating
- For all companies – lapse, mortality, and investment income have been declining in recent years

Is LTC An Insurable Risk?

- Uninsurable risk – where money trades hands and/or risk is completely unpredictable (e.g., Medicare Part B deductible)
- LTC is a low frequency, high cost event…the very definition of an insurable event
- Milliman studies indicate that around 50 percent of insureds who qualify for an LTC policy and hold onto their policies will have a claimable event at some point in their lives (percent varies significantly by age, gender, marital status, etc.)
- For someone to self-insure, significant asset build-up would be needed
- LTC is an insurable event, though it's very complex to price
- Alternatives?

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Top Individual Writers

2004 Top Writers

Rank	Company	Production ($millions)
1	Genworth	153
2	John Hancock	114
3	MetLife	86
4	Bankers L&C	62
5	MassMutual	25
6	Allianz	24
7	UNUM	20
8	Lincoln Benefit	19
9	Prudential	19
10	Penn Treaty	18
11	New York Life	18
12	State Farm	15
13	Physicians Mutual	13
14	MedAmerica	11
15	Mutual of Omaha	9
16	Equitable L&C	8
17	State Life	8
18	Knights of Columbus	4
19	Kanawha	4
20	AFLAC	3

2012 Top Writers

Rank	Company	Production ($millions)
1	Genworth	221
2	Northwestern	118
3	Mutual of Omaha/United	52
4	MassMutual	29
5	John Hancock	27
6	New York Life	26
7	Transamerica	21
8	Bankers Life & Casualty	17
9	State Farm	13
10	MedAmerica	10

Source: Broker World Surveys

Changes in Carrier Landscape

Out of market since 2004:

MetLife

Allianz

UNUM

Lincoln Benefit

Penn Treaty

Physicians Mutual

Equitable L&C

State Life

Kanawha

AFLAC

Newly departed:

Prudential

CUNA Mutual

AIG

American Fidelity

Berkshire

American General

Humana

Physicians Mutual

Back in the market:

- Thrivent
- Aegon

Source: Broker World Surveys

What Has Caused the Turmoil?

- Lapse rates—very low, less than 1%
- Interest rates—very low, 3% to 4% new money
- Mortality—extremely low
- Morbidity—claims quite close for some, very high for others

2012 Sales Characteristics

- Estimated 2012 sales: $564.6 million premium, 233,222 policies; 5% increase in premium and 1% increase in policies over 2011
- Top two insurers wrote 60% of the business
- Significant rate increases and discontinuance of some features/options
- Introduction of gender-based rates; Four planned for 2013 with others considering this introduction
- Average premium was $2,445
- Most sales were comprehensive, TQ, reimbursement

Source: 2013 Broker World Survey

2012 Sales Characteristics (cont.)

- Average issue age 56.3 (vs. 61.3 in 2004)
- 56.2% compound, inflation protection, 6.8% simple inflation, 20.3% future purchase option, 6.6% other, 9.9% no inflation
- 19.9% lifetime benefit period (up from 12.7% in 2012-due to one carrier, but down from 32.2% in 2004)
- 92.2% 84+ day elimination period (up from 12.7% in 2012-due to one carrier, but down from 32.2% in 2004
- 10.7% of new premium in multi-life situations (excluding AARP)

Source: 2013 Broker World Survey

Policy Features With Most Risk

- Lifetime benefit period
- Short elimination periods
- Cash benefits
- Compound inflation, due to greater build-up of reserves and therefore susceptibility to investment income and low lapses

Economics of LTCI

- Lifetime loss ratio target of 55 percent – 60 percent:
  - Level issue-age premium
  - Steep morbidity curve – similar to mortality
  - Deferred benefit – very low loss ratios for many years
- Heaped commissions
  - First year cash flow drain

Economics of LTCI (cont.)

