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# **Pension Protection Act & LTC Combo Products**

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# Discussion Overview

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- **LTC background**
- **Traditional LTCL history / problems**
- **Combo product overview**
- **Pension Protection Act**
- **Recent design trend**
- **Combo product appeal**

# What is Long-Term Care?

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- **Services and care provided to people with a chronic illness or disability**
- **Commonly assists people with activities of daily living (e.g. dressing, bathing, eating, transferring and toileting)**
- **Provided at home, in the community, in assisted living or in nursing homes**
- **Provided to people of all ages**

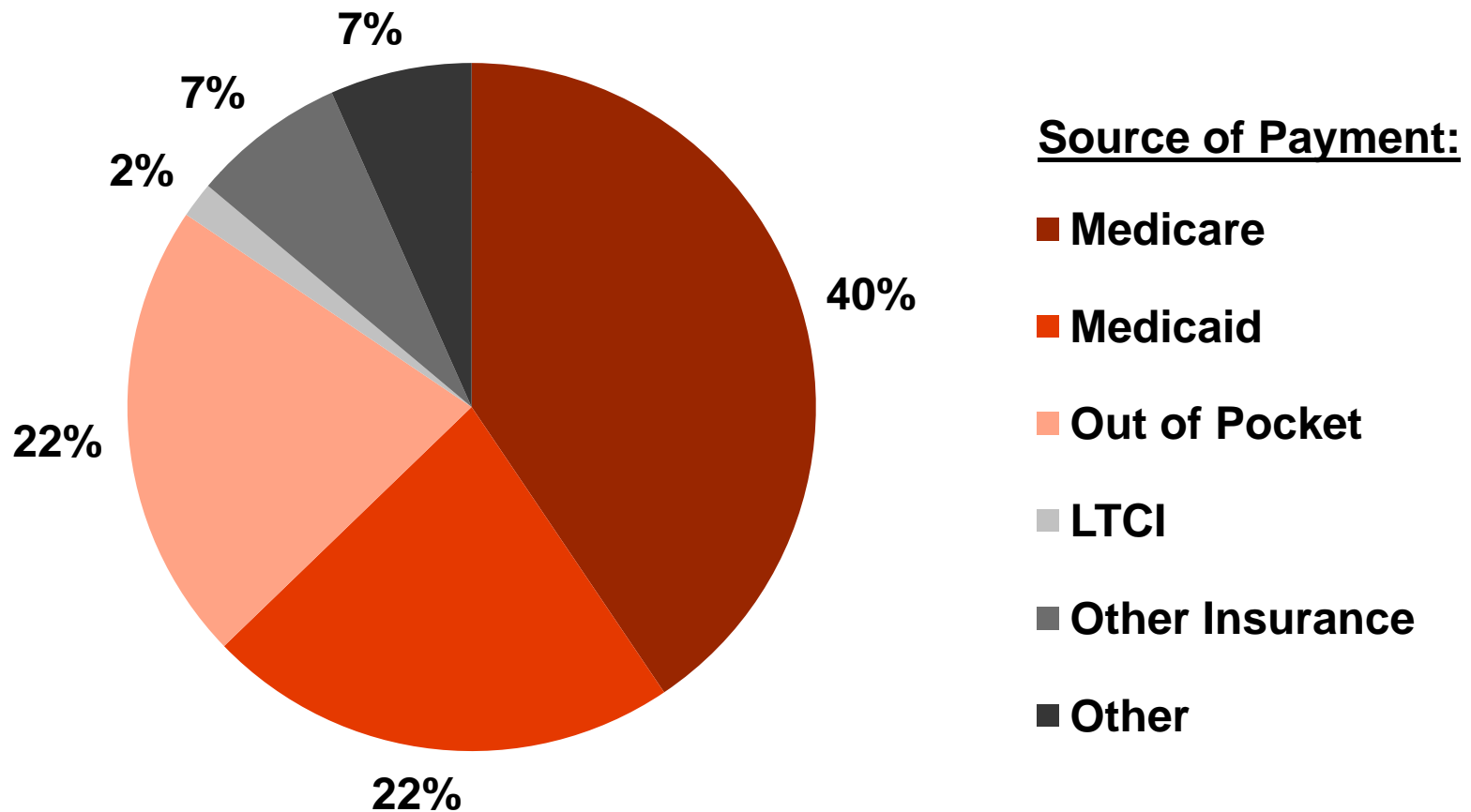
# Average Costs

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- **2009 MetLife Survey Results:**
- **Nursing Homes: \$219/day or \$80,000/yr**
- **Assisted Living Facilities: \$3,130/mo or \$38,000/yr**
- **Home Health Care: \$21/hr or \$26,000/yr**

# Who Pays for Care?

2006 LTC Expenditures Totaled \$180 Billion



# Traditional LTCL Design

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- **Similar to disability income plans:**
- **Benefit trigger is disability threshold**
  - 2+ ADLs or cognitive impairment
  - Common to require LTC services received
- **Fixed or maximum daily benefit**
- **Benefit period, elimination period**
- **Eligibility language, underwriting and claims adjudication have evolved tremendously**

