



## Progress Report Long-Term Care Insurance

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March 8, 2016

As requested in 2015 Minnesota Sessions Law Chapter 59 (see Attachment 1), the Minnesota Department of Commerce (“Commerce” or “Department”) submits this progress report about standards governing the approval of actuarially justified rate increases for long-term care insurance policies issued prior to January 1, 2002.

As required by Minnesota Statutes section 62A.02, subd. 3, Commerce reviews long-term care insurance rate filings. This includes working with companies to identify rate-increase mitigation options to assist consumers who are unable or unwilling to pay the rate increases avoid the loss of their policies. Rate-increase mitigation options are typically in the form of contingent non-forfeiture benefits and/or benefit reductions.

Commerce Department actuaries continue to consult with several organizations, including the National Association of Insurance Commissioners (NAIC), the Society of Actuaries (SOA), the American Academy of Actuaries (AAA) and representatives of the long-term care insurance industry regarding the methodology for approving and disapproving rate increases in compliance with Minnesota law. Minnesota is taking the lead in several venues. The following is a summary of these activities:

- January 2015 and September 2015: Commerce actuarial staff presented on long-term care issues, including rate increases, to the Minnesota Insurance and Financial Services Council (MIFSC) industry trade group.
- March 2015: Commerce actuarial staff participated in the Intercompany Long-Term Care Insurance Conference (ILTCl). Actuarial staff also plan in March 2016 to participate on a panel (including regulators, industry experts and consultants) presenting to the ILTCl on rate increases.
- June 2015: Commerce actuarial staff participated in an SOA meeting where updated long-term care claims experience data was presented. This updated data has been incorporated in the Department’s review method.
- August 2015: Commerce attended an AAA presentation on lapse and mortality experience data that affects long-term care valuation and pricing. This updated data has been incorporated in the Commerce review method.
- August 2015: Commerce convened a full-day public hearing to solicit views and concerns of consumers, consumer advocates, industry’s consulting actuaries, and industry CEO’s on rate increase (as well as other consumer) issues. Both video and audio recordings of this hearing, as well as presentation materials, are available on [the Commerce Department website](#).

- October 2015: Commerce actuaries made a presentation on increased state collaboration to other Midwest regulators at the annual NAIC Midwest Zone meeting in Saint Paul. Feedback at that meeting was favorable.
- November 2015: Commerce actuaries presented a draft rate increase review methodology to the NAIC in a public forum that included regulators from other states, industry representatives and members of the SOA and AAA. The methodology presented by the Commerce actuaries attempts to improve states' methodologies by increasing efficiency, accuracy, predictability and uniformity. See Attachments 2-4. Feedback has been favorable.

In 2016, Minnesota Commerce Commissioner Mike Rothman became chair of the Senior Issues Task Force. At the November 2015 NAIC Fall National Meeting, the Task Force created a new Long-Term Care Innovation Subgroup to address the future of long-term care and examine innovations. Commissioner Rothman serves as vice chair of the new Subgroup.

The charge of the NAIC Long-Term Care Innovation Subgroup includes:

- Reviewing the number of alternative products structures being developed and, in some cases, sold by companies (i.e., LTC/life combination products, term products and universal LTC policies);
- Considering whether these are viable alternative products and what other types of products may assist in financing long term care costs;
- Discussing legal and regulatory barriers and the role of private market insurance products in assisting in financing long-term care needs;
- Considering pricing issues with potential new long-term care financing products and whether the pricing of these products creates a stable market;
- Working with private insurance companies on the future role of insurance in financing long-term care given the history of long-term care insurance over the last few decades; and
- Working with consumers and consumer advocates on financing long-term care needs, including whether they see a role for the private market and, if so, the types of products most appealing to them.

Over the past year, Commerce has worked with companies that have filed rate increase requests. To facilitate improvements in the filing process, Commerce staff have explained the agency's methodology and received generally favorable feedback. The Department has also developed a template data request letter in consultation with these stakeholders. The

letter attempts to more fully identify the reasons for requested rate increases. A generalized form of the letter has been shared with the NAIC, industry and the public. See Attachment 4.

