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

The American Long-Term Care Insurance Program (ALTCIP)

By Paul E. Forte

Actuaries
Risk is Opportunity.[sm]

ALTCIP

The American
Long Term Care
Insurance Program

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Abstract: The American Long Term Care Insurance Program (ALTCIP) proposes a public-private partnership for financing long term services and supports (LTSS). At once an exchange that offers consumers greater access to affordable products and a mechanism for ensuring ongoing quality, the ALTCIP could increase the number of persons with private LTSS coverage in the next ten years, thus relieving government spending, while giving insurers themselves protections not available in the open market. A paper on the ALTCIP detailing its regulatory structure and operations was submitted to the Commission for Long Term Care in 2013. An abbreviated version was published in Contingencies *(January 2014) under the title "Fresh Thinking on Long Term Care."*

PAUL E. FORTE is Chief Executive Officer of Long Term Care Partners, LLC.

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The LTC Archipelago

It is more than 40 years since the 1980 US Census that underscored the coming age wave and how it would change everything. The private long term care insurance industry is at least as old. Its first generation products released in 1964. The public sector "LTSS" world is at least as old as Medicare, which called attention to what it was not supposed to cover even as it picked up the bulk of acute health care expenses for retirees. Long term care has attracted many bright and capable people both in the private and public sectors. Nevertheless, the LTC world is an archipelago, a group of islands separated by strong currents. There is of course contact among key participants, but it is intermittent.

Fig. 1: *The "Archipelago" of LTSS Stakeholders*

Each participant has its particular interest, its science or truth. Some work together better than others. So Congress/policy makers/regulators/media work together because they all court public recognition and approval. Brokers, insurers/reinsurers, and investors are of course linked by their mutual interest, chiefly profits. At best, LTC is a confederation with an imperfect understanding of its fellow participants and no strong links binding them together. It is a loose association of entities with little or no alignment and no common purpose.

Worse, the repeal of CLASS on the one hand, and the withdrawal of some 25 insurers from the LTCI market over the last decade, on the other, has created a kind of vacuum at the center that must be filled.

In truth, LTCI is a world with many players, all of whom are dependent on one another. The ALTCIP seeks to connect stakeholders within the LTC world who are currently isolated and apart. It seeks to foster a sense of common purpose by aligning public and private sectors, increasing financial transparency, and making better use of private resources hitherto not marshaled in an optimal way.

Fig. 2: ALTCIP Basics

What is the ALTCIP?

A proposed federally-sponsored and regulated national exchange for long term care insurance with advantages for both consumers and insurers. The ALTCIP:

1. Brings together the expertise of the private sector and the stability of the U.S. Government for the express purpose of financing LTC/LTSS
2. Offers consumers streamlined and attractively-priced LTCI products through a new, online exchange
3. Ensures accounting transparency via quality assurance performance management
4. Provides insurers with incentives, including large risk pools and access to reinsurance
5. Lessens reliance on government as source of LTC/LTSS funding

The ALTCIP is an exchange, if you will, but *an exchange with a difference*. In most exchanges, the purpose is to make a product or service available at an attractive price. The ALTCIP generate sales of LTCI, but it would also help to ensure that what is purchased remains appealing and provides fair value to consumers over the long term. This can only happen if 1) There is a structure in place that will monitor results over time; and 2) insurers think that such a structure works to their benefit because the terms they enjoy are also improved.

The ALTCIP would help carriers not by shifting more risk onto the heads of insureds, ultimately a self-defeating strategy, but by making more efficient use of available premium dollars, spreading risk more widely, and relieving surplus strain. This should allow insurance company boards of directors and investors to breathe easier.

The ALTCIP would promote “basic” coverage for the most pressing support services rather than specialized policies, at least initially. Offerings would be based on reliable claims event triggers, such as not being able to perform at least two of the six activities of daily living for what is expected to be an extended period of time, or cognitive impairment requiring close supervision. The ALTCIP would allow consumers to choose between levels and sites of care, giving them various price points, but they would also have protections that should be required of every LTCI policy, such as independent third party review for disputed claims, international benefits, and contingent non-forfeiture if rates exceed a certain level.

