SOCIETY OF ACTUARIES

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

Compilation of Abstracts

The following is a complete listing of the abstracts for each paper in the
2014 Long-Term Care monograph

Copyright 2014 by the Society of Actuaries.
All rights reserved by the Society of Actuaries. Permission is granted to make brief excerpts for a published review. Permission is also granted to make limited numbers of copies of items in this monograph for personal, internal, classroom or other instructional use, on condition that the foregoing copyright notice is used so as to give reasonable notice of the Society's copyright. This consent for free limited copying without prior consent of the Society does not extend to making copies for general distribution, for advertising or promotional purposes, for inclusion in new collective works or for resale.

Actuaries
Risk is Opportunity.[sm]

Abstract

The Impact of Long-Term Care Costs on Retirement Wealth Needs

Vickie Bajtelsmit and Anna Rappaport

This paper provides an overview of the risks and costs of long-term care (LTC), including a discussion of who bears the risk, and the advantages and disadvantages of various funding mechanisms for long-term support and services. A summary of recent simulation studies provides evidence regarding the size of the risk and the impact on household financial well-being. We conclude that advance planning for LTC risk is critical for low- to middle-income households. For other than the wealthiest households, the cost at the retirement date of any LTC financing strategy will likely be prohibitive and may deplete household emergency funds. For those with greater wealth and income, paying for LTC costs as they are incurred may be a workable option.

Abstract

How American Society Will Address Long-Term Care Risk, Financing and Retirement

John Cutler

While long-term care (LTC) expenses can be devastating to individuals and society, the premise of this paper is that few proactive measures are in play to address the problem. Notwithstanding the risk to the lifetime financial security plans of individuals and households, the management of this risk is uneven. Likewise societal response (synonymous for this purpose with government) is erratic and lacking in focus.

If this is true—that few solutions are being put into play today to take care of tomorrow—what happens when tomorrow comes? In spite of the exhortation by many experts that solutions must be created today, it is more likely that individuals and society will procrastinate. This will result in the adoption or adaptation of whatever mechanisms or options are available at the time. In essence, what if we have a crisis and no one comes? What if we muddle along and do nothing? Or rather, at best, we only move forward with incremental public initiatives, and the private sector similarly makes marginal product changes. What does America look like if we ignore all the warnings?

This paper uses a literature search and reflective analysis of current programs and policies to lay out a path by which these tools could be employed. The review covers Medicare, Medicaid, health insurance, LTC insurance (including life and annuities), Social Security, pensions, housing and reverse mortgages as well as family, caregiving and the workforce. What is clear is that a variety of approaches, both public and private, are currently available to address LTC risks. In fact, it might well be that we ARE seeing LTC reforms underway but too incremental (and fragmented) to be obvious.

So the tenet of the paper is *not* that there won't be changes in the way insurance and retirement will be addressed. To the contrary, it seems probable that there will be a wide array of policy proposals or product ideas to address the growing number of individuals moving into older ages and retirement. In addition, it is clear that there will be both a public as well as private component. Even if a private market option is chosen, it has to have government involvement. Both empirical research as well as expert opinion hold that the government must be involved as a key player. But, by the same token, the government can only do so much, which means, in turn, a social insurance solution also cannot be chosen as the only answer.

Abstract

Improving Retirement by Integrating Family, Friends, Housing and Support: Lessons Learned from Personal Experience

By Anna Rappaport, FSA, MAAA

This paper provides insights about choices made with regard to housing and supportive services based on personal experience with family and friends. The first experience is about my mother and her choices that involved a move into independent living, assisted living, and ultimately a nursing home. The second story is about an individual interested in a continuing care retirement community (CCRC) and that individual's attempts to investigate CCRC options. The third story relates to people who live in a community where residents help each other out. All of the stories offered insights, most of which were not obvious to me, and which so far as I know, are not easy to find in the literature. Additional insights come from discussions with friends who have been involved.

Some of the questions explored include:

- Is moving out of my home a good idea? Under what circumstances?
- What choices do different models offer you?
- How important is it to have a support system nearby?
- What are some of the potential pitfalls and traps in a CCRC with a large down payment?
- What should you think about in evaluating options for special housing?
- Where do friends, children and family members fit in?
- How much can you plan ahead?

The personal experiences are supplemented with research and some data, including a few cost examples.

