

# 2016 Chicago Actuarial Association

**March 23, 2016**

**Life and Annuity Living Benefits: SOA Research Results, and Recent Developments**

**Carl Friedrich, FSA, MAAA  
Consulting Actuary & Principal  
Milliman, Inc.**



# 2015 Society of Actuaries Report on Life and Annuity Living Benefit Riders: Considerations for Insurers and Reinsurers

- SOA research report by Milliman on a wide range of living benefit riders with medically related triggers on life or annuity products, including a survey with responses from 34 direct writers covering 83 different living benefit plans, and interviews with 8 reinsurers

Benefit	Number of Riders	Benefit	Number of Riders
Chronic Illness	23	Terminal illness	35
Life linked benefits	8	Critical illness	3
LTC accelerated benefits	8	Annuity linked benefits	6

# Model Regulation 620 Plans

- Acceleration of life insurance benefits under conditions prescribed by a rider
  - Four allowable “qualifying events” identified under the Model, which include clauses commonly used to define terminal illness, critical illness, or older forms of chronic illness (specifically, permanent confinement in an eligible institution)
  - A fifth clause allowing for any other definition approved by the commissioner, which has allowed a more modern form of chronic illness trigger that is tied to the Internal Revenue Code (IRC) section 7702B definition of a chronically ill individual (2 of 6 ADL’s or cognitive impairment), often with an expectation of permanence requirement
  - Tax treatment under chronic illness and terminal illness designs covered under Section 101(g) of the IRC

# Model Regulation 620 Plans

- Other Model Reg provisions
  - Lump sum payout option required, commonly interpreted by regulators as annual lump sum, but not in all states
  - No restriction on use of proceeds
  - May not be marketed as LTCI
  - Pricing methods include a dollar for dollar death benefit reduction approach with upfront charges, a discounted death benefit approach, and the lien approach
  - Various filing and disclosure requirements
  - Prescribed limits on interest discounts used under discounted DB approach, and on lien interest rates

# Interstate Insurance Product Regulation Commission

- Includes a Standard for Accelerated Death Benefits
- Updated Standard effective 12/2014

## Variations from Model Reg

Terminal illness must be included if any other type of acceleration is sold

Previously included an expectation of permanence requirement, but that provision is now allowed but no longer required under the updated Standard

Incidental test requirement, where the premiums and present value of benefits of the rider must be no more than 10% of the corresponding base plan values for the product in aggregate

# Direct Writer Survey - Chronic Illness

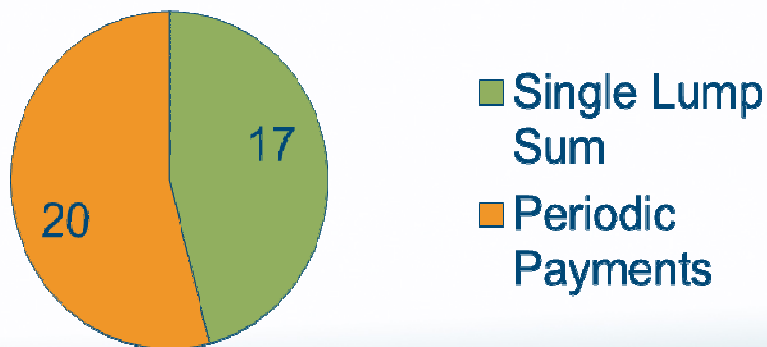
- Sales reported for 21 plans in 2013 were \$1,197M
- Attached to a variety of base plans, with the most common being UL (17), WL (10), IUL (8) and VL (6), and even 2 on term
- Triggers usually include LHCP cert, 2 of 6 ADLs or cognitive impairment, but 7 require permanent nursing home confinement
- 14 of 23 require expectation of permanence

Chronic Illness Approach	# of Companies Using Approach
Lien approach, all charging interest	8
Dollar for dollar DB Reduction (use upfront charges)	6
Discounted DB	9 (2 discount based on underwriting at time of claim, the rest based on age at claim or age and duration since claim)

