Statement
of the
American Council of Life Insurers

On

"Long-Term Care Insurance: Helping Americans Achieve Retirement Security"

Before the

Senate Special Committee on Aging
of the
United States Congress

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My name is Malcolm Cheung and I am Vice President and Actuary for Long-Term Care at Prudential. Today I am representing the American Council of Life Insurers (ACLI), a Washington D. C.-based national trade association representing more than 350 member companies that offer life insurance, annuities, pensions, long-term care insurance, disability income insurance and other retirement and financial protection products.

By way of background, I joined Prudential's Long-Term Care Division in June of 1999. My current responsibilities for Prudential include pricing, product development, contracts, compliance, financial reporting, and risk management (underwriting and claims) for Prudential's group and individual long term care insurance products. I am also a Fellow of the Society of Actuaries, where I serve as the Secretary of the Long-Term Care Insurance Section Council; a member of the American Academy of Actuaries, where I serve on the Federal Long-Term Care Task Force; and am the current chairman of the American Council of Life Insurers' Long-Term Care Policy Committee.

Prudential Financial has been in the long-term care insurance business since 1986 when it issued its first group long-term care insurance contract. Prudential entered the individual long-term care insurance market in 1999 offering one of the first comprehensive products with a cash payment option. Today, Prudential is one of the fastest growing long-term care insurance carriers and is firmly committed to helping Americans achieve and maintain financial security in retirement.

We are delighted that this Committee is addressing an important issue facing this nation – long-term care – through the hearing process. We applaud Chairman Smith (R-Oregon) and Ranking Member Kohl (D-Wisconsin) for drawing attention to this matter, and we are pleased to discuss with the Committee the role that private long-term care insurance plays in helping to provide the retirement security of millions of middle-income families.

ACLI recently released a comprehensive update on its landmark study titled "Long-Term Care Insurance or Medicaid: Who Will Pay for Baby Boomers' Long-Term Care?". Many of the statistics I will share with you today come from this important research, which can be found at www.acli.com.

Currently, about 55 percent of those 85 and older require some form of long-term care and about 19 percent of all seniors suffer from some degree of chronic impairment. By 2050, it is estimated that up to 5.4 million seniors will need the services of a nursing home – the most costly form of long-term care – and another 2.4 million will require home health care.

The cost of long-term care is high and increasing, averaging $69,422 annually for a private room or $61,116 annually for a semi-private room in a nursing home, $18.58 per hour for a visit by a home health aide, and an average annual *base* rate of $30,265 for the services of an assisted living facility. Since 1990, the price of nursing home care has increased at an average annual rate of 5.8 percent – almost double the overall inflation rate.

Current Financing for Long-Term Care Services

Total annual expenditure on long-term care for the elderly is estimated to be $135 billion, which accounts for over 9.7 percent of total spending on health care for persons of *all* ages. This is roughly 1.2 percent of the U.S. GDP. Because baby boomers are aging and the cost of care is increasing, total spending on nursing home care is expected to more than triple over the next 25 years and to increase more than five-fold in the next 45 years. These increases will place a heavy burden on Medicaid and ultimately on taxpayers, most of whom are working-age adults. Currently, there are about 5 working-age adults per senior, but by 2030, there will only be 2.9 – a 40 percent decline. This decline will occur while both the need for and cost of long-term care increase.

Given the strong possibility that the typical senior will require long-term care, and given the escalating costs of that care, whether elderly boomers enjoy a comfortable retirement or suffer economic hardship may depend largely on their ability to afford long-term care. Most boomers have not planned for this reality and face the prospect of paying large sums out-of-pocket or relying on Medicaid. (In its current form, Medicaid only covers the cost of long-term care after a senior has spent down virtually all assets and retirement income.) Neither option is very appealing and may leave seniors and their spouses impoverished, with few long-term care choices.

- **Long-Term Care Insurance**

Private insurance currently pays for 8 percent of total nursing home expenditures but 36 percent of overall health expenditures. There is clearly a large gap in the financing of long-term care services that private insurance can fill.

If three-quarters of individuals between the ages of 40 and 65 who can afford long-term care insurance were to purchase and maintain a policy throughout their senior years, then by 2030, annual savings in Medicaid nursing home expenses would total $19 billion, and annual savings in out-of-pocket expenses would total $41 billion.

Both the individual and group (employer-sponsored) segments of the long-term care insurance market are evolving and growing. The American Council of Life Insurers, with the assistance of America's Health Insurance Plans, recently surveyed long-term care insurance providers and found:

- The market has grown to nearly $7 billion in premiums, and now covers over 5 million people.