Abstract

The 65-Plus Age Wave and the Caregiving Conundrum: The Often Forgotten Piece of the Long-Term Care Puzzle

By Sandra Timmermann, Ed.D.

Both family caregivers and those who work as paid caregivers are the backbone of the long-term care system, but are often the forgotten link in the long-term care financing discussion. Families continue to provide the lion's share of care. It is estimated that there are approximately 65 million caregivers, representing nearly 39 percent of the population; 7 in 10 are working. Family caregivers are stretched to the limit, juggling work and caregiving responsibilities, which takes a toll on their personal health and finances. Paid caregivers are a critical element in the care continuum, both in the home and in facilities, but with low wages and few opportunities for advancement, the jobs are difficult to fill, turnover is high. and the potential for elder abuse is always present.

With the aging of the baby boomers and the prospect that many of them will live into their 80s, 90s and beyond, it is critical to address the caregiving crisis and come up with supportive mechanisms, financing strategies and creative solutions to meet this growing need. The subject is not only of concern to families and public policymakers, but also to the financial services industry as it develops new long-term care products and services.

There are four inter-related factors that should bring caregiving issues to the forefront in policy discussions:

- The increasing reliance on family members as the primary caregivers and the impact of caregiving on their health, employment status, and financial security, as well as on their productivity in the workplace, which impacts the employer;
- The rise of the aging-in-place movement, which points to the need for community-based infrastructures and financial solutions to support the care recipient and the family;
- The impending shortage of paid caregivers, holding low-wage job such as home health aides, nursing assistants and personal care aides; and
- The rising cost of long-term care services and the lack of personal planning for a long-term care event, impacting the finances of both the care recipient and the family.

The paper provides an overview of the situation, including current data, in each of these four areas; highlights some innovative programs and initiatives that are underway by communities, employers and policymakers; and offers some "blue sky" strategies and solutions for both the public and private sectors to bring these issues to the top of the national agenda.

Abstract

Home Equity and At-Need Annuities—A Dynamic Long-Term Care Funding Duo

Steve Cooperstein, FSA
Steve Cooperstein & Affiliates
http://www.InnovatingBeyondThe9Dots.com

In the mid-'80s, when AIDS struck the gay community, viatical settlements were created enabling terminally ill life insurance policyholders to tap into the stored legacy value of their policies to pay for treatments or otherwise use these monies while they lived. In a somewhat similar vein, in the late '90s, "at-need" annuities were brought to market to mesh with the cost of long-term chronic care ("at-need" meaning when long-term care (LTC) cost needs have already commenced). Combined with the stored legacy value of home equity, these at-need annuities can be especially helpful in dealing with this other scourge—the potentially financially devastating, and all-too-frequent uninsured, cost of LTC.

Besides actually using this option "at-need," the possibility of being able to opt for it "at-need" could change how people address the spectrum of choices for funding potential LTC costs.

This paper describes the LTC funding problem, including weaknesses of reverse mortgages and Medicaid in these respects, and how this combination of an at-need annuity/home equity combination can offer "late-in-the-game" additional insurance leverage.

An extensive anecdotal example is provided describing how this option can be effectively used to maximize care outcomes by building on other funding. Cash flow analyses of alternatives are discussed, as well as sensitivities involved and the need to focus on risk/reward choices.

The potential and broader implications for practical layered funding of LTC costs, which this possibility facilitates, are also discussed.

Abstract

An Overview of the U.S. Long-Term Care Insurance Market (Past and Present): The Economic Need for LTC Insurance, the History of LTC Regulation and Taxation, and the Development of LTC Product Design Features

Larry Rubin, FSA, CERA, MAAA: PricewaterhouseCoopers, Partner
Kevin Crowe, CPA: PricewaterhouseCoopers, Partner
Adam Fisher: PricewaterhouseCoopers
Omar Ghaznawi: PricewaterhouseCoopers
Richard McCoach: PricewaterhouseCoopers
Rachel Narva, ASA: PricewaterhouseCoopers
David Schaulewicz: PricewaterhouseCoopers
Tom Sullivan
Toby White, FSA, CFA, Ph.D.: Drake University, Associate Professor of Actuarial Science

