

# Benevolence Assistance Liabilities: A Hidden Risk for CCRC Operators



Session 46-F

Tuesday, 430P to 540P

October 28, 2003

- ◆ Theory
- ◆ AV Powell  
Consulting Actuary
- ◆ AV Powell & Associates
- ◆ Case Example
- ◆ Henrietta Bertelsman  
CFO
- ◆ United Church  
Retirement Communities

# OVERVIEW

- ◆ Identifying the benevolence risk
- ◆ Screening prospective residents
- ◆ Estimating current resident obligations
- ◆ Meshing fund-raising with liabilities

# Identifying the Benevolence Risk

## ◆ Is concern about risk valid?

- Increasing longevity
- Commitment to care for resident for life
- Volatility in investment market
- Pressure from heirs to divest of assets

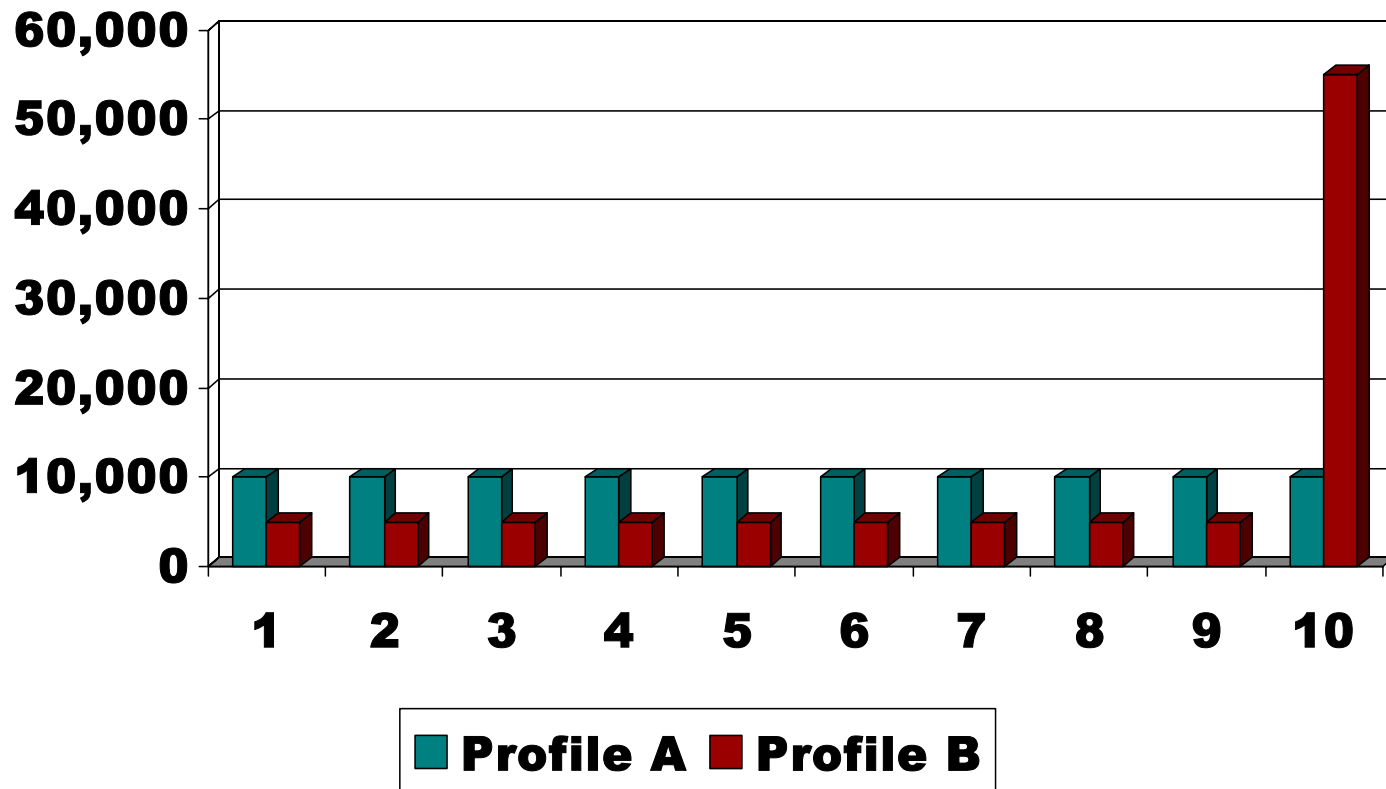
# How Do/Should You Manage Benevolence Liabilities?