# Direct Writer Survey – Chronic Illness

- Several state variations of benefit triggers, especially FL and CT
- Five say they do not pay for unbilled services provided by family members
- 12 of 21 allow benefits to exceed HIPAA limits

## Benefit Payments



- Of those offering periodic payments: eight annual, 14 monthly, and others

# Direct Writer Survey – Chronic Illness

- 9 reinsurance deals pay at time of rider claims
  - Three pay on acceleration only on newer business
  - Two pay on acceleration only if 100% of DB is accelerated
- Required inclusion of terminal illness benefit in many states (and per the Interstate Compact)
  - Very low recognition by direct writers of reduced utilization of chronic illness benefits (and lower mortality)
- 14 of 23 filed through the IIPRC
- IIPRC has removed the permanence requirement from their reg (but still allows)
  - But few carriers indicate they expect to modify their triggers



# Reinsurer Interviews – Chronic Illness

- More reinsurers moving to pay benefits at time of rider claim, but various concerns were expressed
- Prior practices included paying their share at time of death based on NAR frozen at time of rider claim, or based on floating NAR between rider claim and death, or not paying at all
  - Can create some disconnects between direct claim amounts and reinsurance amounts paid, but reinsurance amounts should be aligned with charges
- Some pay on surrender after a rider claim
  - “At lapse you have to figure out what to pay, e.g., what if the CV is greater than the accelerated benefit?”

# Reinsurer Interviews – Chronic Illness

- Many inforce treaties do not clearly address the details of the reinsurance premium and payout calculations
- Some reinsurers' underwriters review direct writers' standards to see if there is any need to adjust mortality for anti-selection
- Reinsurers typically rely on the discounting done by the direct writer, but check the calculations before entering a treaty
  - One problem is the discounted value is based on the PV future death benefits - PV direct writer's premiums (not reinsurer's premium)
  - Some reinsurers add an extra charge to their quotes in these cases to account for the disconnect

# Reinsurer Interviews – Chronic Illness

- The IIPRC requires that terminal illness must be included with the chronic illness rider, and this has implications with the discounted death benefit approach
  - Some reinsurers have expressed concerns about pricing implications

## Biggest Concern is the Discounted Death Benefit Method

Market conduct considerations related to low percentage payouts; more of a concern on the direct side, since reinsurers are a little more protected

In the past, very few people have taken a discounted death benefit offer, since the offers have not been viewed as attractive

Some reinsurers question whether chronic illness discounted death benefits are ultimately viable without underwriting at the time of claim

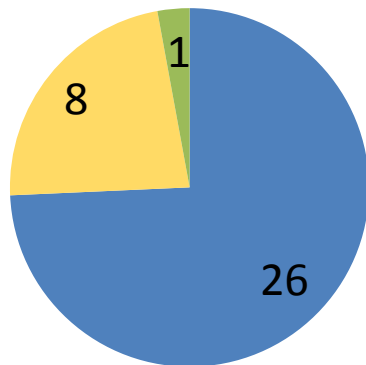
## Reinsurer Interviews – Chronic Illness

- Elimination of the permanence requirement by the IIPRC will cause some reinsurers to be less comfortable with the chronic illness risk
- Some concern about certain riders being issued without what reinsurers consider to be best practice risk controls
- There is a big distinction between riders that charge a premium versus those that don't
  - Companies charging a premium are now viewing this as a way to grow premium, and a way to provide value to the client
- No other meaningful issues identified in other rider categories other than to note that a number of reinsurers are not comfortable with assuming LTCI risks

# Direct Writer Survey - ADB for Terminal Illness

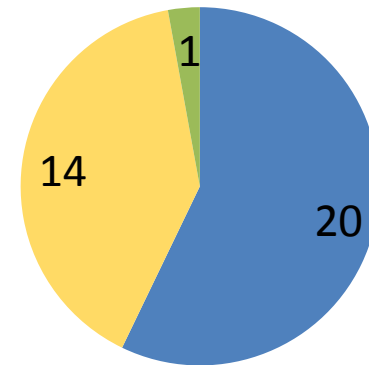
- 25 companies provided responses for 35 plans
- Majority offered on multiple base life insurance product chassis.