The administrator(s) would coordinate the ALTCIP as a program, provide marketing and enrollment support, streamline underwriting, and expedite claims and other functions such as aggregate reporting. The whole apparatus would be held together and run electronically, with a web-enabled operating system and workflows and automated self-service portals facilitating online application, claims submission and rate-increase or plan design substitution mechanisms. Automation, if well-designed, would reduce the cost of messaging, premium administration, plan changes, inflation adjustment, claims adjudication, invoices, complaints, etc.

Additional savings could be derived from replacing the current system of distribution, a costly one, with direct sales. The ALTCIP would not employ agents or other intermediaries in the normal distribution method; rather, prospective applicants would make use of a powerful website with education and decision tools, with well-trained call center representatives standing by for assistance. The Federal Long Term Care Insurance Program (FLTCIP) has demonstrated the success of this approach within the federal community, a very diverse population. In that program the elimination of high up-front commissions, usually a full year's worth of premium, has reduced consumer costs without capital strain and cash flow issues in the early years of a policy's life. Those objecting to what they think will be lost by foregoing the services of live agents should recognize that the ALTCIP would not be geared to high net worth individuals, but rather to moderate-income persons seeking better value and essential protection at a more reasonable cost. Agents would still reign in the most affluent segments of the market.

All ALTCIP enrollee premiums would go into a separate account or fund like the FLTCIP Experience Fund. Under this arrangement all assets associated with ALTCIP enrollees would be segregated from all other assets of the insurance carrier. Such assets could not legally be used by the insurer to meet other obligations. (More about this later.)

LTCI Claims would be handled by carriers themselves or with the help of administrators.

Federal vs. State Regulation

ALTCIP regulation would be managed not by the state but by the federal government. Feds would issue regulations, certify ALTCIP carriers, select one or more administrators via Federal Acquisition Regulation (FAR) contract bid, approve plans, review carrier and administrator performance, determine profit charge awards, and conduct audits. The ALTCIP would follow efforts by the Federal Insurance Office (FIO), a new department of the U.S. Treasury established under Dodd-Frank, to create a modernized foundation for financial regulatory reform. The ALTCIP would benefit hugely from pre-emption from state insurance regulation, much as has the Federal Long Term Care Insurance Program (FLTCIP).[1] Federal agencies like DHHS and OPM,

[1] Those who have worked on the NAIC Interstate Compact will no doubt be disappointed to hear that the ALTCIP would go the federal route. The NAIC has worked hard to improve LTCI regulation. The compact now sweeps in 44 states, and the NAIC has developed a framework for Credit for Reinsurance Model Law (#785) and Regulation (#786), which are geared to modernizing and improving reinsurance regulation nationally. Nevertheless, the NAIC framework has not been implemented. Under the Nonadmitted and Reinsurance Reform Act of 2011 this

which are already dealing with programs designed to cover LTSS/LTC, would sponsor and regulate the ALTCIP under Congressional statute. So could the Department of Treasury. Legislation would be required in the form of a bill, which would mean that a Congressional sponsor would be required.

Fig. 3: ***Federal vs. State Regulation of LTSS/LTCI***[2]

	Federal	State
Strengths	• Uniform approach simpler, better for mobile population • Lower net costs with capital and cash-flow advantages • Better at dealing with non-traditional activities of traditional insurers like AIG (e.g., derivatives trading/CDS, securities lending) • Advantageous for development of international insurance supervisory standards (IAIS/ComFrame) • FLTCIP Experience as track	• Many products tailored to and delivered at local level • Agreements among states to achieve some uniformity (Interstate Compact, NARAB II, SMART Act) • State Guaranty Funds
Weaknesses	• Attention, commitment to insurance vs. banking, other financial products • Expertise may be lacking • Experience lacking in direct regulation of most lines of insurance	• 56 independent jurisdictions; duplicative, inconsistent • Expensive to maintain • Entities whose businesses span multiple jurisdictions • Dealing with reinsurers, captives, other special entities

State regulation by 56 independent jurisdictions, a system that dates back more than 130 years, remains a thicket for consumers and carriers alike. Consumers must deal with protections that vary from state to state (and in some cases erratic pricing), while carriers must manage a host of issues that continue to dog them, including risk-based capital standards that are not applied uniformly across states, different rules for reinsurance risk diversification, different rules for captives and special purpose vehicles, and different rules for market conduct. A 2009 McKinsey study found that the cost of state-based regulation is more than seven times greater than that

framework would preempt the extraterritorial application of state credit for reinsurance collateral law and permit states of domicile to proceed with collateral reinsurance reforms.