- ◆ How much benevolence can you afford?
  - Current size of restricted funds
  - Annual contributions
- ◆ It's not managing cash flows,  
it's managing liabilities

# Making Decisions Based on Cash Flows: Illustration of Pitfalls

- ◆ Projected benevolence needs for illustration
  - Resident A requires \$10,000 for 10 years
  - Resident B requires \$5,000 for 9 years, \$55,000 in year 10
  - Both represent a \$100,000 liability
- ◆ Board authorizes \$10,000 in annual aid

# Subsidy Profiles for 2 Case Examples



# Making Decisions Based on Cash Flows: Consequences of Decisions

- ◆ Annual subsidy capacity appears to be:
  - One (1) profile A resident
  - Two (2) profile B residents; generates unexpected \$100,000 need in year 10
  
- ◆ If made decision based on future liabilities, would have accepted one profile B resident

# Methods for Determining Need for Aid

## ◆ Current residents

- Rules-of-thumb
- Trending current needs; ignores liabilities
- Spreadsheet or software tools
- **Actuarial projection of future liabilities**

# Rules-of-thumb

- ◆ Income equals 2x monthly fee
  - Simple to apply
  - Works with Type A contracts, not with B and C
  - Inadequate for younger ages and couples
- ◆ Life expectancy projections
  - 50% of your population will live longer
  - Difficult to distinguish by level of care

# The Actuarial Process for Estimating Benevolence Liabilities

- ◆ Determine liabilities for current residents
- ◆ Compare liabilities with benevolence assets
- ◆ Calculate new benevolence capacity
- ◆ Apply screening criteria to accept new entrants up to new benevolence capacity

# Actuarial Liability Estimation for Current Residents

- ◆ Collect and verify data
  - Resident demographics
  - Resident movements
  - Resident financial resources
- ◆ Experience study to develop actuarial decrement assumptions that generate life expectancies
- ◆ Project future population flows

# Actuarial Liability Estimation for Current Residents (continued)

- ◆ Generate financial aid liability projections
  - Population flows  $\leftrightarrow$  Resident financial resources
- ◆ Evaluate liability projections
- ◆ Test sensitivity to alternative assumptions
  - Medicaid reimbursements
  - Personal spending money if receiving aid
- ◆ Present results and recommendations

# Caveats

- ◆ Explain to prospects and residents why and how data will be used
  - Unwillingness to provide
  - Fear that fees may be increased
  - Sufficient assets



# Limitations

- ◆ The model is accurate, but limited to input assumptions about several factors:
  - Translation of resident financial data to our format
  - Credibility and validity of resident data
  - Estimating disposable income usage
  - Implementing qualification criteria
  - No test to confirm sufficient resources

# Data Requirements and Format

**Financial Data**

Edit Help

General Information		Record Information	
Information Date	10/27/2002	Person 1	Person 2
Sufficient Resources	<input type="checkbox"/>	ID	3 18
Apply LTC Insurance	<input checked="" type="checkbox"/>	Last Name	CALLAHAN CALLAHAN
Apply Entry Fee Refund	<input type="checkbox"/>	First Name	ADRIANA CLINTON

Monthly Expenses (Excluding Monthly Fees)							Long Term Care Insurance		
Description	ILU Single	ILU Add'l Per	ALU Single	ALU Add'l Per	NCU Single	NCU Add'l Per		Person 1	Person 2
Personal expenses	400	300	100	50	100	50	Benefit Period (Years)	2	2
							Elimination Period (Days)	120	120
							ALU Daily Benefit	30.00	30.00
							NCU Daily Benefit	60.00	60.00
							Inflation Adjusted	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
							Annual Premium	1,000	1,000
							Premium Inflation (%)	2.0	2.0