In Minnesota, approving unjustified rates is illegal under Minnesota Statutes section 62A.02, subd. 3. An example of an unjustified finding is that consumers who have policies with less-rich benefits or lifetime premium period requirements would end up substantially subsidizing others with richer benefits or limited premium-period requirements.

The Department continues to refine its letter and is urging other states to use this template, offering companies a more standardized data request format to work with (as opposed to having substantially different data requests from each state that reviews rates).

Besides leading these efforts, Minnesota has worked with several other states – including California, Texas, Illinois and Florida – to improve collaboration on a rate review method.

Two key aspects of the Commerce Department’s methodology are less reliance on the loss ratio metric and the recognition of asymmetrical information at the time of sale regarding the potential magnitude of future rate increases.

Minnesota law sets a loss ratio as a minimum standard, not as a standard for reasonableness. Commerce’s concerns on using the loss ratio as a standard for reasonableness (as it would be under the NAIC model bulletin) include the following:

- As a block of business decreases in size, those consumers left face extremely high rate increases;
- Investment return performance is not measured and several companies have a valid case that a driver of losses is poor investment returns; and
- Implied profits would be a percentage of premiums (which if they increased would result in higher profits than originally assumed, meaning companies may not only be recovering losses but profiting more after a rate increase if loss ratio standards were the only criteria).

The NAIC model bulletin has been adopted, in some form, in only a handful of states. Many states appear to now prefer the Minnesota approach, as presented to the NAIC. A weakness of the model bulletin is that as long-term care insurance blocks become more mature (with most of the premiums paid in the past), the resulting rate increases applying a loss-ratio approach would be extremely high – sometimes exceeding a 1,000 percent increase. Policyholders would be blindsided by such increases, forcing consumers to surrender their policies and lose thousands of dollars in paid premiums. Trust in the long-term care

insurance industry – and the regulation of the industry – could be questioned if such high rate increases would be approved, as would be allowable under the NAIC model bulletin.

The asymmetrical information – where the company knew or should have known the sensitivity of rates to small changes in factors such as lapse, mortality and investment returns – likely led to the potential misleading situation where policyholders may have known limited rate increases were possible but not increases that would result in rates that potentially could double, triple or more.

The Minnesota approach is an attempt to improve the long-term care rate review process and contains aspects that led to greater efficiency as well as more uniformity and predictability:

- 1) More uniform data requests, which address aspects a regulator could question regarding performance of a block of long-term care business. The requests attempt to eliminate misconceptions and artificial measures of a block's performance and replace them with facts and more accurate measures.
- 2) Regulator collaboration on math aspects of the rates, which includes verification that calculations and the impact of drivers of higher rates are as presented by the company. Attachment 3 describes these math aspects.

The Commerce Department's goal is to balance fairness to consumers and the prevention of financial distress to insurers. Communications with companies and other states in 2015 have led to progress in Minnesota and nationally on achieving this balance through the rate review process. Accordingly, the Commerce Department's recommendation is that no additional legislation is needed at this time. The Department will continue to work with industry members on a company-by-company basis to address their filings.

## ATTACHMENT 1

### 2015 Minnesota Session Laws

#### CHAPTER 59

##### Sec. 4. Rate Approval; Recommendations

(a) The commissioner of commerce may make recommendations to the chairs and ranking minority members of the house and senate committees having jurisdiction over commerce for standards governing the approval of actuarially justified rate increases for long-term care insurance policies issued prior to January 1, 2002. The recommendations may include rate-increase mitigation options, including contingent nonforfeiture benefits and optional benefit changes to protect policy holders that may receive rate increases.