**Base Product**



- Single Life Only
- Single Life & Second-to-Die
- Single Life & First-to-Die

**Benefit Payment Approach**



- Discounted Death Benefit
- Lien Approach
- No Response

# Direct Writer Survey - ADB for Critical Illness

- Defined as the occurrence of a medical condition that, in the absence of extensive or extraordinary medical treatment, results in a drastically limited life span, such as cancer or stroke
- 3 participants offer the plan on multiple base product chassis which have recurring premiums, and automatically include it with the base policy
- 2 use the lien approach; 1 the discounted death benefit approach

# Direct Writer Survey - ADB for Critical Illness

## Critical Illness Triggers

Cancer (excluding Skin Cancer)

Heart Attack

Stroke

Organ Transplant

Renal Failure

- Benefit amount does not vary by trigger
- Benefit paid as a lump sum payment
- Multiple benefits due to multiple triggers
- No re-occurrence benefit
- No explicit charge
- 2 of 3 assess an administrative charge when death benefits accelerated

## LTCL Riders: Part 1, LTC ADB only

- Riders to address long term care needs may be attached to a range of life products
- Not governed by Model Reg 620, but rather Model Reg 641 and Model Act 640 (LTC)

### LTC regulations generally apply, with the following exemptions:

No inflation protection requirement	Loss ratio standards do not apply
No LTC nonforfeiture requirement	No Shopper's Guide requirement
LTC suitability requirements do not apply	No requirements regarding availability of new providers, or rights to reduce coverage and lower premiums



# LTCL Riders: Part 1, LTC ADB only

- Accelerated Death Benefit rider (ADB)
  - Typically pays out a specified portion of Death Benefit per month with a proportionate reduction to Cash Values when traditional LTC triggers are met (2 of 6 ADL's or cognitive impairment)
- Benefit structures include the dollar for dollar death benefit reduction approach, or the lien approach
- Expense reimbursement, indemnity, or disability model designs all allowed (vs chronic illness, which requires a disability model since it Model Reg 620 allows no restrictions on use of proceeds)
- Can qualify as tax qualified LTC under IRC 7702B

## Direct Writer Survey – Life/LTC ADB

- Responses only include plans where an ADB rider is available but no Extension of Benefit rider is available
- Sales reported for 8 plans in 2013 were \$239M
- 53% of sales were for an approximate 2 year ADB period
- Average issue age was 56
- Most are filed under Section 7702B of the Internal Revenue Code (2 of 10 were filed only under 101g)

## Direct Writer Survey – LTC ADB

- UL is the most common chassis
- 5 of 8 reported use an indemnity structure, 2 use a disability model (under the latter, no formal billable care is required), and one uses expense reimbursement

Several use additional underwriting tools beyond those used in life underwriting including:

Prescription Drug Screen

Supplemental App

Cognitive Screens

Also used by a few:

Pre-screening  
questionnaires

Phone interviews

## Direct Writer Survey – LTC ADB

- A variety of charge structures in use
  - For companies primarily using YRT charges, there are a number of states where level charges are used, but the list of those states vary from company to company
- All eight plans using current and guaranteed LTC charge schedules
- Little impact seen relative to policyholder optionality when rider is attached, although expected profits increase for 5 companies
- Conservation of mortality principle only assumed by 2 of the companies
- Only four of the plans are priced using an integrated rider/base plan approach

# Direct Writer Survey – LTC ADB

- Both active life and disabled life reserves are typically generated for the rider using LTC reserving principles, but methodologies and results vary and are dependent on the charge structure
- Surprisingly, for two of the plans it was reported that only a life license was required
  - For the rest, requirements included both a life license and some form of health or LTC license, with variations by state
  - Responses to the applicability of LTCI training requirements were evenly split
- Six of the eight plans reflect significant filing variations, with the most variations reported for the state of NY