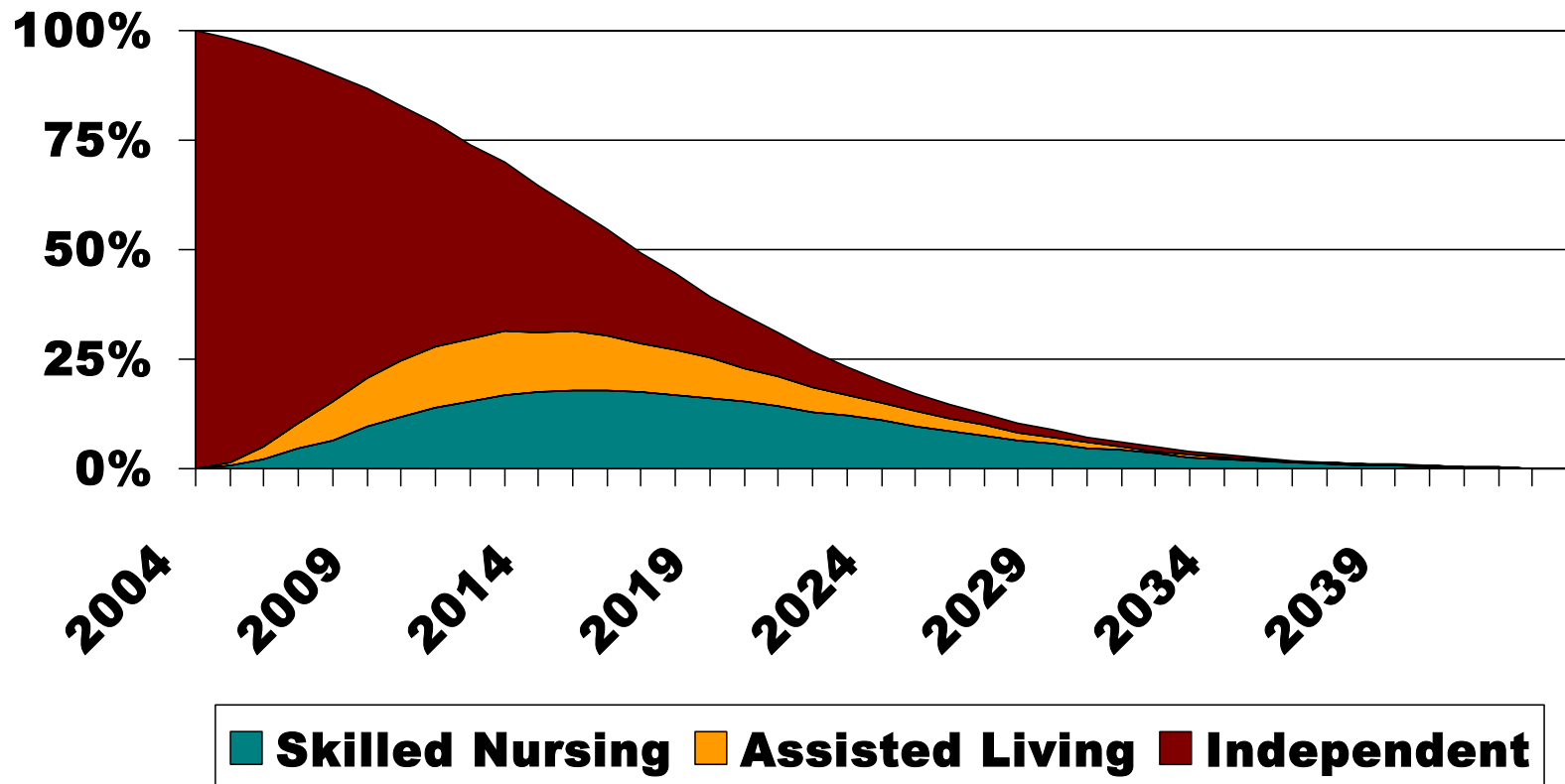
Assets and Income											
Type	Description	Own	Balance	APR %	Freq	Income	Begin	Dur	Inf Adj	Tax	Surv %
Stocks/Equity Func		Joint	20,000	3.0	M	50	NA	NA	<input checked="" type="checkbox"/>	Y	100
Social Security	Adriana	1	NA	NA	M	450	1	L	<input checked="" type="checkbox"/>	SS	SS
Social Security	Clinton	2	NA	NA	M	750	1	L	<input checked="" type="checkbox"/>	SS	SS
Pension	Adriana	1	NA	NA	M	300	1	L	<input type="checkbox"/>	Y	0
Pension	Clinton	2	NA	NA	M	1,000	1	L	<input type="checkbox"/>	Y	60
Real Estate		1	50,000	NA	NA	NA	NA	NA	<input type="checkbox"/>	N	100

OK Cancel

# Actuarial Projection of Survivors

- ◆ Identify current census
  - 111 residents/78 contracts
  - Average age: 80.3 years
  - Average years in community: 0
  - Percentage female: 69.4%
- ◆ Apply actuarial decrements to project:
  - Deaths, move-outs, and transfers
  - Couple density, average health care usage by level
- ◆ Generate sensitivity projections