- Between 2003 and 2004, the individual long-term care insurance market grew 7.5 percent and the group market grew 25 percent.
- The amount paid out in claims has also increased with carriers paying $2.1 billion in benefits in 2004, about 20 percent more than in the previous year.

Because private long-term care insurance is priced on the assumption that an individual will hold the same policy and pay the same premium until they need long-term care, premium rates vary depending on the age of the policyholder at policy issue and the specific benefits and coverage chosen. Additionally, younger candidates for policies are much more likely to pass underwriting screens than are older candidates. For these reasons, consumers are encouraged to purchase insurance while they are in their 40s and 50s, when premiums are lower and more affordable.

The typical buyer of long-term care insurance is aged 55-60 (although the average age of those who enroll in group plans is in the forties), married, college educated, with an annual income in excess of $50,000. Women are more likely to buy coverage than men. Although the market for long-term care insurance is growing, most Americans have not yet purchased this insurance protection. Impediments to even greater market growth include competing demands for discretionary income, limited tax incentives to purchase long-term care insurance, and the lack of awareness of the need to plan for potential long-term care expenses.

Long-term care insurance products continue to evolve to give policyholders more choices and flexibility at the time of claim. When long-term care insurance was first offered, most plans were nursing home-only. Recently, more flexible care options and consumer protections have become available. Today, most policies provide coverage for care received at home, in an adult day care facility, in an assisted living facility, or in a nursing home. Additionally, plans are now guaranteed to be renewable, have a 30- day “free look” period, offer inflation protection, cover Alzheimer’s disease, have a waiver of premium provision, and offer unlimited benefit periods. Benefits are paid when a person needs help with two or more activities of daily living (such as eating, dressing, or bathing) or is cognitively impaired.

- **Long-Term Care Partnerships**

One way to ease budget burdens for the government and individuals is through the Partnerships for Long-Term Care program. The United States Congress passed important provisions to allow for the expansion of long-term care partnerships in the recent Deficit Reduction Act, which was signed by President Bush on February 8.

The Partnerships allow consumers to purchase a long-term care policy whose benefits must be fully utilized prior to qualifying for Medicaid. Because consumers utilized their insurance coverage under the Partnership, they can protect assets equal to the amount of Partnership plan benefits received. The Partnership concept is currently operational in four states: California, Connecticut, Indiana, and New York.

Many states are now vigorously working to seize this new public policy opportunity by passing state plan amendments to their Medicaid programs and creating implementation frameworks. Insurers anticipate that the Partnership, in addition to the changes to Medicaid eligibility standards that were also a part of the Deficit Reduction Act, will provide greater incentive to purchase long-term care insurance in new states that choose to participate, as it has in the four current states.

- **Flexible Retirement Security Proposal**

Many Americans preparing for their future recognize retirement security has multiple components—there is a need to accumulate assets while working, manage those assets in retirement, prepare for premature death, and be financially prepared in the event that long-term care is needed. Currently, there are a limited number of products available to accomplish all of these different goals. In fact, the tax code limits the ability to combine different products.

H.R. 3912, The Flexible Retirement Security for Life Act of 2005, introduced by Reps. Nancy Johnson (R-Conn.), Phil English (R-Pa.), and Stephanie Tubbs Jones (D-Ohio), would make product combinations possible—satisfying the evolving needs for some individuals by facilitating the addition of a long-term care rider to either an annuity or a life insurance contract. It would also update the tax code to include long-term care insurance contracts and riders among the insurance products that can be exchanged on a tax-deferred basis. Under the leadership of House Ways and Means Chairman Thomas (R-Calif.), this bill was incorporated into the House's pension reform bill and ACLI strongly urges Members of this Committee to support it as the House and Senate meet in conference.

This proposal would create more flexibility and choice for American consumers. During working years, individuals could accumulate assets in an annuity; at retirement, depending on the needs of the individual, that annuity could be used to provide lifetime income. Throughout, a long-term care insurance rider to the annuity would pay long-term care benefits. For the long-term care/life insurance combination, the life insurance would serve its critical function of death protection, while also being available to provide funds for payment of long-term care costs.

While stand-alone long-term care insurance is key for many individuals, others may be deterred due to the absence of a savings accumulation feature within the product. Permitting long-term care coverage to be combined with the savings and asset management available in an annuity, as well as the death protection in a life insurance policy, enhances the ability of Americans to structure their long-term care planning to suit their retirement planning and estate planning needs.