(b) In developing these recommendations, the commissioner may consult with the National Association of Insurance Commissioners, the Society of Actuaries and the Academy of Actuaries, representatives of the long-term insurance industry, and the house and senate committee chairs and ranking minority members for the committees having jurisdiction over commerce. The commissioner may submit progress reports to the chairs and ranking minority members of the house and senate committees having jurisdiction over commerce on October 15, 2015, and February 1, 2016.

## ATTACHMENT 2

### **From draft minutes of the November 18, 2015 Long-Term Care Actuarial Working Group Session at the NAIC National Meeting:**

Mr. Andersen (Actuary at Minnesota Department of Commerce) presented a draft proposal for a collaborative LTCI rate review process intended to increase uniformity and predictability of LTCI rate reviews among the states. He said he wants the first phase of the project to be a collaborative effort among the states to define the mathematical calculations that will be used. He said that, after the first phase, the states may work toward reducing differences in their rules and interpretations.

Mr. Andersen presented a draft template letter with points for the states to discuss with insurers filing LTCI rate increases. He said the questions in the letter are a condensed version of the questions the Minnesota Department of Commerce currently asks insurers seeking LTCI rate increases.

## ATTACHMENT 3

### Summary of Outline of “Minnesota Approach,” distributed and discussed at the November 18, 2015, NAIC National Meeting, Long-Term Care Actuarial Working Group session

#### DRAFT - Collaborative LTC Rate Increase Review Method

There are several different long-term care rate increase calculation methods being used by companies to prevent financial distress and by regulators to balance preventing this distress with being fair to consumers. However, there is widespread thought that the multitude of methods is causing a lack of transparency by insurance companies and regulators with respect to rate increase requests and approvals. This, in turn, is causing confusion regarding the viability of the long-term care insurance market.

There have been attempts to put methods in place that may prevent insurer distress but several regulators believe they do not adequately handle consumer fairness issues.

The following method is an attempted step to balance these key principles.

Phase 1: 50 states agree on the following math components:

- (a) Original premium
- (b) Benchmark original premium
- (c) If you knew then what you know now (“If Knew”) premium
- (d) Makeup or catchup premium

Original premiums are known.

The If Knew premium is the premium that would have been charged at issue if the insurer knew then what it knows now regarding material factors including investment, lapse, mortality, and morbidity rates. Benchmark and If Knew premiums require regulator judgment on assumptions. The regulator judgment could be applied by a representative group of states. The benchmark original premium is based on information known at the time of pricing. Sources could include assumptions generally used by most industry players at the time and Society of Actuaries’ experience and trends.

The makeup or catchup premium is manually input (through spreadsheet function “goal seek”) and can get the company back to one of two metrics: the original loss ratio or the original present value of profits. Commerce prefers the present value of profits metric due in part to concerns with the loss ratio metric stated in Appendix 1, below. To more accurately measure the adversity of experience versus original pricing assumptions, actual or average available investment experience should be used when determining the present value of profits (as opposed to the loss ratio approach of using the life insurance valuation interest rate at the time the policy was issued). The use of more realistic investment experience helps prevent a company making a case for a rate increase when it is actually profiting more than initially expected. Care should also be taken to prevent a company making a case for a rate increase based on worse investment experience than actual being unfairly shifted to



the insured pool. Note that in Minnesota, the loss ratio standard only applies as a minimum, not as a maximum or a standard of reasonability.

A goal is to have all four of the math components, including the appropriateness of underlying assumptions, agreed upon by all of the states.

Phase 2. (Shorter-term goal): States make transparent adjustments for compliance with state rules and consistency with state interpretations.

Examples of adjustments include the following:

(a) In cases where a company's original premium was significantly below the benchmark original premium, a factor could be applied such that the percentage rate increase would be partially based on the benchmark original premium instead of being completely based on the original premium. This would help prevent bait and switch, encourage adequate pricing, and not allow companies to intentionally underprice with the knowledge that they could make up for initial losses.

