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Managing the Impact of Long-Term Care Needs and Expense on Retirement Security Monograph

An Affordable Long-Term Care Solution through Risk Sharing

By Kailan Shang, Hua Su, and Yu Lin

Actuaries
Risk is Opportunity.[sm]

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Prepared by

Kailan Shang[1]

Hua Su[2]

Yu Lin[3]

[1] Kailan Shang FSA, CFA, PRM, SCJP, is managing director at Swin Solutions Inc. He can be reached at kailan.shang@swinsolutions.com.

[2] Hua Su FSA, CFA, is manager at AEGON-CNOOC Life Insurance Co. He can be reached at suhua@aegon-cnooc.com.

[3] Yu Lin ASA, M.S. in statistics, is actuarial associate at Manulife Financial. She can be reached at yu_lin@manulife.com.

EXECUTIVE SUMMARY

Long-term care (LTC) protection plays an essential role in maintaining the financial security and the quality of life for retirees. However, the economic conditions and the rising expenses of LTC put a lot of pressure on the social health care system, the insurers, and the retirees. The social health care systems are facing funding stress and will unlikely be able to provide more LTC benefits in the near future. Due to the low and stagnant interest rate environment in the long term and unexpectedly high LTC benefit payments, insurers either increased the premium for LTC protection or exited the market. Many people cannot afford the rising LTC premium when they are also struggling to save for retirement.

It is critical to have an LTC solution that insurers are willing to sell and for which the premium is affordable for middle-class families. There have been innovative ways of providing LTC benefits in recent years. Some combine the LTC benefit with other insurance benefits such as a death benefit or annuity payments. The aggregate risk is lower than that of the stand-alone LTC product because the combo product contains offsetting risks. However, it does not necessarily reduce the risk inherent in the LTC protection. Other products add flexibility in the premium and benefit payment to reduce the risk for carriers, but it may not be transparent enough. Moreover, policyholders may prefer different and riskier investment strategies than what insurance companies normally choose.

In this paper, we propose an LTC product that has an investment-risk-sharing mechanism between the insurer and the insured. The investment risk will be partially transferred to the clients with a guarantee that is much cheaper than those provided by traditional LTC products. The insurance risks are still borne by insurers. The benefit is adjustable with a floor, and the premium is flexible. Policyholders can choose their own investment strategies according to their risk tolerance depending on ages, levels of wealth, and other factors. The benefit of the risk-sharing arrangement is three-fold: (a) the risk of the new product is lower for the insurers, (b) the price of the product is flexible and affordable, and (c) more risky investment strategies can be used at the discretion of the policyholders to address the rising LTC expenses.

The paper compares the new design with a traditional LTC product to illustrate different levels of risk for the insured and the insurer. Policyholder behaviors, investment strategies and risk management are also touched on. It is hoped that the new design leads to an acceptable level of risk for the insurers and an acceptable price for the clients.