## LTCL Riders: Part 2, Life/LTC or Annuity/LTC

- These include both an accelerated LTC benefit and additional benefits independent of the base plan (“Extension of Benefits” or EOB provisions)
- All LTC regulations apply to EOB provisions/riders
- Various charge structures allowed, typically including YRT or level charges per thousand of NAR on life hybrids, and either level bp charges or per thousand of NAR on annuity combos
- Requirements for offer of 5% compound inflation benefit and LTC nonforfeiture benefit apply
  - Poses some challenges in keeping premium levels within acceptable parameters for some designs (IRC 7702 issues, premiums exceeding \$1000 per unit of life face amount, etc.)

## Direct Writer Survey – Life/ LTC Linked Benefits

- 4 attached to single premium products only, one attached to both single and recurring premium plans, and two attached to recurring premium products only

Life/LTC Linked Benefit Approach	# of Plans Using Approach
Expense Reimbursement	5
Disability/Cash	2
Indemnity	0

- Maximum Lifetime LTC benefit is linked to the life insurance face amount for all 7 plans
- Most plans have a 90 day elimination period that does not need to be consecutive, and that is satisfied once in a lifetime

## Direct Writer Survey – Life/ LTC Linked Benefits

Return of Premium Benefit	# of Plans
100% ROP	4
90% (2 years), 100% (years 3+)	1
80% OR 80% grading to 100%	1
None	1

Inflation Protection %	Simple Interest	Compound Interest	# of Plans
3%	X		4
5%	X		2
3%		X	2
5%		X	6



## Direct Writer Survey – Life/ LTC Linked Benefits

- All 7 plans include nonforfeiture option in the base coverage, rather than offer as an optional benefit
- For most plans, the base plan and rider compensation are intertwined, with separable commissionable target premiums defined for the base plan and riders
- 4 of the 7 plans use in-house underwriters to underwrite the benefit
  - Majority of the plans (6 of 7) link the LTC underwriting classes to the life underwriting classes
- 5 of the 7 plans use in-house claims administration
  - Claims experience from 2010 through 2013 has been close to or better than expected for all plans
- 3 life/LTC linked benefit plans are reinsured: YRT (2), Coinsurance (1)
  - Reinsurer pays share of benefits at time of claim

## Direct Writer Survey – Life/ LTC Linked Benefits

- Most calculate a separate additional active life reserve for the ADB, EBR, and IPR using standard LTC reserving methods
- When the insured is receiving LTC benefits, most plans hold an additional disabled life reserve for the ADB, EBR, and IPR calculated using standard LTC claim reserving methods

# Direct Writer Survey - Annuity/LTC Linked Benefit

- Basic designs
  - Pot of money (2) – LTC lifetime benefit is a fixed multiple of initial premium
  - Tail design (2) – LTC lifetime benefit is a fixed multiple of AV at time of claim, claims paid first from AV
  - Coinsurance (0) – As tail, but monthly benefits come partly from AV and partly from insurance until AV used up
- Target markets are those seeking insurance and tax leverage on funds to cover LTC needs
- Sales reported for 6 plans in 2013 were \$320M
  - Authors have information indicating 2014 sales are likely over \$500M

## Direct Writer Survey - Annuity/LTC Linked Benefit

Base plan chassis	Number of plans
Book Value Annuity	3
Market Value Adjusted Annuity	2
Variable Annuity	1

Premium for base	Number of plans
Single Premium	4
Recurring Premium	1 (very limited renewals)

## Direct Writer Survey - Annuity/LTC Linked Benefit

Benefit Structure	Number of plans
Expense Reimbursement	3
Indemnity	2

Maturity Provision for LTC	Number of plans
Policyholder can extend maturity date by one year on a year by year basis	2
Ends at base plan maturity date	2
LTC paid up at base plan maturity date	1

## Direct Writer Survey - Annuity/LTC Linked Benefit

Underwriting	Number of plans
Supplemental or expanded app	5
Prescription Drug DB screen	4
PHI	3
Cognitive screen	3
Face to face exam	2
Medical records	1

