EBRI

T-61

Statement of

Dallas L. Salisbury,
Robert B. Friedland, Ph.D.,
and
Deborah J. Chollet, Ph.D.

Before the
United States Senate
Committee on Finance
Subcommittee on Health
May 27, 1988

*Dallas L. Salisbury is president of the Employee Benefit Research Institute in Washington, D.C.; Robert B. Friedland is research associate, and Deborah J. Chollet is senior research associate. The views expressed in this statement are solely those of the authors and should not be attributed to the Employee Benefit Research Institute, its officers, trustees, sponsors, or other staff.

EMPLOYEE BENEFIT RESEARCH INSTITUTE
2121 K Street, NW / Suite 600 / Washington, DC 20037-2121
Telephone 202-659-0670 FAX 202-775-6312

SUMMARY

Introduction

- Among the general population, recognition that neither Medicare nor most private insurance plans cover long-term care has come slowly.

- Since few people have recognized the likelihood of needing long-term care, most do not plan to save sufficiently to finance care or budget to purchase insurance.

Employer Response

- A growing number of employers are looking to more orthodox insurance models to help employees finance long-term care.

Employer experience with retiree health insurance

- New accounting procedures recognizing accruing liability for retiree health insurance could influence employers' willingness or ability to assume responsibility for paying long-term care insurance premiums.

Long-term care as an employee benefit: an emerging market

- The limitations in the policies developed so far reflect insurers' hesitation to commit to long-term care insurance products as a result of insufficient data and uncertainty over present tax law.

Long Term Care Insurance as an Employee Benefit

- Insurers' tentativeness about entering the long-term care market has been matched by employers' reluctance to institute new benefits or to assume additional health care financing obligations for workers and retirees.

Goals of a System of Long-Term Care Financing

- The development of an insurance system.
- Adequate coverage.
- Universal access.
- Flexibility.
- Efficiency.

Conclusion

- The Committee faces a difficult challenge as they confront the complexities of this issue. Senator Mitchell has articulated the major issue clearly: "The policy issue we face is how to target our limited resources to the elderly that are most in need."

- Through tax incentives, the federal government now encourages a substantial and growing system of pension provision for retirees. That system provides an important part of the income that could pay for long-term care insurance and now helps finance long-term care services.

- We commend the Committee for undertaking the challenge of structuring a workable system of long-term care financing in the United States, and stand ready to assist the Committee in its efforts.

Introduction: the Long-Term Care Insurance Gap

Among the general population, recognition that neither Medicare nor most private insurance plans cover long-term care has come slowly. Retirees and workers have only begun to understand their exposure to the risk of needing costly community or institutional long-term care, as an increasing number have faced the desperation of caring for a parent, spouse or child needing chronic (and often increasing) assistance for personal care. Currently, an estimated 13 million people, or 5 percent of the population, require such care. Since few people have recognized the likelihood of needing long-term care, most do not plan to save sufficiently to finance care or budget to purchase insurance.

Employer Response

Employers' response to this new understanding has been mixed. New employee benefits, usually provided through employee assistance programs, have been formulated to assist workers in caring for disabled dependent parents, spouses and children. These programs include financial planning services, personal and family counseling, support group therapy, service referral and assessment and placement services, as well as adult day care. Flexible hours and leave arrangements also assist workers with disabled dependents. In addition, a growing number of employers are looking to more orthodox insurance models to help employees finance long-term care.

Employer experience with retiree health insurance

The employer cost of providing health insurance to active workers,

retirees and dependents has been increasing at rates two to four times the rate of general inflation. With plan costs uncontrolled despite employers' attempts, health insurance has become a significant source of unpredictable labor costs. Not surprisingly, employers have devoted substantial attention to attempting to limit and control their health plan liabilities.

New accounting standards, currently under development by the Financial Accounting Standards Board (FASB), are likely to force employers to focus on a variety of issues concerning their retiree medical benefits. In an exposure draft to be issued later this year, FASB is likely to require that employers estimate accrued liability for retiree health benefits, and include unfunded liability as a balance sheet entry; funding would become an income statement expense. For many firms unfunded liability for retiree health benefits is substantial relative to assets; annual plan expense is a significant percent of active worker pay. The anticipated FASB accounting rules could jeopardize their ability to raise capital and maintain present employee benefit programs. For publicly owned firms, bond and stock prices are likely to be adversely affected as lower corporate earnings are reported. New accounting procedures recognizing accruing liability for retiree health insurance could influence employers' willingness or ability to assume responsibility for paying long-term care insurance premiums.