[2] Sources: "Financial Regulatory Reform / A New Foundation: Rebuilding Financial Supervision and Regulation," U.S. Department of the Treasury white paper, June 2009; "How to Modernize and Improve the System of Insurance Regulation In The United States," Federal Insurance Office, U.S. Department of the Treasury, December 2013, and McKinsey & Co., April 2009.

for federal. With its uniformity, consistency, and lower cost, federal regulation of LTCI would seem a real advantage.

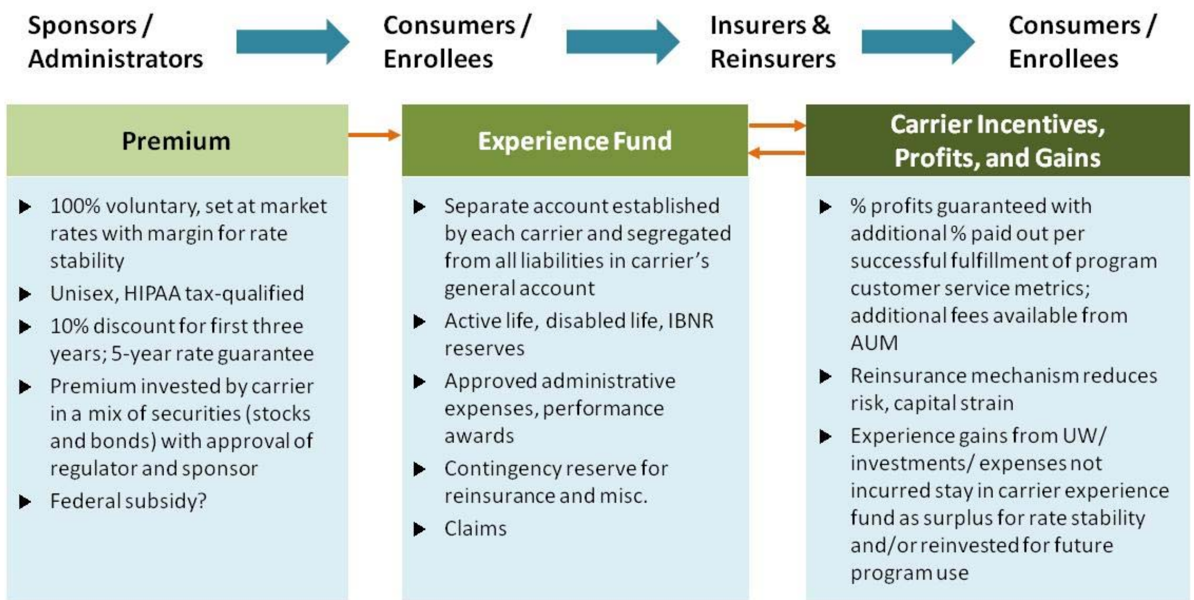
Premium and Experience Fund

Premiums would be 100% voluntary unless the feds offer to subsidize. These would be funneled through the administrator, who would set up the exchange and build its enrollment and premium portals. Premiums, level or step rated, would be guaranteed for five years for those who apply and are approved in the initial enrollment period. After this period, premiums could increase. [3]

Premiums would go into separate accounts called "experience funds," as noted above. These funds would capture all experience-based gains from underwriting, investment, administration, and investment of assets under management. Experience funds would be completely segregated from other insurer assets and thus protected from call for other liabilities of the insurer, and would be invested in a prudent mix of securities, stocks, and bonds, for long term growth and stability (*for a detailed diagram of the ALTCIP funding mechanism, see Appendix I*).

[3] Some may object that this is the situation that commonly prevails in the market today. While it is true that the ALTCIP would allow rate increases, ALTCIP benefits would not reduce unless the enrollee chose such an option in lieu of the increase. Thus the ALTCIP experience fund is different from that put forward by Roger Loomis, who makes LTCI benefits variable, with amounts rising and falling in accordance with the experience of a fund in which each policyholder purchases shares. See "Land this Plane: A Delphi Study of Long-Term Care Financing Solutions," by John O'Leary, March 2014.