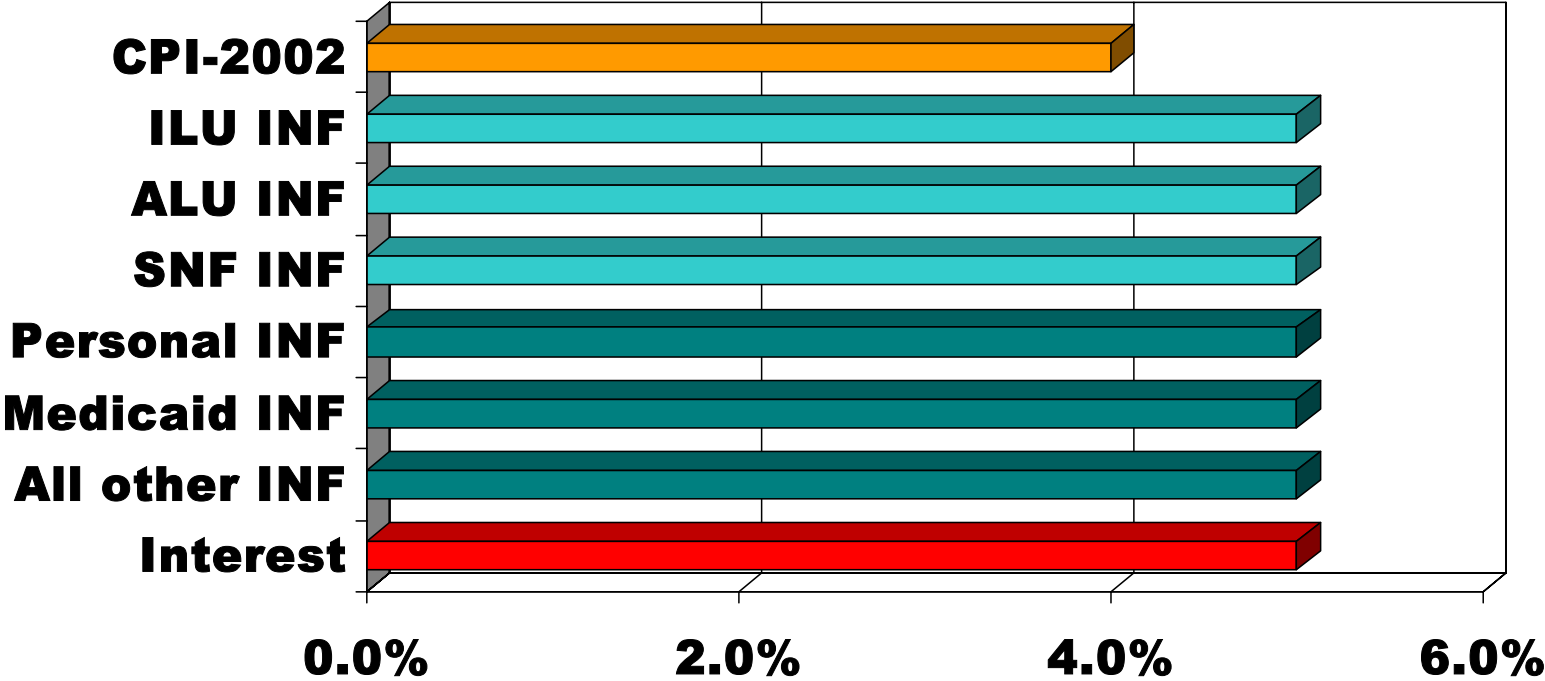
# Survivorship Projection



# Key Assumptions

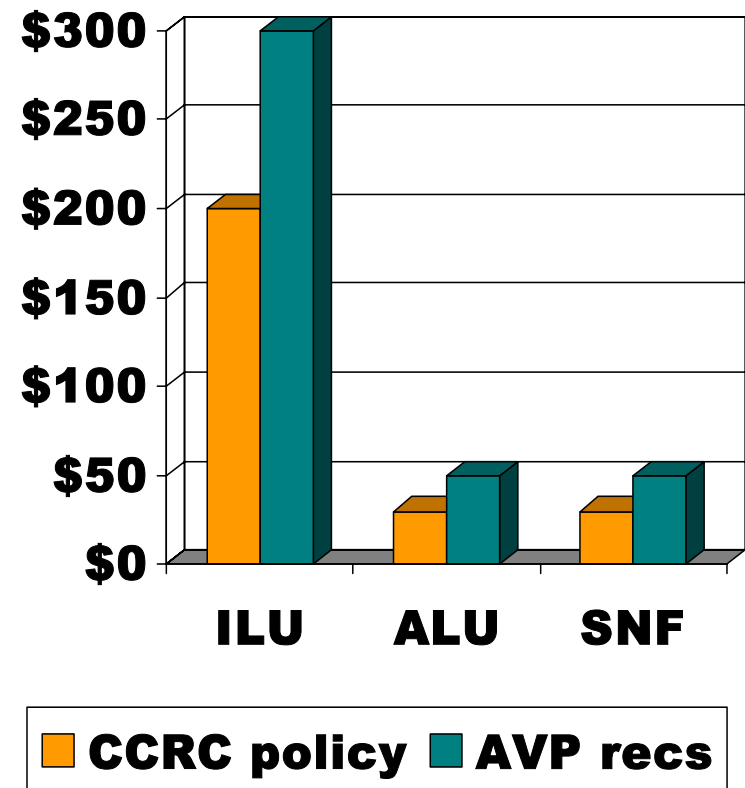
- ◆ Economic assumptions
- ◆ Actuarial assumptions (life expectancies)
- ◆ Personal income exemption
- ◆ Use of disposable income
- ◆ Medicaid and community spend-down policies
- ◆ Federal and state tax rates