# Traditional LTCL Pricing

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- **Issue age rated / guaranteed renewable**
- **Very steep morbidity curve – similar to mortality**
- **Very cash flow positive early on, changing to very cash flow negative in later years**
- **Large policy reserves and RBC**
- **Sensitive to interest and lapse rates**

# Traditional LTCl Complexity

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- **Requires specialized talent in all areas**
- **Administration**
- **Technology platform**
- **Product management**
- **Distribution system!**
  - **Access to / creation of LTCl specialists**
  - **Of 150+ carriers that entered, top 10 always had ~80% market share**



# The Complex LTCI Sale

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- **Traditional LTCI sale is multi-step:**
- **Usually takes several hours**
- **Educate customer on need for coverage**
- **Explain product and choose options**
- **Very expensive, especially older ages**
- **Highly specialized distribution required**

# Traditional LTCl Sales

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- **Steady decrease in sales during 2000's**
- **Minor increases in sales in middle of decade due to federal employee program**
- **Contrary to increasing size of target market**
  - **Baby Boomers entered target age market of 55-69**

# Drivers of LTCL Sales Decrease

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- **Rate increases on older business**
  - Missed pricing assumptions
  - Plan design flaws
  - Underwriting and claim process flaws
- **Increased regulation**
  - Resulted from rate increases
- **Drove new business premium higher**
  - Conservative pricing mandated