Long-Term Care As An Employee Benefit: An Emerging Market

Interest in long-term care insurance among the public and among insurers

has grown substantially, raising the number of policy options and policy holders more than four-fold in the past few years. At least nine large employers have established long-term care as an employee-pay-all benefit, enabling access to coverage by tens of thousands of employees. Most of these plans recognize employees' parents as qualified dependents.

This market has emerged against overwhelming odds. Products have been structured and priced without sound actuarial data. State insurance regulations and federal tax laws are confusing and ambiguous. Recognizing that most states have no laws explicitly governing long-term care insurance, the National Association of Insurance Commissioners (NAIC) developed a model act and regulations to assist state legislators. At this time, 25 states have enacted some type statute governing private long-term care insurance; 15 have based their legislation on the NAIC model act. Another seven states have pending legislation based on the NAIC model.

Ambiguity in the Internal Revenue Code regarding the tax status of long-term care insurance reserves has affected the pricing and selling of insurance products. By one estimate, premiums could be as much as 11 percent lower for insurance purchased at age 65 if long-term care insurance reserves were given the same tax status as life insurance reserves.[1] For consumers, it has not been clear whether either the benefits received or the premiums paid would have the same tax treatment as other health insurance benefits or premiums.

---

[1] U.S. Department of Heath and Human Services, "Catastrophic Illness Expenses." Report to the President, p. 78 (November 1986).

Other barriers to consumer interest in purchasing commercial long-term care insurance include: (1) confusion about the long-term care coverage provided by accident and health insurance, Medicare, retiree health plans, Medigap policies, and Medicaid; (2) ignorance or confusion about the lifetime risk of incurring a disabling condition; and (3) denial by many individuals that life contains this contingency. The anticipated cost of public education necessary to market commercial long-term care insurance has been a significant barrier to market development.

Nevertheless, this market is emerging without a full understanding among providers or policy makers of what constitutes effective long-term care delivery, how alternative forms of reimbursement affect delivery, how to objectively assess patient needs, or how to coordinate care among different providers and sites. Finally, this market has emerged without clear legislative signals from the Congress.

The limitations in the policies developed so far reflect insurers' hesitation to commit to long-term care insurance products. Although many insurers are attracted by the profit opportunities of a new insurance line, they recognize the difficulty of limiting their financial liabilities yet offering a product attractive to consumers.

Long Term Care Insurance as an Employee Benefit

Insurers' tentativeness about entering the long-term care market has been matched by employers' reluctance to institute new benefits or to assume

additional health care financing obligations for workers and retirees.[2] Frequent and pervasive legislative changes affecting their tax-qualified plans have exacerbated their apprehensions about providing long-term care insurance.

Nevertheless, in the last two years, at least nine employers have offered access to a long-term care insurance product to some part of their current or former workforce. At least six additional employers have publicly expressed their intention to sponsor long-term care insurance. A recent survey of 144 large companies indicated that 55 of these companies had or were then investigating the feasibility of long-term care as an employee benefit. Among those who had not, 38 companies anticipated conducting an evaluation in the next two years.[3]

Employer-sponsored long-term care plans typically have been made available to active workers, their parents, and retirees. With one notable exception, employees pay the entire premium. Separated employees have been able to continue coverage by paying the premium at the same rate plus a charge for administrative cost.

Annual premiums are typically age-related, ranging from $120 to $158 for individuals purchasing at age 30, and $204 to $384 for individuals initially

---

[2] Issues related to financing long-term care as an employee benefit are discussed in D. J. Chollet and R. B. Friedland, "Employer Financing of Long-Term Care." In R. M. Scheffler and L. F. Rossiter, eds. Private Sector Involvement in Health Care: Advances in Health Economics and Health Services Research 9 (Greenwich, CT: JAI Press, 1988).

[3] R. Levin and R. Frobom, The Corporate Perspective on Long-Term Care: Survey Report (Appendix 2) (Washington, DC: Washington Business Group on Health, 1987).

purchasing coverage at age 50. In at least one of these plans, the premium for an initial purchase at age 75 is $1,800 a year.

