COMBINATION LONG-TERM CARE PRODUCTS

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Combination Long-Term Care Products

- Long-Term Care Insurance can be purchased in conjunction with some other insurance policies:
  - Life insurance
  - Deferred annuities
  - Life annuities (Life care annuity)

- Focus of this presentation is the life care annuity
  - Description
  - Potential advantages to consumers
  - Tax and regulatory treatment

Life care annuity: Description

- An integrated insurance product consisting of a life annuity and long-term care insurance segments (Murtaugh, Spillman, Warshawsky, 2001)
- In return for one or more premium payments, a life care annuity pays a stream of fixed, periodic payments (the life annuity segment) and in the event of disability, provides an additional payment to cover the costs associated with long-term care.
  - The annuity payments can be fixed in nominal terms, increasing, or inflation-indexed.
  - The long-term care portion can be structured as a disability indemnity policy or reimbursement for long-term care services.
- Product intended for purchase at around the time of retirement to protect against longevity and disability risk.

Challenges facing standalone annuity and LTCI products

- The life care annuity is intended to address shortcomings in the market for long-term care insurance and life annuities by offsetting the risks that hamper each product.
  - Life annuities are subject to adverse selection by low-mortality classes, raising the price relative to a product without adverse selection.
  - Long-term care insurance policies are underwritten to exclude high mortality classes, because the level premium nature of the product prohibits premiums from covering expected claims.
- In principle, combining long-term care insurance and life annuities would reduce adverse selection for the annuity portion, resulting in lower premiums, and would allow for a relaxation of underwriting standards for the long-term care insurance portion.

Advantages of the life care annuity

- Research on risk pooling properties of the life care annuity:
  - Currently, around 15-25 percent of the 65-year-old population is ineligible for long-term care insurance. The life care annuity would enable all but 2-4 percent of the 65-year-old population to become eligible (Murtaugh, Spillman, Warshawsky, 2001; Brown, Warshawsky, 2013).
  - A gender-rated life care annuity could be sold more cheaply than the two products sold separately, thanks to offsetting longevity risks (Murtaugh, Spillman, Warshawsky, 2001; Brown, Warshawsky, 2013).
- The life care annuity would allow people to delay long-term care insurance purchase till closer to retirement.
  - This has the further benefit of allowing insurers to better account for trends in disability, longevity, investment returns, and other sources of risk in designing and pricing policies.

Life care annuity: Tax and regulation

- The Pension Protection Act specifically recognized combination qualified long-term care insurance/annuity products.
- The life care annuity is slightly more tax advantaged than standalone annuity/qualified long-term care insurance policies (Brazell, Brown, Warshawsky, 2008).
- Regulatory uncertainty/impairments might limit the life care annuity as a distribution option in a qualified retirement plan (Brazell, Brown, Warshawsky, 2008).
  - Minimum distribution requirements
  - Sex neutral pricing of life annuities
  - Incidental benefits

References

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- Murtaugh, C., B. Spillman, and M. Warshawsky, 2001, "In Sickness and In Health: An Annuity Approach to Financing Long-Term Care and Retirement Income," *Journal of Risk and Insurance*, 68(2): 225-254.