- Low lapse rates
- Conservative statutory reserve standards (revised in 2004)
- Significant risk-based capital requirements (RBC)
- Commissions, reserves, and RBC all lead to early duration statutory surplus strain

Illustrative Example
Base Assumptions - Expected Durational Profits
20 Percent Profit Premiums – All Ages Combined

Item	No Inflation – Policy Year					
	1	2	3	4	10	Lifetime @ 5.25%
Premiums	100.0	100.0	100.0	100.0	100.0	100.0%
Investment Income	(0.9)	4.1	7.1	10.2	30.4	29.0
TOTAL	99.1	104.1	107.1	110.2	130.4	129.0
Claims Incurred	5.1	9.2	12.6	15.8	42.9	46.0*
Δ Additional Reserves	0.0	52.0	49.8	48.7	38.4	23.7
Commissions	104.3	14.9	14.9	14.8	14.5	21.9
Expenses	24.5	11.6	11.9	12.4	15.6	17.4
TOTAL	133.9	87.7	89.2	91.7	111.3	109.0
Pre-Tax Profit	-34.7	16.4	17.9	18.5	19.1	20.0%

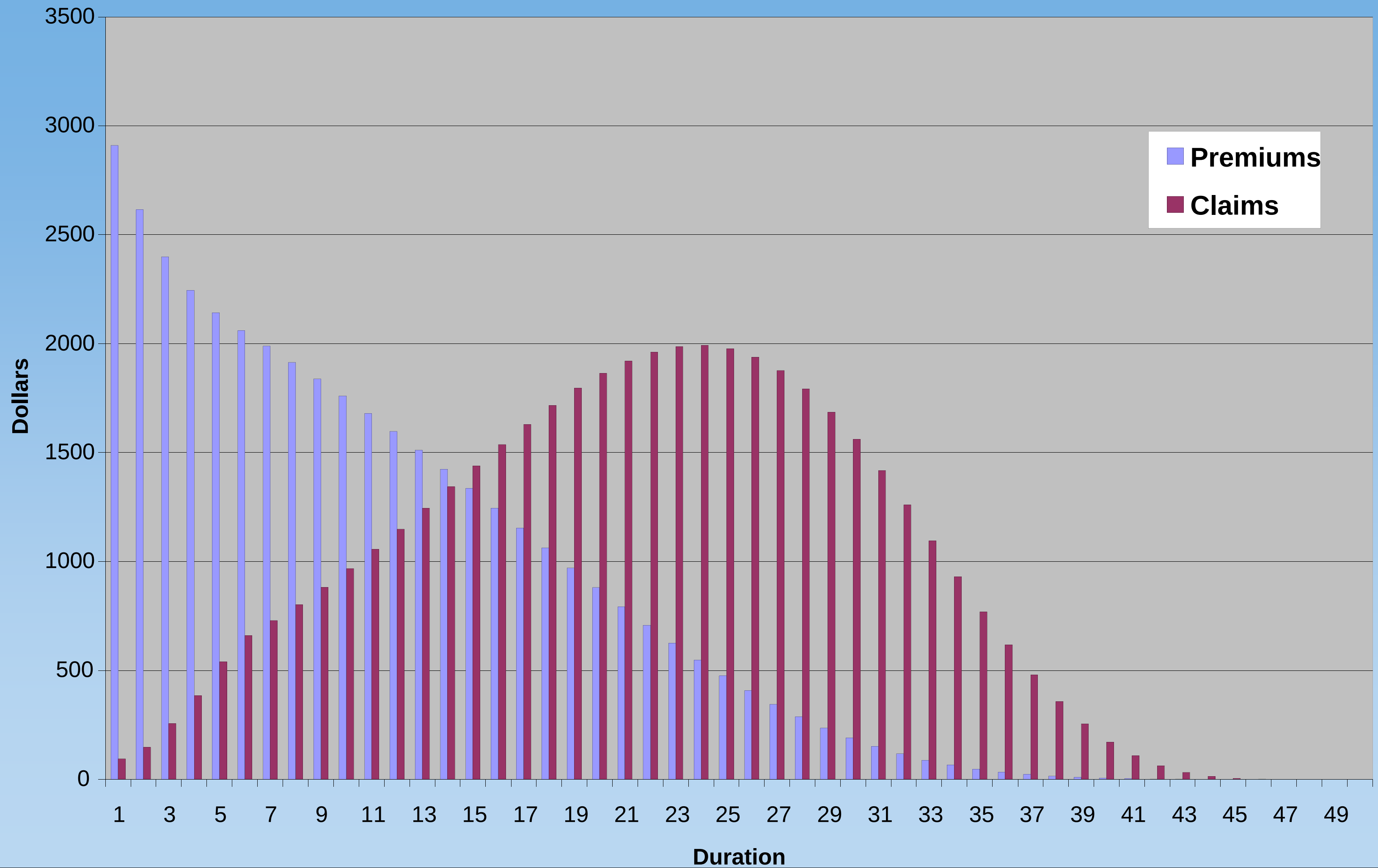
*** 51.3% discounted at 4.0%.**

Illustrative Example
Base Assumptions - Expected Durational Profits
20 percent Profit Premiums – All Ages Combined

Item	With Inflation – Policy Year					
	1	2	3	4	10	Lifetime @ 5.25%
Premiums Investment Income	100.0 (0.5) 99.5	100.0 4.1 104.1	100.0 8.8 108.8	100.0 13.6 113.6	100.0 48.6 148.6	100.0% 73.6 173.6
Claims Incurred Δ Additional Reserves Commissions Expenses TOTAL	1.0 0.0 104.9 17.5 123.4	2.0 83.5 15.0 8.9 109.3	2.9 84.0 15.0 9.0 110.9	3.8 86.2 15.0 9.2 114.2	13.2 109.9 14.9 10.3 148.4	53.8 67.2 19.5 13.1 153.6
Pre-Tax Profit	-23.9	-5.2	-2.1	-0.6	0.3	20.0%

* 67.2% discounted at 4.0%.