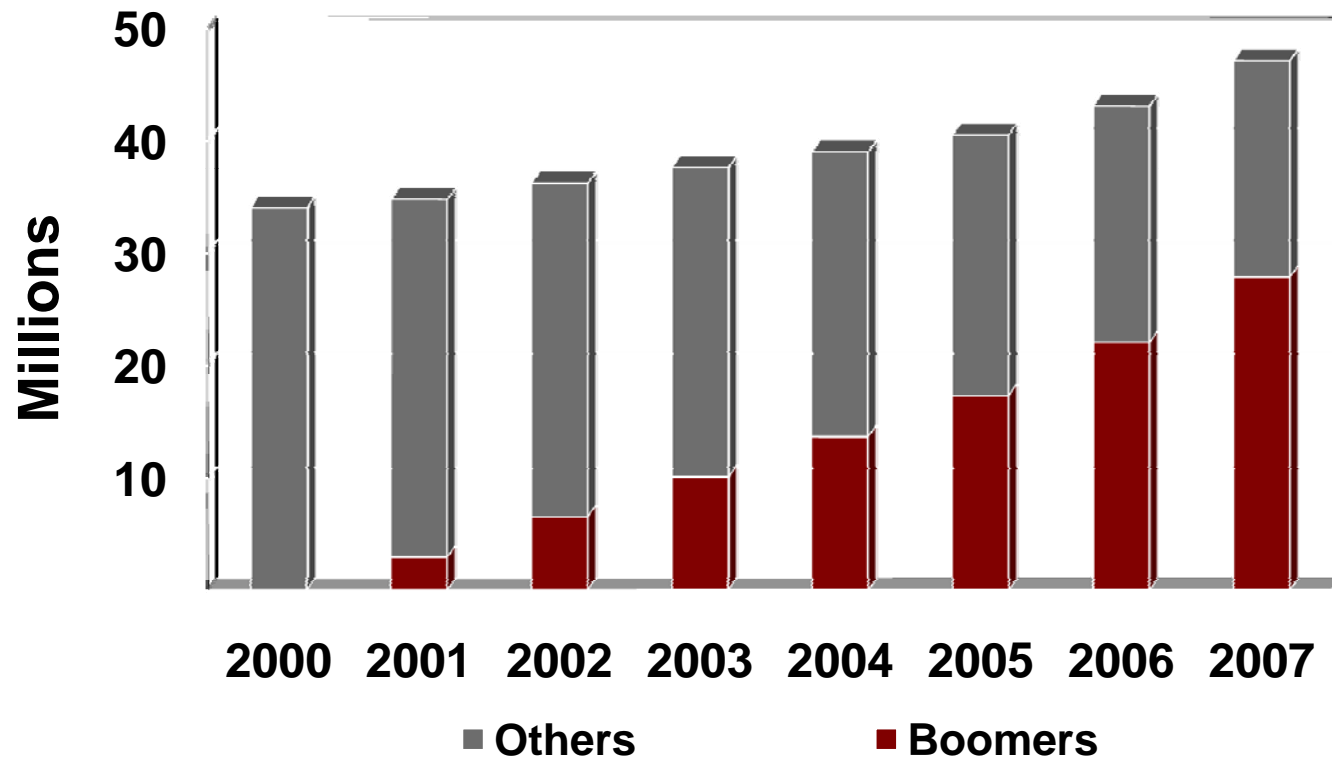
# Drivers of LTCl Sales Decrease

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- **Higher new business premiums led to:**
- **Decreased production**
  - Shrinking specialist distribution
- **Carrier exits**
  - Decreased production
  - Fear of risk
- **Not to be discounted:**
- **Attitudes of changing target market**

# Changing Target Market

## Population Aged 55-69



Source: U.S. Census Bureau



# Baby Boomer Attitudes

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- **Less risk averse than parents**
- **Wealth transfer is not the primary goal**
- **Less patience - need simpler sales**
- **Want a product they can “cash out” from**
- **Old product and distribution don't work**

# LTC Combos Offer Hope

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- **Many traditional LTCL barriers don't exist**
- **2006 Pension Protection Act clarified taxation**
- **Seeing new entrants instead of exits**
- **Potential to overtake traditional LTCL in a short amount of time**

# What Are LTC Combos?

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- **Combine elements of non-LTC and LTC**
- **LTC is typically viewed as the “add-on”**
- **Not a new concept – dates to early 90s**
- **Had taken a back seat – but changing**



# Types of Combo Products

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- **Life Insurance Benefit Acceleration**
- **Deferred Annuity / LTCL Hybrid**
- **Immediate Annuity / LTCL Hybrid**

# Life Benefit Acceleration

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- **Can be attached to any type of permanent life product**
- **All or a portion of face amount available for LTC benefits**
- **A small percentage (2%-4%) of face available per month until face exhausted**
- **Fixed or maximum monthly basis**

# Life Benefit Acceleration

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- **Must meet eligibility requirements**
  - **Chronic Illness: Unable to perform 2 ADLs or cognitive impairment**
  - **Common to require that QLTC services are being received**
- **Additional premium or account charge**

# Life Benefit Acceleration

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- **Extension of Benefit variation:**
- **More than the policy face is available for LTC**
- **Alternatively, a residual death benefit is provided if entire face is accelerated**
- **Has obvious additional risk**