We provide reasons for why U.S. individuals should save for and buy private long-term care (LTC) insurance in the context of demographic trends and increasing cost and coverage constraints on Medicare, Medicaid and the federal budget. Then, we review the history of national regulation (including the recently repealed CLASS Act), especially with respect to pricing and rate review processes. We also examine the U.S. tax code, as it has affected LTC insurance, with specific focus on distinguishing between qualified and non-qualified LTC policies and the lack of a cash surrender value, non-forfeiture clauses, and marketability due to long waiting periods. Next, we examine the LTC insurance market from the early years (1980s and 1990s) through today, with emphasis on the inadequacy of the level-premium structure, dissatisfaction with core LTC products from both consumers and insurance companies, and which carriers have either left the market or persisted into 2014. Finally, we contrast the primary features of LTC product design (so far) to what is needed to make LTC insurance viable going forward, with specific discussion on benefit triggers, coverage portability, non-forfeiture provisions, initial price levels and contract language, all as they help better align the interests of policyholders, regulators and insurers.

Abstract

Can Long Term Care Protection in Other Developed Countries Provide Guidance for the United States? Germany as an Example

Prepared by
Doug Andrews, FCIA, FSA, FIA
University of Waterloo, Canada
dwa007@hotmail.com
August 29, 2014
In response to a Call for Papers by the Society of Actuaries

This paper presents comparative research with respect to a number of developed countries regarding the adequacy and sustainability of programs for care and support of the elderly of which long-term care (LTC) is one component. It may provide guidance to those in the United States by helping to place the adequacy and sustainability of their programs for care and support in an international context. It suggests that the approach to LTC used in Germany of mandated social insurance provided by private sector insurers would be worthy of consideration for implementation in the United States.

Abstract

Key Pieces of the Retirement Security Puzzle: Financing Future LTSS and Long Life through More Flexible 401(k)s and IRAs

Karl Polzer

This paper proposes and evaluates changing 401(k) and individual retirement account (IRA) rules to help address two major risks facing participants in defined-contribution (DC) retirement accounts: 1) the risk of outliving one's savings; and 2) the risk of having to pay substantial amounts for long-term services and supports (LTSS). The proposal would allow retirees to invest a portion of their DC retirement savings in a special retirement account for longer without penalty than under current tax rules and could provide additional tax incentives for money drawn from the accounts used to pay for LTSS or long-term care insurance (LTCI).

The administration recently took a significant step that could help DC account holders manage the risk of outliving their savings. On July 2, 2014, the Treasury Department and Internal Revenue Service (IRS) published a final rule allowing conversion of part of DC account balances into longevity annuities with guaranteed lifetime payments. The new rules allow DC account holders to use up to 25 percent of their account balance or $125,000 (whichever is less) to buy a longevity annuity without tax penalties that otherwise might result from noncompliance with existing minimum distribution rules.[i]

The policy change explored in this paper addresses issues facing policymakers in both the retirement and long-term care (LTC) financing arenas. Key findings and observations of the analysis are:

- DC plans increasingly are the predominant way that Americans save for retirement. Many, if not most, Americans participating in DC plans are at risk both of outliving their savings and of not having enough to cover future LTSS costs.
- Lack of awareness of these major financial risks, along with tax rules that incentivize withdrawal from DC accounts beginning just after age 70, make it more difficult for people to save and invest in order to prepare to meet these risks.
- In planning for retirement, people could benefit from education on how to balance the need for streams of income to cover everyday retirement living expenses with the risk of living a long time and future LTSS costs. Preparing for retirement needs and risks poses significant trade-offs.
    - Allowing DC account owners to keep a portion of their total balance invested without tax penalty could help them to increase their earnings through a longer investment time horizon. However, saving and investing to cover future risks in this way would mean that they could use less for living expenses early in retirement.

- Americans may be surprised by the modest levels of income that can be yielded from what may seem to be large amounts of DC savings.
    - For example, for each $100,000 in total IRA/401(k) balances, account owners now have to withdraw about $4,000 annually beginning at age 71 to avoid a stiff tax penalty. If funds in the accounts are earning an average of 2 percent annually after inflation, annual "minimum distributions" remain somewhat level, staying between $3,500 and $4,500 a year until age 96, but then decline below $3,000 at age 100.