(b) Where the company did not inform consumers at sale of the sensitivity of premiums to small changes in factors (such as persistency) or where the timing of the rate increase request substantially lagged the time where the presence of adverse experience was known, a cost-sharing adjustment may be appropriate.

In this method, the adjustment would be explicit and include a factor which represents the weighted average between the makeup premium and the If Knew premium. There would be less making up for past deficient premiums where state rules or interpretations lead to the case that the company did not provide the consumer adequate information to avoid increasing sunk costs.

Persistency since inception may be considered as a factor in the adjustment to ensure a small group of remaining policyholders is not paying excess premiums to cover losses related to the group of policyholders who used up their benefits.

The adjustment may be a set percentage, staggered (higher cost sharing percentage for higher total rate increases since inception), or developed under another transparent approach.

(c) Any additional explicit adjustment, based on risk transfer principles or specifics related to the case.

(d) Any solvency concerns may be considered.

Phase 2, (Longer-term goal): States move toward converging their rules and interpretations such that the adjustments noted above would converge, leading to added consistency in rate increase approvals between states.

Comments:

The rate increase approval method would be based first on the original premium. Then adjustment is made for the current premium, reflecting past increases, such that the methodology underlying total rate increases since inception is consistent. It could lead to illogical results to have new rate increase approvals based on today's methodology to be added on to past rate increases based on a past methodology. It should be noted what was communicated to regulators and policyholders following any past rate increases regarding the grounds for subsequent rate increases. It should also be noted what the company is planning to say about future rate increases at the implementation of the current rate increase being requested, and the regulator should evaluate this planned statement.

Just as assumptions and pricing change become refined and change over time, the rate review methodology becomes more refined and may change over time. For instance, the interaction of persistency assumption and morbidity assumption may not have been relevant as part of a past rate increase review, but it may be relevant in a current review.

This review may first be performed for the richest block, typically five percent compound inflation, lifetime benefits, at sample issue ages of 55 and 65. Appropriateness of rate increases for less rich blocks at other ages can then be determined.

To help attain information to proceed with this method, see summarized questions in Appendix 2.

## Appendix 1 (of Attachment 3) – Examples of Loss Ratio Weaknesses

Reasonableness review aspect:

Loss ratio is a short-term concept intended to reflect a certain level of profit (or loss) expectations

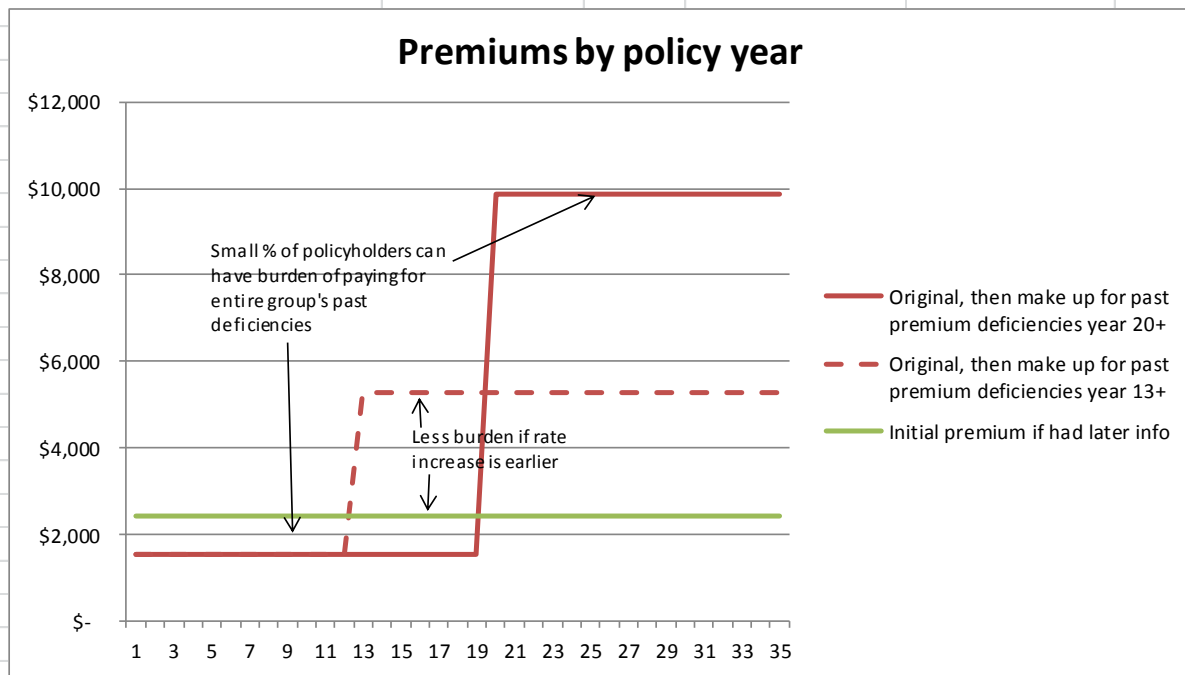
As shown below, this metric can fail in the long-term due to consideration of investment returns in profitability