LTC Insurance Sample Premiums and Claims



Lapse Rate Trends
Pricing Assumptions – Age 65-69

Early Policy Generations			
Policy Year	Company A	Company B	Company C
1	18%	20%	40%
2	14	15	20
3	10	10	8
4	7	8	8
5+	7	6	8

Source: Internal Milliman Study

Recent Lapse Experience

Policy Year	Company D	Company E	Company F	Company G
1	2.0%	4.0%	7.0%	6.5%
2	1.5	2.5	4.2	4.5
3	1.0	2.0	2.7	3.5
4	1.0	1.5	2.1	2.5
5	1.0	1.5	2.0	1.5
6+	1.0	1.0	1.5	1.5

Source: Internal Milliman Study

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Effect of Termination Rates on Number of Insureds Inforce

Beginning of Policy Year	Original Pricing*	Revised**
0	**1000**	**1000**
6	**498**	**865**
11	**365**	**822**
16	**268**	**782**
21	**197**	**744**

* Original total terminations = 20%, 15%, 10%, 8%, 6%

** Revised total terminations = 5%, 3.2%, 2.2%, 1.6%, 1.3%, 1.0%

Source: Internal Milliman Study

Illustrative Example
Effect of Lower Lapse Rates

	Priced Lapses	Revised Lapses
Year 1	**8.0%**	**5.0%**
Year 2	**5.0**	**3.2**
Year 3	**3.5**	**2.2**
Year 4	**2.5**	**1.6**
Year 5	**2.0**	**1.3**
Years 6+	**1.5**	**1.0**

Source: Internal Milliman Study

Illustrative Example
Effect of Lower Lapse Rates

Item (as a percent of premium)	Age 52	Age 62	Age 72	Total
Pre-Tax Profit (No Inflation)	**17.5**	**18.3**	**19.5**	**18.5%**
Premium Change Needed	**4.2**	**3.1**	**1.1**	**2.8%**
Pre-Tax Profit (With Inflation)	**15.3**	**17.2**	**19.0**	**15.4%**
Premium Change Needed	**8.0**	**5.0**	**2.0**	**7.8%**

