<u>Answers to a Few LTCI Questions</u>

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In September 2010, I sent a list of 10 questions to several agents and insurers regarding LTCI. One agent immediately commented, “Great questions,” but I’m not so sure his insurer agreed. Below are excerpted answers from 3 leading LTCI insurers and 1 agent to a few selected questions. This survey may be expanded or revised in the future, with inclusion of additional insurers, possible amended answers from respondents, etc., so please check back for updates.

1) <u>What is the insurer’s rate of return assumption on policy reserves in pricing the policy? And, what happens if the insurer’s actual rate or return is significantly greater than its assumed rate of return</u>?

Leading LTCI Agent: “Investment assumptions will be different based on company structure: Stock or Mutual. Their anticipated returns should be no different than any other long term conservative investment. Remember these products are designed specifically to pay claims when due. Excess profits based on greater than anticipated investment returns would in theory be reflected in premiums. Although it does not often happen, premiums could go down as well as up.”

Genworth: “This is confidential information.” Ditto for second half of question.

Mass Mutual: “The assumption varies by company and is proprietary. LTC assets are held in an insurer’s general account. You can refer to a particular company’s annual statements to determine the general account rate of return.” Regarding second half of question, “A stock company gives the excess to its stockholders. A mutual company gives the excess to its participating policyholders.”

“Prudential considers this information to be confidential and proprietary.” Regarding second half of question, “This scenario is exceptionally unlikely.”

Breadwinners’ Comment: With respect to the first half of this question, please note that in contrast with the assertions of confidentiality on LTCI policies, these insurers on their whole life policies have always had to disclose the rate of return assumption used in building those policies’ <u>guaranteed</u> reserves.

2) <u>What percent of the actuarial value of premiums get paid out in benefits</u>?

Leading LTC Agent: “Theses products were built, as all individual A&H products are, with a massive 65% loss ratio. However later adopted rider provisions must be 85%.”

Genworth: “I can share that NY regulation mandates a minimum 70% loss ratio. Our NY state filed LTCI products meet or exceed the regulatory requirement.”

Mass Mutual: "Information is not available publicly from the insurer. However information is filed with the various state insurance departments and can be obtained via a freedom of information act request."

"Prudential considers this information confidential and proprietary."

3) What lapse assumptions were used to build the policies you currently market?

Leading LTC Agent: "This has turned out to be the most loved policy ever. Subsequent lapses are less than 2% a year. New products are built on this fact. In the beginning it was assumed they would have the same persistency as past Individual A&H, 88%. This caused serious rate adjustments."

Genworth, Mass Mutual, and Prudential all said information is confidential or not publicly available from the insurer. However, Mass Mutual added, "Information is filed with the various state insurance departments and can be obtained via a freedom of information act request." **Note: Breadwinners'** Insurance is now seeking such.

4) How should the advantages/differences between buying a policy at 50 versus at 60 be explained? Assuming all insurability factors are the same at both ages, what is the difference in premiums expressed as an annual interest rate, that is, as a time value of money? For example, yes the premium for the same coverage will be bigger at 60 than 50, but how much bigger? If it is X%/yr larger, but I earn X+Y%/yr on my investments, am I better buying now or waiting?

Leading LTCI Agent: "You are never better off waiting. Your health can turn an abrupt corner and coverage will no longer be available. Premium will rise dramatically, rule of thumb is they double every 8 to 10 years older. You can never use premium dollars to invest your way out of the risk."

Genworth: "I hope you can appreciate that this question is very hypothetical because insurability factors are not the same at age 50 and age 60. I suggest you play with the rate calculations on the AARP web site www.Genworth.com/AARP. It allows you to obtain quotes and it illustrates "the cost of waiting".

Mass Mutual: "The Illustration system contains a cost of waiting report. Beyond that nothing can be provided to you for client use without being filed and approved by the Department of Insurance."

Prudential: "The cost of waiting illustrations in the premium quotation software can assist in demonstrating the cost of waiting to purchase coverage."

Breadwinners' Comment: All of these answers are, in my judgment, unacceptable. None of the insurers' illustration systems shows anything other than a simplistic comparison of the alternative of buying now versus buying at some future date. The question seeks a financial analysis involving the time value of money. It would seem that it ought to be at least a little embarrassing to life insurers and their agents, so endeavoring to be the preferred financial adviser to America's families, to not only fail to provide the meaningful and valid analysis that consumers deserve but in failing such, set the stage for misrepresentations regarding the cost-advantages of buying immediately.

To state, as the agent wrote, "You are never better off waiting," is to make an exaggeration if not a misrepresentation, like those routinely made by agents selling whole life – a subject analyzed in the Archives article "Be Very Wary of Buy Now to Lock-in a Lower Cost." With LTCI, the question of

whether or not one is better off waiting ought to be readily recognized as an empirical matter dependent upon: 1) the consumer's after-tax rate of return on possible investments, 2) the annual percentage increase in LTCI premiums, and 3) possible changes in LTCI premiums due to insurer costs, restructuring of product, etc. Breadwinners' preliminary analysis shows that if the consumers' after-tax ROR is equal to the annual percentage increase in LTCI premiums then the financial advantage in buying early is non-existent. For example, if LTCI policy premium structures change in the future to widely accommodate additional lump sum payments, then, aside from: 1) LTCI premiums' tax deductibility and 2) loading charges- which could and, I believe, will be reduced in the future, a consumer who can grow his funds faster than an LTC insurer grows its reserves will find waiting to buy advantageous as long as his/her health did not change to impact insurability.

Admittedly, the current insurance sales environment does not readily accommodate agents instantly, perfectly, and completely analyzing every personal financial decision for consumer. But for such a general or typical question as this, the LTCI industry ought to have a rigorously documented analysis; time permitting, I might mathematically analyze this advice, possibly thoroughly debunking and discrediting it, much as I have done regarding the industry's specious advice about the costs of waiting to buy a whole life policy. However, at present, in allowing agents to simplistically advise consumers that "You are never better off waiting" (advice that: 1) is, again, not currently properly supported with any insurer's valid financial analysis, 2) is possibly biased by a commission compensated agent's interest in making the sale immediately, and 3) masquerades as unequivocal and definitive, would seem, at the very least, to be a matter warranting much greater industry study.) Indeed, LTC insurers could well have opened the door to litigation from policyholders, especially those who because of financial difficulties lapsed their policies. If such were to occur, it would be more than a little ironic, because from those whom the insurer expected to obtain a subsidy, it could owe a settlement! Oops.

The End.