# Economic Assumptions



# Personal Income Exemptions

- ◆ Includes prescriptions, travel, clothes, gifts, pocket money
- ◆ Some residents receiving subsidy claim they have expenses that exceed \$1,000 per month



# Use of Disposable Income

- ◆ What does resident do with income in excess of monthly fees plus allowance?
  - Spend all
  - Invest in savings
  - Invest in equities
  - Invest in taxable bonds
  - Invest in tax-exempt bonds
- ◆ Baseline assumption: residents spend all

# Medicaid Reimbursement and Aid Qualification Criteria

- ◆ Medicaid reimbursement rate and per diem  
((\$120 reimbursement/\$150 per diem))
- ◆ Medicaid minimum asset spend-down (\$2,500)
- ◆ Community minimum asset threshold  
(use Medicaid)

# Federal and State Income Taxes

Income	Constant	Percent
\$ 0	\$ 0	10.0%
6,000	600	15.0%
27,930	3,893	27.0%
67,770	14,625	30.0%
141,250	36,690	35.0%
307,050	94,720	38.6%

Income	Constant	Percent
\$ 0	\$ 0	2.0%
12,750	255	4.0%
60,000	2,145	6.75%
120,000	6,195	8.25%

# Description of Financial Subsidy Projection Scenarios

- ◆ Developed four sets of projections
  1. Type B; resident's personal expenses; no Medicaid
  2. Type B; resident's personal expenses; Medicaid
  3. Type B; corporate personal expenses; no Medicaid
  4. Type A; corporate personal expenses; no Medicaid  
(monthly fees for Type A are actuarially = Type B)

# Benevolence Projection Statistics

- ◆ Expected present value for financial subsidy liability for current residents
- ◆ Buffer factor based on ruin probability of 5% (or 25%) depleting benevolence funds
- ◆ Cash outflow projection for current residents only
- ◆ Expected Medicaid participation, if applicable

# Projected Number of Residents that will Require Assistance

	Residents	Contracts	Percentage (contracts)
Scenario 1;Type B	60	44	54%/56%
Scenario 2;Type B	60	44	54%/56%
Scenario 3;Type B	54	40	49%/51%
Scenario 4;Type A	29	23	26%/30%