For nursing home care, these plans pay $50 to $100 per day; for home health care, they pay $20 to $50 per day. Some plans do not pay for care necessitated by Alzheimer's Disease.

Each plan limits plan liability, typically imposing a lifetime maximum of four years of nursing home care (or the dollar equivalent) and a 90-day deductible or exclusionary period. Some plans offer an option to index benefits, accommodating increases in the cost of care; some will return part of the premium if the covered person dies before using any benefits. Preliminary information suggests that the average age of the purchasers of this employment based coverage is about 40.

So far none of these products have been true group products: individuals can be denied coverage due to an existing or past medical condition. Nevertheless, these products offer the consumer considerable savings over searching for and purchasing individual products. In particular, the costs of administration (unless the employee leaves the firm) and, more substantially, the marketing expenses (including sales commissions) are less and are likely to be paid by the employer.

Goals of a System of Long-Term Care Financing

In debating alternative systems of long-term care financing, a number of

general goals can be articulated for any system. These include:

- o The development of an insurance system. By spreading the cost of long-term care need among a larger population than those immediately at risk, insurance would rationalize long-term care financing. This insurance system may be mostly private, mostly public, or a combination of private and public.

- o Adequate coverage. Adequate coverage would guarantee access to needed care without imposing on participants unreasonable levels of uninsured, out-of-pocket expense.

- o Universal access. The system should be accessible to all members of the population. This goal raises issues of affordability for participants. If the system relied on asset accumulation to finance long-term care, this goal also raises issues of portability and asset preservation. Finally, it raises the question of coordinating long-term care financing with individual retirement saving and pensions (for example, targeting pension annuities for long-term care insurance).

- o Flexibility. Any financing system should accommodate individual preferences for alternative forms of service delivery, including community-based care, institutional care, and composites of residential, medical and personal care services such as life-care communities. The system should also recognize families and assist them in providing long-term care.

- o Efficiency. Any financing system should pay providers in a manner that encourages cost-efficient service delivery and readily accommodates technological change.

Any of a number of alternative financing systems might meet these goals. S. 2305 would encourage a mixed, private-public insurance system. To encourage the private market, the bill would clarify various tax code provisions related to employer-sponsored and individual long-term care insurance plans, extending to qualified plans the same tax treatment as health insurance. Qualified plan reserves (contributions and earnings) would be tax exempt, in the same manner as life insurance reserves are exempt, lowering premiums and encouraging wider participation. Conceivably, acute and long-term care coverage could be underwritten in the same insurance plan,

expanding case managers' options in planning care for high-cost cases. Also, S. 2305 establishes employer-based long-term care insurance as a welfare plan, presumably extending ERISA protections from state taxation and regulation and establishing fiduciary standards for plan administration. By establishing long-term care as a qualified cafeteria-plan benefit, S. 2305 also allows employer-based plans to be wholly or partially employee-financed with pre-tax earnings.

However, S. 2305 does not clearly address issues that relate to ensuring that workers have long-term care coverage at the point of greatest probable need: after retirement. Current employer group products rely on asset accumulation. Premiums are priced according to the participant's entry age (older new participants pay more for coverage than younger new participants) and participants can maintain coverage by continuing premium payments after they separate from the group. Since these plans are relatively new, we have no experience to suggest the rate at which terminated employees actually continue coverage. Experience with employees failing to transfer preretirement lump-sum pension distributions into tax-qualified individual retirement accounts, however, is not promising. It is likely that a significant number of workers who separate from a long-term care insurance plan will fail to continue payment if they anticipate no immediate need for benefits. In the context of private pensions, the Congress is now considering issues of asset preservation and portability to ensure an ultimate stream of income for retirees in return for tax incentives (S. 1349). These issues are critical components of other programs designed to provide economic security for retirees.

Conclusion

The Committee faces a difficult challenge as they confront the complexities of this issue. Senator Mitchell has articulated some major issues clearly:

> The policy issue we face is how to target our limited resources to the elderly that are most in need.... I believe that the insurance industry will respond to the demand for long-term care insurance with the development of policies to meet the needs of our aging population.

Through tax incentives, the federal government now encourages a substantial and growing system of pension provision for retirees. That system provides an important part of the income that could pay for long-term care insurance and now helps finance long-term care services.

We commend the Committee for undertaking the challenge of structuring a workable system of long-term care financing in the United States, and stand ready to assist the Committee in its efforts.