# Deferred Annuity Combos

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- **Account value (e.g., \$50k) available for LTC benefits**
  - Reduced or no surrender charge
- **Additional LTC benefit (e.g., \$100k) available after account value is exhausted**

# Deferred Annuity Combos

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- **Payment structure similar to life acceleration:**
  - **Small percentage available monthly until maximum benefit is exhausted**
  - **Eligibility triggers similar as well**
- **Additional premium or account charge**

# Immediate Annuity Combos

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- **Base monthly annuity benefit (e.g., \$2,000) starts immediately for life**
- **Increases to a higher benefit (e.g., \$4,000) while LTC eligibility is met**
- **Additional single premium charged at issue**

# Pension Protection Act

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- **Became effective January 1, 2010**
- **Clarifies taxation of premiums and benefits of “Qualified LTC” coverage**
  - QLTC defined in existing code (7702B)
  - When provided on life & annuity policies
  - Regardless of effect on policy values
- **Basically:**
  - QLTC component of policy / rider is considered to be a separate contract



# Pension Protection Act

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- **Premium / charges for QLTC coverage:**
- **Not considered to be an investment in the contract**
- **Not considered to be taxable withdrawals from account balance**
  - **Previously unclear**

# Pension Protection Act

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- **Premium / charges for QLTC coverage:**
- **Not included in premiums that are compared to guideline premium limitations**
  - **Previously only cash value charges were added to the guideline premium limitations**
- **Not counted as medical expenses**
  - **Previously unclear**

# Pension Protection Act

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- **QLTC benefits paid to policyholder:**
  - **Not considered taxable withdrawals from cash values or account balances**
    - **Previously unclear for annuities**
- **Policy exchanges:**
  - **An annuity, endowment, life insurance or QLTC policy can be exchanged for a QLTC or combo product tax-free**
    - **Previously, exchanges to or from LTC not tax-free**

# Pension Protection Act

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- **DAC tax change:**
- **All life and annuity policies with QLTC benefits capitalize at 7.7% of premium**
- **Even if QLTC benefits provided as a rider**
- **Big change for Annuities - were 1.75%**

# LTC Combo Product Appeal

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- **For the Customer:**
- **Easy to understand**
  - **Pot of money vs. daily benefits and benefit periods**
- **Cost effective**
  - **Add-on premiums are generally less than stand-alone premiums**
- **“Equity” exists in base product**

# LTC Combo Product Appeal

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- **For the Distributor:**
- **Easy to sell - does not require specialists**
  - May require training by regulation
- **Sold as an “add-on” to other coverage**
- **Underwriting leverages base policy UW**
  - Life combos may have a supplemental health application
  - Annuities usually have initial waiting periods

# LTC Combo Product Appeal

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- **For the Carrier:**
- **Mitigated risks**
  - Exposure limited to NAR for life ADB
  - Equity in base coverage acts like a “co-pay”
  - Early evidence of lower utilization
- **Existing distribution can sell them**
- **Valuable benefit differentiator**
  - Currently a “nice to have” option
  - Likely to become a “must have”

# Considerations

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- **LTC benefit subject to regulation**
  - **Must meet minimum standards**
    - **NAIC LTCI and NAIC ADB Models**
  - **Additional standards to meet IRS guidelines**
  - **Less requirements than traditional LTC**
- **Knowledge of LTC is required**
  - **Product design, filing and pricing**
  - **Ongoing product management**



# Considerations

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- **Administrative capabilities:**
- **Back office training for LTC claims**
- **Technology alterations for LTC**
  - **Premiums / charges for rider and effects on AVs**
  - **Reserving capabilities for active and disabled lives**
  - **Ability to process claims**
  - **May consider outsourcing**

# Conclusion

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- **Clear need for LTC coverage**
- **Traditional LTCL has not and likely will never penetrate to significant levels**
- **Combo products are a viable alternative**
- **Will likely become a “must have” as they continue to increase momentum**
- **PPA appears to be “greasing the skids”**



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