	Investment Return	Discount Rate	Ending Surplus	PV Ending Surplus	Loss Ratio
Original profit expectations	4.5%	4.5%	\$ 211,000,000	\$ 61,000,000	65%
Actual profit	Actual	4.5%	\$ 796,000,000	\$ 229,000,000	65%
Profit if average investment returns	Average Available	4.5%	\$ 425,000,000	\$ 122,000,000	65%

Unfairness review aspect:

Getting back to original loss ratio becomes more burdensome on persisting policyholders over time

Policyholder paid premiums over time to accumulate to help lower future premiums



Unjustified review aspect:

With the loss ratio approach, dollar profit expectations increase proportionally to the increase in premiums

We believe it is unjustified for part of the increased rates to support an increased dollar of profits

	PV of Premiums	PV of Claims	Loss Ratio	PV of Expenses	PV Ending Surplus
\$	610,000,000	\$ 396,500,000	65%	\$ 152,500,000	\$ 61,000,000
\$	1,220,000,000	\$ 793,000,000	65%	\$ 305,000,000	\$ 122,000,000

## Appendix 2 (of Attachment 3) – Summary & Details of Template Questions

<u>Template question #</u>	<u>Documentation Request</u>	
1	Rate Schedule	
2	Increase History	
3	Updated Memorandum	
4	ASOP compliance	
5	Rate Stabilization	
6	Original Memorandum	
7	Premium Comparison	
8	Other States' Approvals	
9	Notification Letter	
<u>Template question #</u>	<u>Assumption, Technical, Management Request</u>	<u>Additional info</u>
10	Pricing Attribution	Increase rationale & impact on pricing from changes in assumptions
11	Experience Data	Actual to expected on investment returns and actuarial factors
12	Data Sources	Including credibility and relevance
13	Assumption Adjustment	Company-specific adjustment if base is an outside source
14	Morbidity Details	Summary and details of claim frequency and severity
15	If Knew Premium	Premium charged if now-known factors were known at issue
16	Policyholder Options	Is actuarial equivalence a goal?
17	Increase Differences	Request differs by benefit period and inflation amount?
18	Cash Flows	Including investment income
19	Retrospective Cash Flows	Versions with initial and current assumptions
20	Prospective Cash Flows	Reflecting current assumptions
21	Factor Attribution	Cash flow impact of changes in key assumptions
22	Reserve Development	Formulaic, premium deficiency, and asset adequacy
23	Block Management	Investment, reinsurance, experience monitoring, efficiencies
24	Reserve Updating	Have past profits been released due to under-reserving?
25	Assumption Timing	Has reserving and pricing been appropriately updated?
26	Past Notification	Further deterioration since last rate increase?

Responses to questions 10-21 impact the math component and responses to questions 22-26 impact the adjustment component. Questions 1-9 address documentation.

