CalPERS

Finance and Administration Committee

Agenda Item 8c

December 20, 2016

Item Name: Long-Term Care Valuation Report

Program: Actuarial

Item Type: Information

Executive Summary
This agenda item provides the results of the California Public Employees' Retirement System Long-Term Care (LTC) Program annual actuarial valuation for the fiscal year ending June 30, 2016. A copy of the actuarial valuation report is attached to this agenda item.

This actuarial valuation reflects the Stabilization Plan that was approved by the Board of Administration (Board) in October 2012 that included premium increases for certain policies and permitted policy conversions for policyholders to move to a less expensive policy. The actuarial valuation also includes new policyholders that have purchased LTC policies since the reopening of the CalPERS LTC Program. This actuarial valuation includes 132,274 policies, among them 1,264 are LTC4 policies.

The margin for the LTC Program has decreased from 14.44 percent as of June 30, 2015 to 9.59 percent as of June 30, 2016. The decrease in margin was mostly due to the increase in the claim cost assumption, which is caused by observed worse than expected morbidity in the previous few years and more credibility assigned to the Program's experiences. For further details on the reasons for the changes in margin, please refer to the Analysis section of this agenda item.

Even though the margin decreased from last year because of change in claim cost assumption, Fiscal Year 2015-16, the margin of 9.59% as of June 30, 2016 is close to the Board approved 10% margin requirement and consistent with the goal of the Stabilization Plan. We are not recommending any premium changes this year.

Strategic Plan
This agenda item supports the Strategic Plan Goal A - Improve long-term pension and health benefit sustainability.

Background
The CalPERS LTC Program started in 1995 and the Program has 132,274 policyholders as of June 30, 2016. Information on the types of policies offered through the program and the number of policyholders under each type can be obtained in Appendix E in the valuation report attached to the agenda item.

Similar to LTC insurance providers, the CalPERS LTC Program has experienced worse than expected morbidity, higher than expected claims, lower than expected voluntary termination, and lower than expected investment income since its inception. CalPERS has taken corrective action to stabilize the LTC Fund. The most recent change was the adoption of the Stabilization Plan in October 2012, that included a premium increase of 85 percent, two 36 percent premium increases applied over 2015 and 2016 respectively, or a one-time 79 percent in 2015, for certain policies and permitted policy conversions to a less expensive policy.

Analysis

Funded Status and Margin for the Program

The results of the actuarial valuation are based on the membership data and fund balance as of June 30, 2016. The funded status as of June 30, 2016, is 106 percent and the margin is 9.59 percent.

The following table shows how the funded status and margin were derived and compares the key results from the valuation to the key results from the June 30, 2015, actuarial valuation.

Component	6/30/2015 ($ in Millions)	6/30/2016 ($ in Millions)
1. Present Value of Future Benefits	$6,144	$6,225
2. Present Value of Future Expenses	$388	$404
3. Present Value of Future Premiums (PVFP)	$2,868	$2,589
4. Valuation Liabilities (= 1 + 2 - 3)	$3,664	$4,040
5. Valuation Assets	$4,078	$4,288
6. Valuation Margin (= 5 - 4)	$414	$248
7. Margin as a % of PVFP (= 6 / 3)	14.44%	9.59%
8. Funded Status (= 5 / 4)	111%	106%

Main Reasons for Changes in Margin

The margin of the LTC program decreased by 4.85 percent from 14.44 percent in 2015 to 9.59 percent in 2016. The main reason for the decrease in margin was the increase in the claim cost assumption. The claim cost assumption is credibility-weighted between CalPERS' Program's experience and the industry assumption. The new claim cost assumption increases as observed worse than expected morbidity in the previous few years and more credibility assigned to the Program's experiences which is slightly worse than the industry assumption.

The funded status and the margin have decreased in the past two years, mainly due to the investment loss and increase in the claim cost assumption. The LTC program has a long term horizon and changes should not be made simply in reaction to short term losses or gains due to worse or better than expected experience. Experience of the program should be reviewed and monitored annually for long-term trends to make sure the Program will be stable over the next 60 years.

Please refer to the "Risk Analysis" section on pages 19 to 22 of the attached valuation report for more information on how sensitive the margin of the LTC Program is, to changes in the key actuarial assumptions.

The table below provides the breakdown of the reasons for the decrease in margin between 2015 and 2016.

	Results as a Present-Value of Premiums
Margin as of June 30, 2015:	14.44%
Projected One Year Forward (Passage of Time)	1.60%
Demographic Experience Gain	0.79%
Investment Loss for FY 2014-15	(0.91%)
Morbidity Assumption Change	(5.45%)
Expenses Assumption Change	(0.88%)
Margin as of June 30, 2016:	9.59%

For more information on the experience of each key actuarial assumption in the last fiscal year, please refer to the "Summary of Key Assumptions" section in the attached valuation report.

History of Funded Status and Margin

The Program's funded status has been more than 100 percent funded and the margin has been positive since 2013 after the implementation of the Stabilization Plan. The table below shows the funded status and the margin/(deficit) for the LTC Program for the last 5 years. In the past two years, there is a steady decline in the funded status and the margin. The main drivers for the decrease in the funded status and the margin are investment loss and higher than expected claim cost.

5 Year History of Funded Status and Margin

Valuation Date	Funded Status	Margin
June 30, 2012	96%	(4.66%)
June 30, 2013	123%	19.66%
June 30, 2014	123%	23.49%
June 30, 2015	111%	14.44%
June 30, 2016	106%	9.59%

Budget and Fiscal Impacts

The June 30, 2016, actuarial valuation was prepared internally. United Health Actuarial Services, Inc. (UHAS) did a parallel valuation. Funding was already identified within existing budgetary resources.

Benefits and Risks

The actuarial calculations performed as part of the actuarial valuation are based on a number of assumptions about very long-term demographic and economic behavior. Unless these assumptions (morbidity, lapses, deaths, expenses, and investment return) are exactly realized each year, there will be differences on a year-to-year basis. The year-to-year differences between actual experience and the assumptions are called actuarial gains and losses and either increase or decrease the funded status and margin of the LTC Program. If the actual experience differs from the assumption over a prolonged period, it may result in a need for premium changes to ensure the financial integrity of the LTC Program. To minimize the risk that actual experience is not in line with assumptions, actuarial assumptions are periodically revised as they were in this valuation.

One of the key assumptions that poses the most risk to the program if not realized is the investment return. LTC insurance is characterized by level premiums and increasing claim costs over the coverage period. The collected premiums are invested, and the aggregate premiums plus investment income are used to pay out future claims. Investment income is a significant component of the income as the block of insurance matures. If investment returns were to be lower than expected over a prolonged period then more premiums would be needed to make up for the reduced growth in assets.

Other assumptions that could have a significant impact on the LTC Program if not realized over a long period of time include the morbidity assumption (i.e. amount of claims paid each year), lapses and mortality. These assumptions, (i.e. excluding investment returns) are not subject to wide variances from year-to-year, and typically the changes to these additional assumptions would only gradually change over time. Please refer to the “Risk Analysis” section of the valuation report for more information on how sensitive the margin of the LTC Program is to changes in the key actuarial assumptions.

Attachments
Attachment 1 - Actuarial Valuation Report of the CalPERS Long-Term Care Program as of June 30, 2016.

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