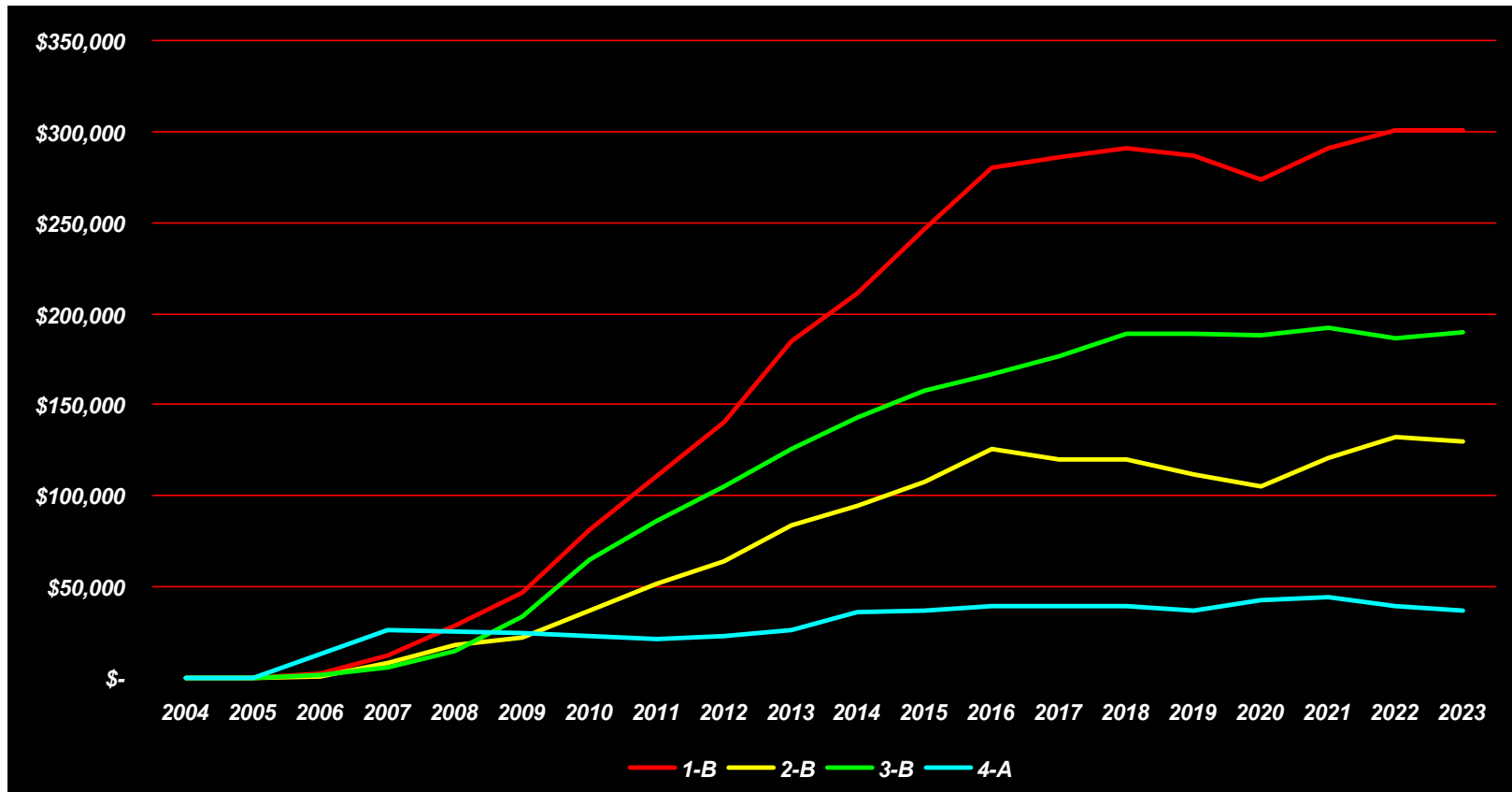
# Present Value of Subsidy for Current Residents

	Present Value	Buffer Factor
Scenario 1;Type B	\$ 2,784,295	1.18 to 1.50
Scenario 2;Type B	\$ 1,125,678	1.22 to 1.46