Fig. 4: ***ALTCIP Funding Structure***



Insurer, reinsurer, and administrator(s) risk and profit charges would effectively be capped via a formula that would be negotiated with the federal sponsors and regulators. This formula would guarantee only a portion of the profit. The rest would have to be earned by meeting or exceeding a set of metrics geared to ensuring high quality. Failure to meet metrics would mean earnings less than the contractual profit available. Unpaid profit would remain in the carrier's experience fund.

Finally, an additional percentage of premiums would be set aside for reinsurance. Reinsurance would be mandatory for all insurers offering LTCI products through the ALTCIP. Such reinsurance would be facilitated by the ALTCIP administrator or could be purchased directly by carriers in the global reinsurance market, who, with federal government actuaries, would negotiate a standard reinsurance treaty (*see p.11 for further details*).

Voluntary vs. Mandatory Approaches

Some will contend that the ALTCIP cannot succeed, because voluntary approaches—whether private, as we have seen in market policies, or public, as in the recently withdrawn CLASS Act—mean lower participation, more anti-selection, and a smaller base over which to spread fixed costs. These, it is argued, will not reduce Medicaid dependency, much less help the large numbers of people who are now already frail and in need of services.

While it is true that a voluntary program may not post the same numbers as a mandatory one right out of the gate, the ALTCIP's lower expense structure coupled with national scope and longevity should mean larger numbers of applicants (especially if a limited-time discount were offered), unprecedented economies of scale, and more assets under management, among other advantages. The new Affordable Care Act exchanges have generated between 7.2 and 9.3 million voluntary enrollments, according to a June 4, 2014 article in *Forbes*.[4] It is hard to argue that scale in LTCI is impossible to achieve, unless one questions the value of the product. LTCI does not offer the same instant gratification as health insurance, whose value is immediately apparent. But again, one must view the offer of LTCI within a new framework, one marked by increased longevity and strained financial resources. A program that has strong government endorsement and participation by major insurance carriers is bound to get attention.

One way to boost participation in a voluntary scheme is to liberalize underwriting requirements, a feature of most group LTCI plans for more than 20 years. But whereas many group plans guarantee issue to active employees, and occasionally to active employee spouses, the ALTCIP would require some degree of medical evidence underwriting to prevent immediate claims and to minimize the risk of a rate spiral. The ALTCIP might allow for some underwriting concessions, including admitting certain pre-existing conditions contingent upon the applicant's willingness to accept a vesting period. A vesting period could be two years, three years, or—as was the choice of CLASS—five years. That program, because it was repealed, did not have a chance to test the efficacy of its five-year vesting requirement, so we cannot be sure what the results would have been. But a vesting period either in addition to liberalized underwriting or in place of it would allow more people to receive coverage, increasing the size of the risk pool and spreading overhead.

[4] Caressi, Greg, "ACA: Now Serving Millions...So Far" (*Forbes*, 6/4/2014)

Fig. 5: Pros and Cons of Voluntary vs. Mandatory Funding Approaches[5]

	Voluntary	Mandatory
Strengths	• Allows for greater flexibility and choice • Higher benefit packages available to meet all levels and sites of care • Minimal costs to taxpayers • Adequate size for economies of scale • Not subject to means testing or freezes	• High participation • Minimal anti-selection • Administration expense spread over wider base • Will help large numbers of working people who are disabled • Could reduce Medicaid dependency because many more people covered
Weaknesses	• Medical underwriting • Smaller risk pools, never reaching 100% • Anti-selection risk high • May not help working people who are already disabled • May not reduce Medicaid dependency significantly	• Eligibility requirements • Long vesting periods • Supported by tax revenue/subsidies • Subject to change (budget cuts, freezes) • Daily benefit modest • Benefit/rate increases could require tax increases

Against such terms the mandated benefit appears deficient, aside from its accessibility. Most mandated benefits put forward as part of a social insurance program are small. They are geared to home and community-based care. While such care is in demand, it may not be the kind of care needed in the later phases of dependency. But those phases arrive, as anyone who has tried to maintain an Alzheimer's or dementia patient at home knows. It is doubtful whether any mandated benefit would be able to provide comprehensive care, including care in a nursing facility, as the cost would simply be too high.

