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Hybrid Life/LTCi: Breaking Down Barriers And Bridging Gaps

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Finding the right long-term care plan is a big key to retirement planning, experts say.

By Tony Laudato

Recent months have seen a steady drip of bad news from life insurers, as firms have had to boost their reserves to the tune of billions in an expectation of soaring payouts for long-term care insurance policies.

While troubling, the news simply confirms something that has been fairly obvious for some time: the old long-term care market – once popular as a means of funding assisting living, nursing home and home care services – is now more of a headache than an opportunity for insurers.

The market now must significantly review assumptions made long ago when the first such policies were written, during a period when interest rates and projected lapse rates were higher and health care expenses lower. To say the equation has shifted would be an understatement. The cost of assisted living has increased by 67 percent over the past 15 years, according to the Genworth Cost of Care Survey. Meanwhile, one in two Americans has a chronic health condition, the Centers for Disease Control and Prevention reports.

The resulting increased premiums have decimated the LTCi industry. Many providers have withdrawn from the market altogether, and those that remain must be increasingly restrictive with their policies.

Axing an entire revenue stream, however - especially one that was once so lucrative - is a risky choice to make in a situation where demand is clearly not the problem. The need for long-term care is going nowhere.

As such, the market is increasingly starting to turn to hybrid policies. Hybrid policies work by combining the two types of coverage – life insurance and long-term care – and allow for payouts based on accelerated or early payments of a death benefit. Importantly, the combination also allows insurers to stabilize the risk profile of the product, and provide a sustainable means of growing both the top and bottom lines.

These policies are designed to make LTCi profitable again, and in doing so they may also present a way to partially tackle another problem - the decline in the life insurance market. The number of Americans holding life insurance has been falling steadily for decades and more than 40 percent of Americans have no coverage, according to LIMRA and Life Happens. While this problem is concentrated among younger Americans – not the traditional market for late-life health care – research shows that one of the main reasons younger Americans don't buy life insurance is a lack of flexibility and innovation in the product itself. LTCi is much cheaper the younger you are when you buy it, and so hybrid policies could well have more appeal here.

The younger market aside, there is every sign that hybrid policies could grow popular among middle-aged and older Americans. As opposed to more traditional standalone policies, hybrid policies provide an option that isn't "use it or lose it" with regard to benefits. With hybrids, there is still a death benefit even if the LTC benefit isn't used. For wealthier clients who have accumulated financial assets throughout their lives, hybrid policies additionally provide a way for them to protect those assets from the high cost of late-life care should it be needed.

The current gap in the LTCi market is more circumstantial than reflecting anything fundamental. The financial crash and its aftermath engendered a lack of product innovation, with the LTCi market suffering from this as providers scrambled to de-risk their portfolios. Hybrid solutions, however, offer a solution to this impasse that comes with a far more favorable risk profile, will genuinely benefit all parties involved and could help breathe life back into the ailing sector.

In addition to potentially reopening the LTCi market, hybrid policies could simultaneously help the market reverse the downward trend in life insurance. Evidence suggests that one of the main barriers to buying life insurance perceived by today's consumers is the lack of flexibility and control associated with traditional products. By addressing this, hybrid policies promise to turn two problems into a new and untapped market for the sector.

As a result of all these favorable factors, sales of hybrid policies are increasing, with more than 260,000 such policies sold in 2017, LIMRA reported. But there is still a long way to go. Sales of this product have been stymied by an understandable skepticism on the part of the industry, still reeling from the impact of the earlier miscalculations and erroneous assumptions in LTCi that continue to cause losses today.

If the LTCi market is to enjoy a hybrid revival and avoid the mistakes of history, carriers will need to ensure that the design of such products is right, and certainly more robust and well-founded than those of the previous era of standalone products. As the history of the aviation industry teaches us, hyper-engineering is the best form of reassurance.

Given the nascent stage the new product is at, getting it right requires a specific set of underwriting skills, a granular understanding of the pricing and risk modeling involved, a deep expertise in area of mortality rates, and new reinsurance structures to support risk transfer. For those that can get it right, the rewards will be significant.

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