Scenario 3;Type B	\$ 1,953,139	1.23 to 1.62
Scenario 4;Type A	\$ 541,408	1.18 to 1.60

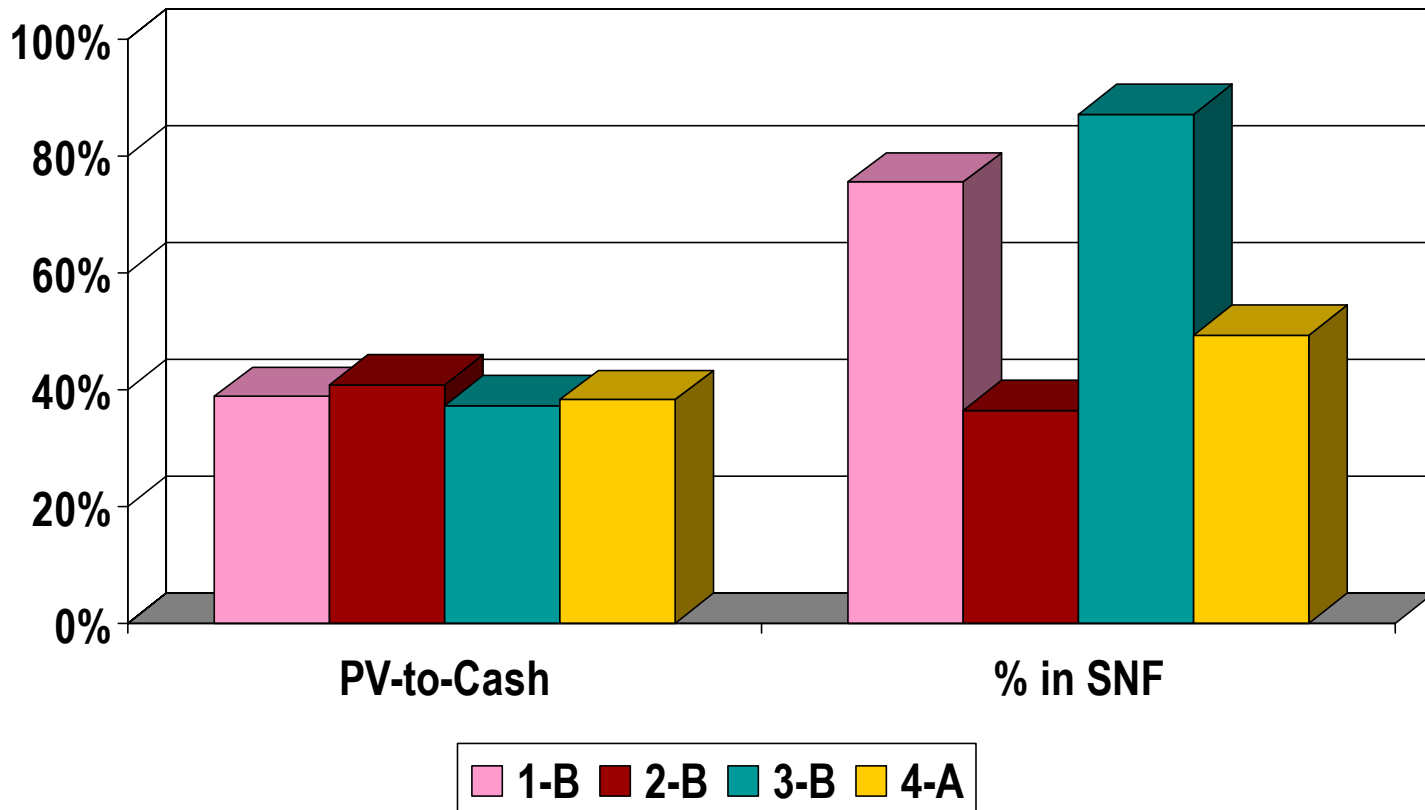
# Cash Outflow of Subsidy for Current Residents