Reinsurance and Other Forms of Stop-Loss

Reinsurance has not been much used by the industry in the last decade due to requirements by reinsurers to review the acquisition of underwritten business, inconsistencies with credit for reinsurance among states, and uneasiness with captive reinsurance. As already stated, reinsurance would be mandatory in the ALTCIP. Reinsurance premiums would be collected

[5] See Tumlinson, et al, "Insuring Americans for Long-Term Services and Supports: Challenges and Limitations of Voluntary Insurance," *Avalere Health*, March 2013.

automatically and debited from the carrier's contingency fund to ensure the spread of risk necessary for premium stability over the long term. The ALTCIP would offer a standard reinsurance agreement, pre-negotiated with commercial reinsurers. Carriers could opt out in favor of a comparable separate reinsurance arrangement or cede to unauthorized reinsurers via letters of credit, Regulation 114 Trusts, funds withheld, and other methods of collateralization. It is not too of a stretch to anticipate that reinsurers might themselves ceded risk to retrocessionaires in the international risk markets.

While the industry has used coinsurance or quota share in the past, such arrangements have limited practical financial utility to carriers as they only split premiums, reserves, and profits; they do not affect the ratio of capital to policy issued, nor do they reflect parameter risk, where incidents occur at unpredictable intervals within certain periods of time. An excess of loss arrangement would be better for carriers, as it would limit outside risk, but this wouldn't allow reserve or capital relief, as risk would remain on the carrier's books until a certain limit was reached—and of course, there would be less in it for reinsurers themselves. All of this would have to be worked out. But I think that a massive program, under federal auspices, offering more uniform rules and presenting fresh opportunity, could bring reinsurers to the table, with advantages for everyone.

Another form of reinsurance involves investors. An insurance carrier wishing to mitigate risk can issue a catastrophe bond, as we are seeing in the property and casualty market. The carrier issues a bond for a certain amount of protection it wishes to have. This protection is usually above a limit that it is comfortable with. Investors are paid a competitive rate of interest for a certain term, say five years. If claims experience exceeds the stipulated limit, the insurance carrier issuer has the right to retain interest, and, if necessary, principal. There is some $11 billion outstanding in such bonds giving issuers protection against tornados, hurricanes, and other natural disasters, even climate change[6]. The LTCI industry should evaluate such an

[6] See Sarah Mortimer, "PCS Eyeing $11 Billion Sandy Loss Estimate," reuters.com, November 23, 2012. For ways that insurers are covering risks associated with climate change, see Robert J Shiller, "Buying Insurance Against Climate Change," May 24, 2014.

arrangement for excess loss associated with long term claims caused by Alzheimer's, dementia, Parkinson's, and other catastrophic risks.

Of course, it is also possible that the federal government could offer a backstop as an alternative or in conjunction with ALTCIP reinsurance. There are many examples of federal backstops that have been introduced when information needed for underwriting a risk was not available (National Flood Insurance Program), when losses exceeded anything imaginable (Terrorist Risk Insurance Program), or simply when private markets failed (home mortgage market in the 1930s and again in 2008-2009).

Some might think such a mechanism in the context of long term care implausible. But it is only implausible if you look at a risk as being a purely private matter, as opposed to one having significant public or social consequences for a nation and an economy. The cost of an immediate backstop for LTCI set up out of general revenues would be miniscule when compared to the staggering sums taxpayers are carrying each year for Medicaid LTC—over $200 billion in 2012, taking into consideration both federal and state payments.