## ATTACHMENT 4

A template list of questions distributed and discussed at the November 18, 2015, NAIC National Meeting, Long-Term Care Actuarial Working Group session. The Minnesota Department of Commerce developed this template data request letter in consultation with stakeholders. The letter attempts to more fully identify the reasons for requested rate increases.

October 21, 2015 (date template drafted) - **DRAFT**

TO: Insurance Company

RE: Talking points for discussion on long-term care rate increase filing

In our review of long-term care rate filings, we attempt to review the documentation, assumptions, technical aspects, and management associated with the block of business. We have questions and requests from a template addressing the fair, reasonable, equitable, and justified standards our law provides for approval or disapproval of rate filings.

The following list contains items that could be determined to be necessary to support a complete filing. This document will serve as a basis for discussion to determine the extent to which these aspects are relevant to the Company's particular circumstances. At this point, response to the items stated below is not necessary. Follow-up correspondence will lead to the need for a response.

Related to review of documentation:

1. Provide the new premium rate schedule. [Model Reg / Guidance Manual (GM)]
2. Provide a new disclosure of rate increase history. [GM]
3. Provide an updated actuarial memorandum, including reflection of revised, reasonable pricing assumptions. [GM]
4. Please ensure that the actuarial justification for pricing, including assumptions and methods, are documented and reflective of the Code of Professional Conduct and applicable Actuarial Standards of Practice. For example, is the documentation sufficiently clear such that another actuary qualified in the same practice area (in this case the regulatory actuary) could make an objective appraisal of the reasonableness of the actuary's work?  
[Emphasizes ASOP's and clear, complete documentation]
5. If applicable, provide a demonstration of rate stabilization compliance, including a demonstration of original assumptions for post-2002-written policies containing appropriate margins reflecting moderately adverse conditions. [Necessary to review compliance of post-rate-stabilization policies]

6. Provide the original actuarial memorandum, including original pricing documentation, including the original anticipated loss ratio, original pricing assumptions, and original mix of business. Also provide the actual mix of business. [GM mentions the need for an explanation of the original assumptions that were not realized in support of the requested rate increase. In some cases the original memorandum is not available, and alternative demonstration could be acceptable.]

7. After the requested rate increase, would existing policyholders pay a higher premium than new policyholders on similar policies? [GM]

8. Provide an exhibit showing the timing and size of rate requests requested and approved in other states. [traditional request in many states]

9. Provide the letter you will use to notify the insureds of the rate increase. [discussed in GM revision process]

Related to review of assumptions:

10. Ensure that the rationale for the rate increase is clearly stated. Provide an exhibit showing a comparison of key original versus updated pricing assumptions and an attribution analysis showing the impact on the premiums due to each change in assumption, including lapse, mortality, claim incidence, claim severity, and investment returns. [GM & to see numbers behind reasons for request]

11. Provide the data on actual experience of investment returns and other factors such as lapse, mortality, morbidity, claims frequency, claims severity, administrative expenses, and commissions. Provide the actual-to-expected ratios for each assumption: one where “expected” is the original pricing assumption and one where “expected” is the current pricing assumption. [to see level of adversity in experience]

12. Provide a detailed explanation of the data sources, including commentary on the credibility and relevance of the data, explanation of the review performed by the actuary as part of setting the assumptions, and explanation of which demonstrations in support of a rate increase request reflect experience of the block within the scope of the request and experience including other blocks. [verify prudence in setting of assumptions]

13. Show how lapse, mortality, and morbidity assumptions have been appropriately adjusted from tables from outside sources in light of the company’s own health underwriting practices, target market, and policyholder demographics. [verify prudence in setting of assumptions]

14. If revised morbidity expectations are driving a significant portion of the reason for the rate increase, include a narrative summary and supporting details of claim frequency, claim severity, and other relevant aspects of the morbidity assumption, including justification of

the assumption and supporting experience. Please provide actual-to-original expected and new expected-to-original expected ratios for claims incidence and claims severity along with the most recent comprehensive claims study. [new item in light of (a) LTC Valuation SG report that companies may not have a good handle on claim severity and (b) recent cases of morbidity being the key rationale for the rate increase request]

Related to review of technical and dynamic aspects of the analysis:

15. Provide the premium that would have been charged at issue if the insurer knew then what it knows now regarding material factors including investment, lapse, mortality, and morbidity rates. Include similar margins as in the original pricing. [could be an aspect of the process for reviewing the reasonableness of the rate increase request.]