	Expected	Likely Maximum
Scenario 1;Type B	\$ 7,185,644	\$ 15,793,593
Scenario 2;Type B	\$ 2,761,411	\$ 6,367,864
Scenario 3;Type B	\$ 5,232,048	\$ 13,593,135
Scenario 4;Type A	\$ 1,415,740	\$ 3,669,402

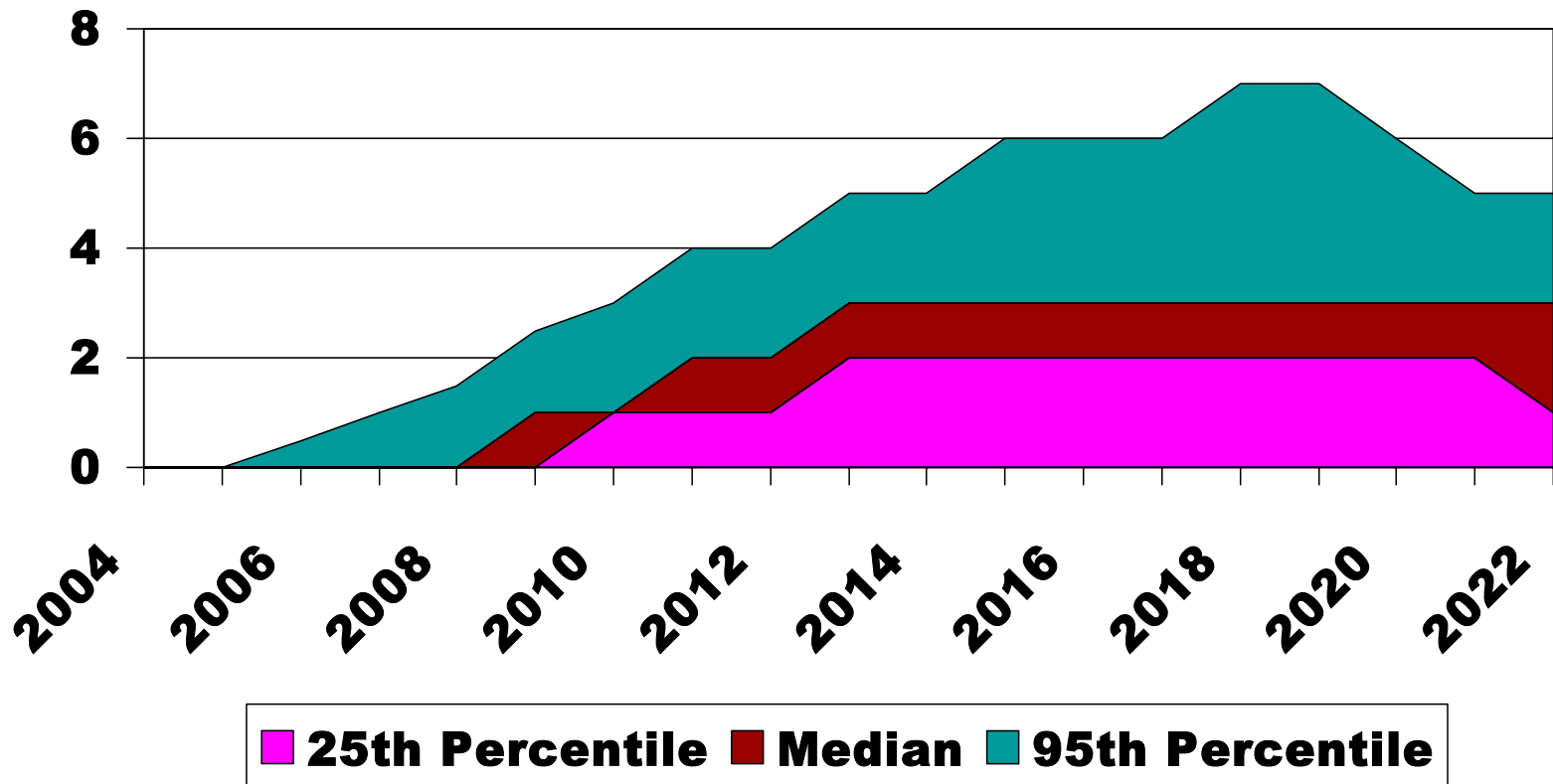
# 30-year Subsidy Cash Outflows



# Actuarial Ratios from Benevolence Subsidy Projection



# Projected Resident Medicaid Eligibility



# Matching Admission Criteria with Current Resident Needs

- ◆ Step 1: Determine if you have sufficient assets to cover current resident needs.
  - If no, implement policy that severely restricts to future fund-raising expectations or eliminates future aid
  - If yes, consider policy that allocates portion of surplus to cover future resident aid
- ◆ Step 2: Develop a policy or tool that consistently screens new entrants so that annual increase in aid liabilities does not exceed corporate capacity

# Application of Process to Scenario 1-Type B

- ◆ Assume that benevolence reserves equal \$3.0 million and Board can raise \$250,000 annually
- ◆ If decide to fund expected current resident liability of \$2.8 million, then can fund up to \$200,000 in prospective resident liabilities plus \$250,000 annually
- ◆ If decide to fund contingency to cover 5% (or 25%) ruin probability, then shouldn't accept prospective aid resident for several years

# Screening Prospective Residents

## Single Female Entrant

	70	80	90
Cash Outflow	\$ 86,469	\$ 29,092	\$ 10,223
Present Value	\$ 34,135	\$ 15,354	\$ 6,455
Exp{1 <sup>st</sup> year}	12	10	8
Exp Lifetime	12.1 yrs	7.9 yrs	5.2 yrs
Prob{Subsidy}	48.0%	39.0%	20.0%

# Policy Recommendations

- ◆ Know your benevolence capacity
- ◆ Define fund-raising goals and benevolence fund distribution policies
- ◆ Apply financial screening criteria that is consistent with goals and policies
- ◆ Quantify and provide annual Board reports on benevolence assistance

# Summary

- ◆ Keys for successful and useful data collection
  - Communications with residents
  - Attention to details
- ◆ Few organizations approach issue scientifically
- ◆ CCAC accreditation standard II-B
  - Describe and evaluate financial assistance policies and how you project and intend to fund this need

# CASE STUDY OVERVIEW

- ◆ The URCH Perspective
- ◆ Management Concerns
- ◆ Challenges
- ◆ Outcomes

# The UCRH Perspective

## 3 “Type C” CCRCs

	<u>Abernethy</u>	<u>Piedmont</u>	<u>Lake Prince</u>	<u>Opened</u>
HC	174	54	40	1971
AL	38	62	52	1986
IL	157	173	129	2002

Use both FORCAST and FINAID to estimate TOTAL potential commitment for Benevolent Care.

# Management Concerns

- ◆ While unbundled contracts have less health care risk, they present MORE financial aid risk
- ◆ It is essential to accurately estimate the timing and duration of stays at each level of care
- ◆ Use data in long-range strategic planning effort to estimate level of care resource strategies

# Challenges

- ◆ Management needs to agree on key assumptions to be utilized (e.g., personal income exemption).
- ◆ It is vital to have data “set up” correctly and consistently
- ◆ Obtaining resident financial information in a format consistent with software requirements
- ◆ Educating Board to understand funding strategy

# Outcomes

- ◆ Estimate of current resident benevolent obligations
- ◆ Estimate of risk associated with new admissions/prospects
- ◆ Coordinated fund-raising with future obligations
- ◆ Enhanced credibility with residents, Board and other constituents