Conclusion

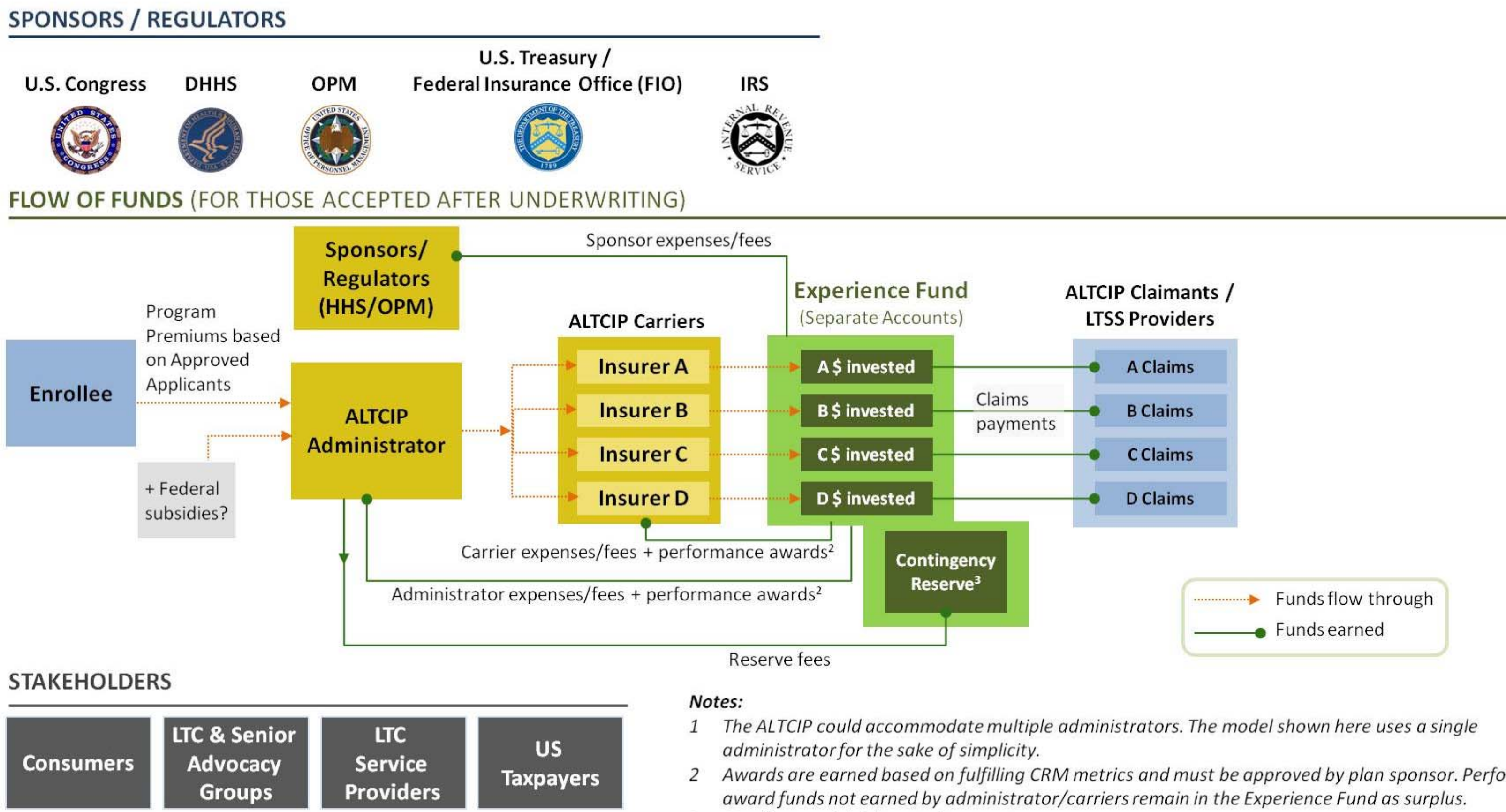
The ALTCIP is not a panacea. It would not address the needs of every American requiring LTSS/LTC in the future. Nor, given the number of its moving parts, would it be easy to operate. Big questions remain, such as what plan designs would be offered, what underwriting guidelines/vesting periods would be required, what reinsurance treaties would be feasible, would a federal government subsidy prove necessary or effective, would the federal government have the expertise to run such an exchange, how the ALTCIP would interact with updated Medicare and Medigap polices, etc. Modeling is required before these questions can be satisfactorily answered.

I have not had the resources to do modeling—but even without it, the advantages of the ALTCIP are evident. The ALTCIP would address deficiencies of current private market stand-alone LTCI by a structure that promotes attractive, well-designed and affordable policies;

generates applications via powerful online self-service portals; lowers processing expenses through other forms of automation; spreads risk; and reduces capital strain. Assuming average claims utilization and persistency rates for those on Medicaid, taxpayers could save $50 billion a year down the road in future Medicaid expense for every million persons who enrolled in the ALTCIP.

One thing is clear: without some such mechanism as the ALTCIP in the near future, taxpayers will be assuming the expenses of the remaining large cohorts of baby boomers, millions of whom will be turning age 65 each year for the next 20 years. The massive tax increases needed to cover such costs will weaken our economy, which is already in a fragile state, owing to long-standing entitlements like Social Security and Medicare, and costs associated with ACA. Long term care threatens to narrow the horizon of future generations. The ALTCIP could make a difference.

