

To: Secretary Sebelius

From: Kathy Greenlee, CLASS Administrator

Re: Memorandum on the CLASS Program

Date: 14 October 2011

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The purpose of this memorandum is to transmit the attached comprehensive report written jointly by the Community Living Assistance Services and Supports (CLASS) Office, the Assistant Secretary for Planning and Evaluation, and the Office of General Counsel documenting policy, marketing, and legal analyses conducted on the CLASS Act. I have also included my recommendation as to how the Department should proceed with its responsibilities under the CLASS Act.

### Background

The CLASS Act establishes a voluntary insurance program for American workers to help pay for long-term care services and supports that they may need in the future. The program seeks to help enrollees live independently in the community. By law, CLASS benefits must be funded entirely through enrollee premiums without any taxpayer subsidy, and requires that the program be solvent over a 75-year period.

There is a crucial need to find ways to help Americans prepare for their long-term care needs. Almost seven out of ten people turning age 65 today will experience, at some point in their lives, functional disability and need some paid or unpaid help with basic daily living activities. While most people who need long-term care are in their 70s and 80s, young people also can require care. Forty percent of long-term care users today are between the ages of 18 and 64.

Long-term care is expensive. While costs for nursing home care can vary widely, they average about \$6,500 a month, or anywhere from \$70,000 to \$80,000 a year. People who receive long-term care services at home spend an average of \$1,800 a month. The average lifetime long-term care spending for a 65 year old is \$47,000; 16 percent will spend \$100,000 and 5 percent will spend \$250,000. Medicare does not cover long-term care services. Since Medicaid pays only for services for people with limited financial means, individuals only qualify for Medicaid assistance after depleting all their resources.

Few private mechanisms are available to help people plan ahead to pay for their future care. Long-term care insurance, by far the most popular private option available, can be costly and difficult to purchase, particularly for those with pre-existing health conditions or disabilities. Only about 2.8 percent of Americans currently have a policy. For workers who already experience a disability, the options are even more limited.

Through the CLASS Act, Congress sought to add a new option for American workers. The CLASS program's distinguishing features include an offer of lifetime benefits, lack of underwriting, availability of a cash benefit, and the fact that the program would be administered by the federal government.

As you have stated on a number of occasions, you cannot go forward with implementation of the CLASS program unless you determine that the benefit plan to be offered is actuarially solvent over the next 75 years and is consistent with the other requirements of the CLASS Act.

Over the last nineteen months, the Department has conducted substantial analysis of the CLASS statute and possible implementation options for a Federal long-term care insurance program, consistent with the CLASS Act. All of us who have worked on this issue appreciate your commitment to finding options for those who cannot participate in the current market. We share your view that the current lack of alternatives available to many middle-class Americans is unacceptable, as it can force people into poverty and avoidable institutionalization.

You charged the CLASS Office, ASPE, and OGC with performing a broad and thorough analysis to design attractive benefit plans and to determine if those plans met the twin tests of solvency and legality. Consulting individuals with a broad range of expertise, we worked with an in-house actuary and two outside actuarial firms. We subjected our actuarial modeling to expert review, and subjected potential benefit plans to thorough legal review.

The report attached to this memorandum describes this work. The report contains the results of actuarial and policy analyses of the CLASS Act and the legal analysis of various benefit plan options. This report contains important findings that will help advance the cause of charting a path to affordable and sustainable long-term care options.

### Analysis

In order to implement CLASS, we need to be able to identify a benefit design that is actuarially solvent (so that premiums are sufficient to fund the program given an assumed rate of participation), marketable (so that the assumed take up rate is reasonable), and consistent with the authorizing CLASS statute.

The design and implementation of the CLASS program involve two areas of tremendous uncertainty. First, because there is no precedent for the CLASS program in either the private market or in other government programs, such as Social Security or Medicare, there is great uncertainty around the assumptions used in the actuarial modeling to assess solvency. Second, while the CLASS statute requires that the CLASS plan be actuarially sound, and that no taxpayer funds may be used to pay plan benefits, it is silent about what would happen if, at some future point, actuarial soundness could no longer be achieved. It is uncertain whether, if the program could no longer go forward, those holding policies could be assured of receiving the benefits they had purchased, or could transition to other long-term care insurance programs (especially

since some might have developed medical conditions that mean they no longer can meet the underwriting requirements of private long-term care insurance). In light of these two types of uncertainty, it is critical that there be a high degree of confidence that the designated CLASS plan is fiscally sound and consistent with the statutory requirements.

We developed a broad range of alternative CLASS benefit plan options and used independent actuarial models and analysis by the CLASS Office Actuary to compute premium estimates and assessments of the actuarial soundness of the plans. These analyses indicate that the premium for the Basic CLASS Benefit Plan, which is the benefit design that follows from the most natural reading of the statute, produces a benefit costing between \$235 and \$391 dollars a month, and may cost as much as \$3,000 per month, if adverse selection is particularly serious. Moreover, the benefit in this plan, which calls for an average fifty dollar per day benefit for a beneficiary's lifetime, diverges significantly from the design most buyers in the private market choose. Most buyers prefer higher daily benefits over a few years. The benefit package described in the CLASS Act will make it difficult to attract purchasers who could otherwise meet underwriting requirements and obtain policies in the private market. If healthy purchasers are not attracted to the CLASS benefit package, then premiums will increase, which will make it even more unattractive to purchasers who could also obtain policies in the private market. This imbalance in the beneficiary pool would cause the program to quickly collapse.

We have identified potential benefit plans that could be actuarially sound and avoid the risk of adverse selection. These plans have benefit designs and premiums that appear marketable. Some of the characteristics of these plans include, for example, phased enrollment, higher earnings requirements for enrollees, and improved benefit design. All of these design options rely on the following strategies: they significantly increase the minimum earnings requirement specified in the statute, modifying it from \$1,120 to at least \$12,000 per year; they alter the benefit package so that it more closely resembles the typical package in the private market; and they phase enrollment in the plan, initially limiting eligibility to groups with better-than-average health risk profiles. While these benefit plan options show some promise in achieving actuarial solvency, they may be inconsistent with other provisions of the statute. There is concern regarding the legal authority for some of the plan features expected to increase solvency, and the more of those features that are incorporated into the plan, the greater the legal risk. In other words, as we take necessary steps to mitigate solvency risks, we concomitantly raise the legal risk that the plan could be found impermissible under the statute. If some of these solvency enhancements have to be changed, it is highly likely that the CLASS program could no longer continue and, as noted above, it is not clear whether the program could deliver on its commitment to those participants who had already enrolled.

### Recommendation

For the reasons stated above, I do not see a path to move forward with CLASS at this time. I recommend that we work with Congress and stakeholders, including consumers, insurers, and

employers, to continue exploring all of the options to address the critical long-term care needs of Americans.