Source: Internal Milliman Study

Illustrative Example
Effect of Change in Investment Income

Revised Investment Income Rate = 4.25% (Down 100bp)	Item (as a percent of premium)	Age 52	Age 62	Age 72	Total
	Pre-Tax Profit (No Inflation)	**13.7**	**15.3**	**17.6**	**15.6%**
	Premium Change Needed	**10.8**	**8.5**	**5.0**	**8.1%**
	Pre-Tax Profit (With Inflation)	**9.2**	**13.2**	**16.8**	**9.6%**
	Premium Change Needed	**18.3**	**12.3**	**6.7**	**18.0%**

Source: Internal Milliman Study

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Illustrative Example
Effect of Loose Underwriting*

Item (as percent of premium)	Age 52	Age 62	Age 72	Total
Pre-Tax Profit (No Inflation)	**5.8**	**4.5**	**5.8**	**5.7%**
Premium Change Needed	**24.4**	**28.3**	**30.3**	**27.2%**
Pre-Tax Profit (With Inflation)	**4.9**	**5.3**	**7.8**	**5.1%**
Premium Change Needed	**25.9**	**26.8**	**26.1**	**25.9%**

* Assuming "moderate" was priced for

Source: Internal Milliman Study

Example of Lifetime Pricing Effect for Sample Company

- Original pricing done 15 years ago (1997)
- Original investment earnings rate = 6.9 percent
- Current investment earnings rate = 4.5 percent
- Original ultimate lapse rate = 4.75 percent
- Current ultimate lapse rate = 1.0 percent
- Morbidity 10 percent higher than originally assumed

Source: Internal Milliman Study

Effect of Revised Assumptions on Lifetime Profits

Age Band	Original Pre-tax Profit % of Premium @ 6.9%	Original Statutory IRR	Revised Pre-tax Profit % of Premium @ 4.5%	Revised Statutory IRR
55-59	**31.8%**	**15.2%**	**-32.3%**	**-0.5%**
65-69	**21.2%**	**15.0%**	**-20.5%**	**-2.3%**
75-79	**13.2%**	**14.4%**	**-7.0%**	**-1.6%**
All	**25.1%**	**15.1%**	**-24.8%**	**-0.9%**
Cumulative loss ratio through 15 durations, at ii rate	**24.9%**		**33.2%**	
Lifetime loss ratio at 4.0%	**62.3%**		**104.6%**	

Source: Internal Milliman Study

Illustrative Example
Other Factors Affecting Profits

- Male/female split assumed and/or where it's applied
- Age distribution
- Distribution by benefit period (BP) and/or EP
- Percent of insureds that are married
- Spouse and/or preferred risk discounts
- Average policy size
- Expenses varying by age
- Reserve assumptions
- Margins for adverse deviation
- Salvage on maximum benefits

Source: Internal Milliman Study

Why the Turmoil?

Based on Companies leaving the market:

- Lapse rates, interest rates, & mortality: low
- Morbidity - claims quite close to pricing for some, very far off for others (depending on aggressiveness of original pricing and on underwriting)
- Concerns about profitability and being able to get rate increases
- Felt that capital was better invested elsewhere (would yield more immediate results)

Why the Turmoil? (cont.)

Based on Producer concerns:

- Rate increases and fewer company choices
- Product complexity
- Rates on new products 40%+ above levels available five years ago

LIMRA 2012 LTC Opinion Survey

- 47 percent out of 83 people expect strong to moderate growth going forward
- 75 percent projected strong to moderate growth for life combos and 66 percent for annuity combos
- Demographics, greater consumer awareness and need for the product are biggest reasons for optimism
- Industry stability and the economy (interest rates) are biggest reasons for pessimism
- 75 percent believe Medicare and Medicaid will NOT offer more benefits in next 20 years
- To increase the market, the products need to be made more affordable and simplified

Summary

- Premiums have increased, due in part to updated lapse assumptions and interest
- Rates have stabilized, but there are still significant differences in market premiums
- Product is capital intensive and still relatively risky
- But…demographics are hard to ignore, companies will likely enter/stay in the market accordingly
- So is there a better way to address the need?

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