- **Tax Incentives**

Although product combinations may prove to be an attractive alternative to standalone long-term care insurance for some individuals, an even more broadly appealing and effective solution to the financing of long-term care would be the passage of S. 1244, the “Long-Term Care and Retirement Security Act of 2005." Cost is a major reason why more Americans have not yet purchased long-term care insurance. This measure provides individuals with a phased-in above-the-line federal income tax deduction for the eligible portion of the premiums they pay to purchase long-term care insurance. In addition, the measure would permit long-term care insurance policies to be offered under employer-sponsored cafeteria plans and flexible spending accounts; and would clarify that a qualified long-term care policy could be exchanged tax-free for another qualified long-term care policy better suited to the insured’s needs. Finally the bill includes a phased-in tax credit to individuals with long-term care needs or their caregivers of up to $3,000.

Long-term care insurers are also closely evaluating other recent legislation that recognizes the importance of the tax incentive component to encourage the purchase of long-term care insurance, such as Chairman Smith’s Long-Term Care Trust Accounts proposal. We applaud Chairman Smith and his staff for their leadership on long-term care issues and look forward to a continued strong working relationship.

Congress should not pass on this historic opportunity to definitively help Americans plan for their long-term care costs by allowing individuals to pay for their long-term care insurance premiums through cafeteria plans and flexible spending accounts, as well as through flexible retirement security combination products for those paying for long-term care insurance outside of employer-sponsored plans. This could have a significant impact on the public policy challenges related to the combination of rising long-term care costs, rising long-term care needs, and rising strains on the Medicaid budget. Individuals will have the ability to pay privately and have the choice of a variety of services and care settings. Such provisions are also found in Senator Santorum's (R-Penn.) Aging with Respect and Dignity Act (S.2281) and we commend him for it.

Future Financing for Long-Term Care

Insurers continue to educate Americans that a financially secure retirement includes a plan to cover future long-term care expenses. To help educate consumers on how to select and purchase a long-term care insurance policy, ACLI maintains educational brochures and information on its website that encourage consumers to do their homework when considering the purchase of long-term care insurance. For example:

1. Look for insurance companies that are reputable, consumer oriented, financially sound and licensed in their particular state;
2. Take time when making a purchase, ask for and read the outline of coverage of several policies;
3. Understand what the policy covers and ask questions to be clear about what the policy is not intended to cover; and
4. Understand when the policy becomes effective, what triggers benefits and if it is tax deductible at the state and/or federal level.

The federal government and the states have also recognized the need to educate individuals in the workplace to plan to cover their future long-term care needs. The federal government, by Act of Congress, has taken the lead and set the example for other employers by offering federal employees and their families the protection of long-term care insurance. Through this program, federal employees are able to help protect their retirement savings from a long-term care event and will have the choice of providing care for themselves or a family member in the home, through assisted living or in a nursing home.

States Promoting the Purchase of Long-Term Care Insurance

Last year, the Department of Health and Human Services began a federal project to increase awareness among retirees and near-retirees about the need to plan ahead for potential long-term care needs. Governors of five pilot states conducted long-term care awareness campaigns over a three-month period, starting in January 2005. The campaign included press conferences, mailings to 50- to 70 year-olds in each state, advertising and follow-up mailings. The five states include Arkansas, Idaho, Nevada, New Jersey, and Virginia. Phase 2 of this “Own Your Future” Campaign, which began this January, includes Kansas, Maryland, and Rhode Island – and is designed to reach 5 million households in the target market.

States are supporting the purchase of long-term care insurance in a number of ways. About half the states have implemented long-term care insurance programs that offer state employees/retirees the opportunity to purchase long-term care insurance coverage. Twenty-four states provide tax incentives for purchasing long-term care insurance. Most state tax deductions share some features with federal rules – allowing all or part of premiums and expenditures to be deducted. Three states provide a tax deduction or credit for employers offering group long-term care insurance policies. As more than 77 million baby boomers approach retirement, the rapidly aging workforce, together with more employees caring for elderly parents, heighten the importance of long-term care planning as a workplace issue.

Private Long-Term Care Insurance: An Important Part of the Answer

In conclusion, we believe that protection and coverage for long-term care is critical to the economic security and peace of mind of all American families. Private long-term care insurance is an important part of the solution for tomorrow's uncertain future. As Americans enter the 21st century, living longer than ever before, their lives can be made more secure knowing that long-term care insurance can provide choices, help assure quality care, and protect their hard-earned savings when they need assistance in the future. We also believe that the costs to Medicaid – and therefore to tomorrow's taxpayers – will be extraordinary as the baby boom generation moves into retirement, unless middle-income workers are encouraged to purchase private insurance now to provide for their own eventual long-term care needs. Education, options, incentives and the efficient use of both public and private resources are critical to our nation's ability to finance long-term care in the decades ahead.

Again, ACLI looks forward to working with this Committee to help Americans protect themselves against the risk and high cost of long-term care.