16. Provide the options that will be provided to policyholders who, faced with a rate increase, would prefer actuarially equivalent alternatives such as benefit reductions. Include demonstrations and state if near-actuarial equivalence is a goal. Actuarial equivalence may be defined by comparing the present value of increase in rates and the present value of reduction in benefits. If near actuarial equivalence is a goal, please demonstrate such. [allows regulator to compare and evaluate the value and appropriateness of options provided]

17. Is the requested percentage rate increase different for groups of policies with substantially different benefit features that have resulted in substantial differences in changes in value over time between the groups? For example, is there a substantial difference in experience between different issue age bands, between products inflation-protected and non-inflation-protected policies, or between lifetime and limited benefit policies? [allows regulator to determine if extensive subsidy between blocks would occur if the request was approved, perhaps sparking a dialog to remove the subsidy]

For questions 18 through 21, provide an explanation and justification of any estimates that are used, in compliance with actuarial standards of practice.

18. Provide spreadsheets showing cash flows by year showing premiums, investment income, claims, expenses, and other cash inflows and outflows related to this block of business. [to demonstrate adequacy including all relevant factors]

19. Provide versions of this spreadsheet for the baseline retrospective view (from the year the first policy was issued until the current year), using initial expected assumptions in one version and actual experience (for premiums, investment income, claims, expenses, other cash flows, and reserve changes) in another version, and reflecting any past rate increases. [to demonstrate adequate using actual experience up to the point of the request]

20. Provide versions of this spreadsheet for the prospective view (from next year through the year the business is expected to run out), with one version applying current premiums and a

second version applying the rate increase the insurer proposes. Each of these prospective versions should reflect the insurer's current assumptions. [to project future adequacy including all relevant factors]

21. Provide versions of these spreadsheets showing attribution of results to a change in each key assumption. [to provide additional information on the rationale for the request]

22. Explain changes in total reserves (including active life, premium deficiency, and asset adequacy) supporting the block of business for which the rate increase is being requested, by year, from the year the first policy was issued until the current year, including a description of the timing of change of key assumptions over time. Provide an explanation and justification of any estimates that are used. [This information is helpful in attaining information on a key aspect of the financial picture of the LTC block, since assets accumulate for this level-premium product]

Related to management of the block:

23. Explain the management of the block of business associated with the rate increase. Examples include asset portfolio management, case management, reinsurance controls, frequent monitoring of emerging experience, reflection of emerging experience in reserving and pricing assumptions, commission structures, and administrative efficiencies. [to attain insight on the appropriateness of the management of the block]

24. Has there been any cause and effect of assumptions underlying past reserves not being updated annually, resulting past profits being released, and the combination of reserves held and future premiums being insufficient to pay future claims? [to review whether the company appropriately reflected up-to-date information in pricing and reserving]

25. Describe the timing of studies or other methods of learning about development of adverse experience and implementation of that updated experience in pricing and reserving assumptions. [to review whether the company appropriately reflected up-to-date information in pricing and reserving]

26. If applicable, provide past rate increase documentation, including the notification letter and documentation on the situation at the time of the most recent rate. What was communicated to policyholders and regulators? Also, provide information regarding the extent to which unforeseeable deterioration of conditions since the last rate increase contributed to the magnitude of the current rate increase request. [GM]

To schedule the conference call with the Department, please contact the State actuary by e-mail or by telephone.