Appendix I: Single Administrator/Multi-Carrier Model



Notes:

1. *The ALTCIP could accommodate multiple administrators. The model shown here uses a single administrator for the sake of simplicity.*
2. *Awards are earned based on fulfilling CRM metrics and must be approved by plan sponsor. Performance award funds not earned by administrator/carriers remain in the Experience Fund as surplus.*
3. *Used for special risks or reinsurance.*

The ALTCIP Single Administrator/Multi-Insurer Model assumes several underwriters/carriers but one administrator (ALTCIP administrator), which would function like a general contractor and could subcontract various functions. Premium would flow through the ALTCIP administrator to the insurers who would establish separate accounts called Experience Funds. A percentage of the premium would be withheld by the ALTCIP administrator in a special contingency reserve. This would be used to finance a credit system for special risks assumed or to purchase reinsurance. Additional fees set aside within the Experience Funds would be used to provide incentives for the administrator and insurers to hit certain annual performance metrics designed to ensure good customer service, such as telephone support, turning around applications, and paying claims. Any credits or performance awards not made would be held in the Experience Funds and become unallocated surplus.

Appendix II: Key ALTCIP Provisions

Legislation	Federal statute created by an Act of Congress		
Sponsorship and Regulation	Federal regulation preempts state rules under broad umbrella of Dodd-Frank 2010, Federal Insurance Office, US Treasury. Sponsored and regulated by DHHS or OPM, who selects carrier(s) and plan administrator(s) via public bid, and audits program. Regulations published in *Federal Register*.		
Plan Administration	One or more administrators chosen by federal bid under Federal Acquisition Regulation (FAR). Customer service support backed by performance-based metrics (administrator loses profit if not met). <u>Role/functions</u>: marketing and promotion, enrollment, UW, premium administration, web portals, care coordination, benefit eligibility determinations, IT, claims adjudication, reporting.		
Insurance Carriers	Chosen by federal bid. Must meet minimum surplus requirements to qualify <u>Role/Functions</u>: risk assumption, policy issuance, pricing, UW guidelines, asset management Profit partially determined by performance-based metrics		
Plan Eligibility	US legal residency; any age; must pass medical underwriting. Applications online or paper-based		
Financing	*Premium contributions*: Voluntary, Unisex *Premium adequacy*: must be modeled and demonstrable for all risks assumed on present value basis out to 75 years	*Premium structure*: level or step-rated *Payment methods*: payroll/annuity deduction, auto-bank withdrawal, direct billing. Claims reimbursed via electronic fund transfer (EFT) Possible augmentation via tax deductions/subsidies; tax-qualified under HIPAA	
Coverage and Benefits	Guaranteed renewable DBA options: $100, $200, $300, $400 Length of coverage: 2, 3, 5 years Inflation protection: 3% or 4% compound, FPO Waiting period/deductible: variable	2 of 6 ADLs or cognitive impairment Claims: reimbursement benefit or indemnity Comprehensive care: skilled, intermediate, custodial Eligible sites of care: HCBC, ALF, Nursing home, adult day care, informal	
Additional Plan Features, Consumer Protections	International benefits Care coordination	Hospice care, respite care Stay-at-home benefit	Independent third-party review of claims International benefits (paid at % of domestic claims rate)
Risk Management	*Reinsurance*: Mandatory for insurers; standard reinsurance agreement provided by ALTCIP with option to opt out.	*Federal backstop*: Federal government as reinsurer guaranteeing a percentage of losses in excess of certain levels, less a deductible based on earned premium, or as bank indemnifying losses and then recouping them with interest through future policy surcharges, to be split between insurers and insureds	
Marketing, Education, Promotion, Outreach	Plans sold direct (no agents or commissions) Website w/interactive tools (comparison, rate calculator, cost of care)	Call center staffed with professional, salaried call center reps Online presentations, live + archived webinars, videos, prospect + enrollee podcasts Promotional campaigns utilizing e-mail, social media	
Other Considerations	Could be offered as stand-alone protection or supplemental to basic social insurance program. Could be made State Partnership-compatible		