- Based on available estimates of DC account balances, about 20 percent of families with the largest DC asset levels would have the ability to pre-finance all or a substantial amount of the cost of LTSS by putting 25 percent of their total DC retirement assets in a "LTSS/longevity" account. Money in the accounts could be used to pay LTCI premiums or to pay directly for LTSS. If families started early enough, it is possible that such accounts could help more people cover a substantial portion or all such costs. Even those with very low DC retirement asset levels might benefit from being able to set aside some funds for longer to better sustain quality of life if they happen to live a long time.
- Currently only about 10 percent of seniors have LTCI. Though still an important financing option, the LTCI market has experienced major problems over the past several years. Most policies do not cover catastrophic costs over a specified upper limit, and a large percentage of older people do not qualify to buy LTCI because they have pre-existing medical conditions.
- Creating LTSS/longevity accounts could play an important role as policymakers explore packages of reforms that attempt to help people who are financially able to take personal responsibility for financing LTSS while expanding social insurance to help those lacking the financial means to do so.
- Establishing federal catastrophic LTSS coverage, which is one option under discussion, could dovetail well with LTSS/longevity accounts by limiting individuals' financial risk. If people knew they only had to cover three years of major LTSS costs, for example, it would be easier for those with moderate incomes to finance all or a major portion of these risks, especially if they started saving and investing early.
- Encouraging private savings for LTSS through tax incentives would increase federal costs but could also reduce Medicaid costs. Federal government costs could be mitigated by tilting tax advantages toward middle- and lower-income people and away from those with higher income.
- While using money in the DC retirement system to finance LTSS would be most advantageous to people with higher incomes and retirement savings levels, such a policy change could be part of a reform package improving retirement security and reducing risk for people across the economic spectrum.

- For example, such a package also could include: providing federal catastrophic coverage for LTSS costs; having the federal government guarantee interest rates for retirement annuities for people of modest means; and raising Supplemental Security Income (SSI) levels. SSI provides funds for room, board and living expenses for the lowest-income aged, blind and disabled people receiving LTSS under Medicaid. SSI levels are currently far below the federal poverty level.

---

[i] Federal Register, Vol. 79, No. 127, July 2, 2014, p. 37633. Also, see: "Treasury Green Lights Longevity Annuities in 401(k)s and IRAs," *Forbes*, July 1, 2014, downloaded from Web July 25, 2014 at: http://www.forbes.com/sites/ashleaebeling/2014/07/01/treasury-green-lights-longevity-annuities-in-401ks-and-iras/.

Abstract

The American Long Term Care Insurance Program (ALTCIP)

By Paul E. Forte

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 10 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 on Long-Term Care in 2013. An abbreviated version was published in *Contingencies* (January 2014) under the title "Fresh Thinking on Long Term Care."

Abstract

Home Equity: A Strategic Resource for Long-Term Services and Supports

Barbara R. Stucki, Ph.D.

In the wake of the Great Recession, the financial decisions older Americans make will affect their ability to continue to live independently. This is especially true for housing wealth. Will homeowners use this asset to help them pay for assistance as they grow older? Or will they quickly exhaust this resource paying for everyday expenses or leisure activities? With Medicaid as the only safety net for people with disabilities and chronic conditions, there is a lot at stake in this evolving economic behavior.
The house is a unique and complex asset that serves as both a place to live and as a store of wealth. It is also becoming the primary setting for the delivery of health care and long-term services and supports (LTSS) in later life. Until recently, however, there has been little discussion about using home equity to pay for LTSS beyond reverse mortgages. This paper examines the diverse body of economic and social research on the magnitude, timing, and motivations for decumulating housing wealth in retirement to pay for LTSS. The aim is to provide a more nuanced framework for incorporating housing wealth in efforts to support older people and family caregivers. The study also reviews new data that show how the use of home equity could change in response to the economic and social pressures of our aging society.

Results of this analysis suggest that home equity is already an important part of the LTSS financing mix. Many older homeowners today save this asset until late in life, to self-insure against the high cost of nursing home care. Looking ahead, increasing economic insecurity and the aging of the boomer generation could cause rapid shifts in the use of housing wealth that could reduce the availability of this asset for LTSS. There is also evidence that boomers are receptive to the idea of using home equity sooner to pay for everyday expenses and health-related costs in retirement. Encouraging such timely use of housing wealth for shorter-term LTSS planning could support aging in community and supplement insurance-based mechanisms that primarily provide protection against catastrophic expenses.

It is becoming increasingly important to consider LTSS financing from the standpoint of private resources as well as government programs. This study will help to fill the gaps by examining a wide array of evidence on the liquidation of home equity for LTSS. The analysis starts by examining national expenditures for LTSS.

Abstract

An Affordable Long-Term Care Solution through Risk Sharing

By Kailan Shang[i], Hua Su[i], and Yu Lin[i]

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.