## Direct Writer Survey - Annuity/LTC Linked Benefit

- LTC ADB/ EBR charge structure
  - Charges based on level bps assessed against AV (2)
  - Charges based on COI assessed against NAR (1)
  - Charge against the remaining guaranteed amount (2)
  - All charge structures are currently unisex
- Only one plan is reinsured (coinsurance)

# **Annuity Enhanced Payout Benefits Triggered by a Health Condition**

- Not clear what NAIC Regulations apply
- Often treated as an incidental benefit
- Interstate Compact has no Standards applicable and will not currently approve
- Despite being a feature offered by more than a few in the market, no direct writers responded to the survey questions for this product



# Summary of Life & Annuity Living Benefits: Considerations for Insurers and Reinsurers

- Widespread interest and participation by both direct writers and reinsurers on the topic
- A wide variety of regulations may apply, and regulatory standards have evolved as these products have emerged
- Reinsurers are working more with direct writers to provide complete reinsurance mechanisms to support this business
- Sales information gathered from the survey was fragmented
  - From data gathered for 2013, plus other sources, the authors estimate chronic illness sales (total policy premium) to be \$1.2B in first year premium, sales with LTCI riders to life to be over \$2B in first year premium equivalence, and annuity hybrid business to be over \$300M and climbing
- Report available on SOA website in April, 2015

## 2012 - 2015: Life Hybrid Product Restructuring, New Players

- Pacific Life entered the Asset Based Market with their product called PremierCare®
  - PremierCare® was the first Combo product with gender distinct LTC rates
  - In the Linked Benefit market where inflation benefits were hardly being sold, Pacific Life launched with a focus on buying long term care with inflation benefit
  - Further focus on longer EOB benefit periods
  - In a Hybrid market where only about 5 - 10% of the sales actually included an inflation benefit, Pacific Life started selling 75%+ of its policies with inflation options
- Nationwide joined the market with their Hybrid solution
  - They built on their success in the 'LTC Rider' market and structured their CareMatters<sup>SM</sup> product with an "indemnity" design, which actually uses a disability model structure (benefits do not require formal care, and benefit levels are set independent of expenses incurred)
- The Hybrid Life Market broke \$1.5 billion with almost 24,000 policies

## 2012 - 2015: Life Hybrid Product Restructuring, New Players

- MoneyGuard® changed the marketplace by modifying their Day 1 Full Return of Premium benefit, adding lower cost choices with graduated ROP ramping up to 100% of premium over 5 or more years
  - Reduces risk of 1035 exchanges in the event of an interest rate spike
  - Reduces early capital requirements and enhances internal rates of return to companies, and policy performance for clients
- New York Life introduced a new Hybrid product, Asset Preserver®
- MassMutual joined the market with a Par product, CareChoice One<sup>SM</sup>
- Ameriprise introduced a new Hybrid product, TrioSource<sup>SM</sup>, after on-going growth with their Accelerated Benefit LTC rider

moves to  
Dedicated  
Wholesaler and  
Simplified  
Underwriting

## Diverse Market Place – Offering Consumer Options for Life Hybrids



### Lincoln MoneyGuard®

*Awareness, huge dedicated wholesaling force*



### Pacific Life PremierCare®

*Full ROP, Inflation Story*



### Genworth

*Full Underwriting, Multiple Risk Classes*



### OneAmerica

*Portfolio of Linked Solutions [Life (single & joint life) & Annuity]. Lifetime LTC*



### Nationwide

*Indemnity*



### MassMutual

*Dividends*

## Pricing Single Premium Life Hybrid Plans in a Low Interest Rate Environment

- MoneyGuard® offered a 3, 5, 7 & 10 Pay version for a decade plus, but nobody was buying
  - Compensation was a factor
  - Product re-priced and re-comped, and sales responded
  - Fits with de-emphasis of ROP
- MoneyGuard® competitors with multi-pay options saw their sales increase
- Nationwide launched their product (2013) with a multi-pay solution
- Pacific Life launched their Multi-Pay solution in 2015