Safeguarding Solvency:
The Role of the Actuarial Study

Presenters

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Learning Objectives

1. Explain how an actuarial study protects a life plan community against the financial uncertainty of residents' future life events.

2. Assess the financial solvency of a life plan community from multiple perspectives with a long-term financial view.

3. Utilize actuarial studies as a management tool to assess financial solvency and communicate that assessment with key stakeholders.

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Discussion Outline

1. Taking Solvency Seriously
2. What's in an actuarial study
3. Summary

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Liquidity versus Solvency

	Liquidity	Solvency
Time Frame	Covers immediate needs, within days or months	Covers long-term needs, over residents' potential lifetimes
Focus	Can we pay our bills, meet payroll?	Will the organization be able to cover its contractual obligations to residents?
Metrics	DCR, DCOH, minimum operating reserves	Net Assets/ASOP#3 Funded Status
What can happen?	Community could run out of ready cash, be forced to tap expensive short-term solutions	Bankruptcy, not being able to meet obligations to residents

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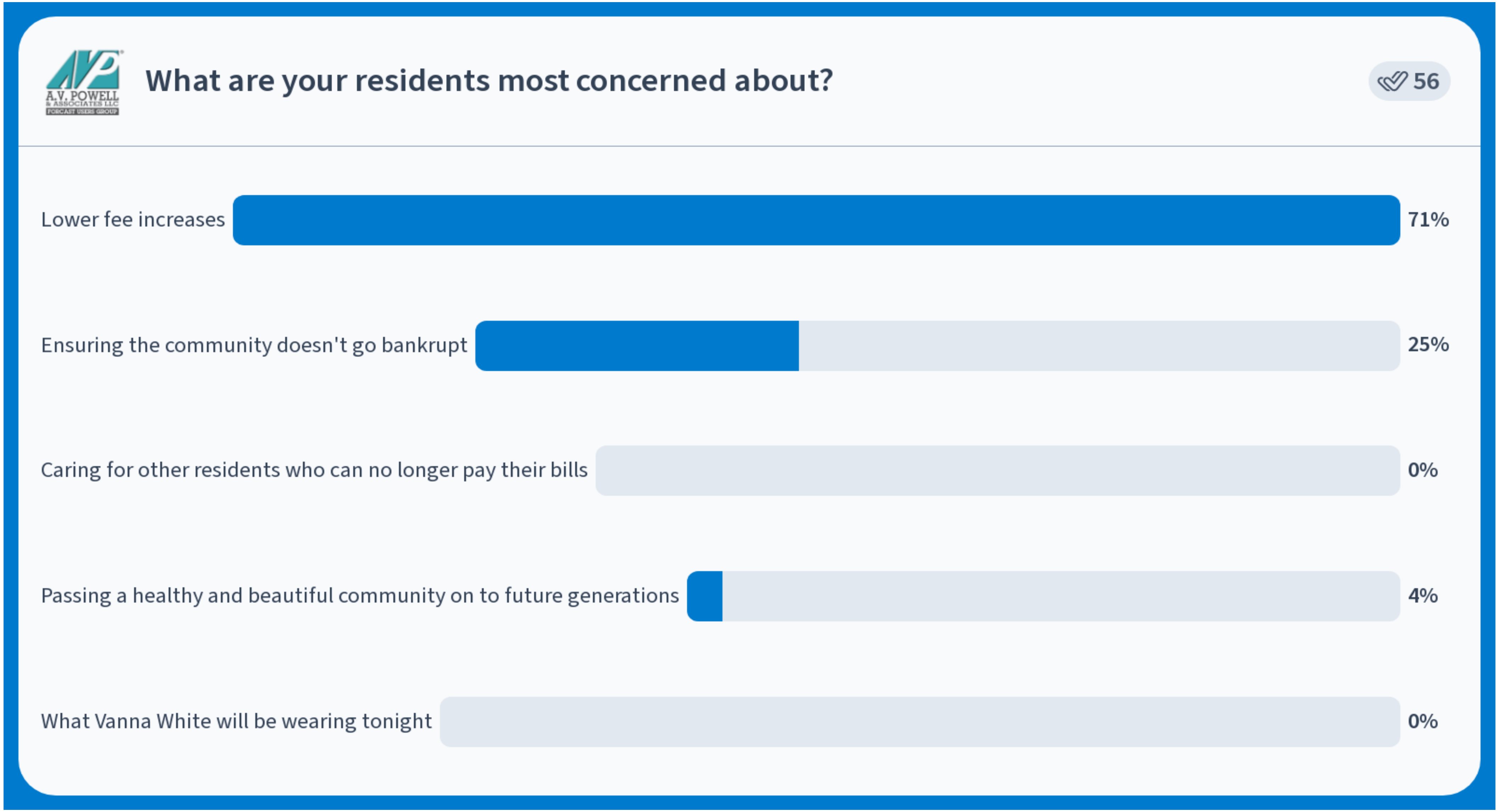
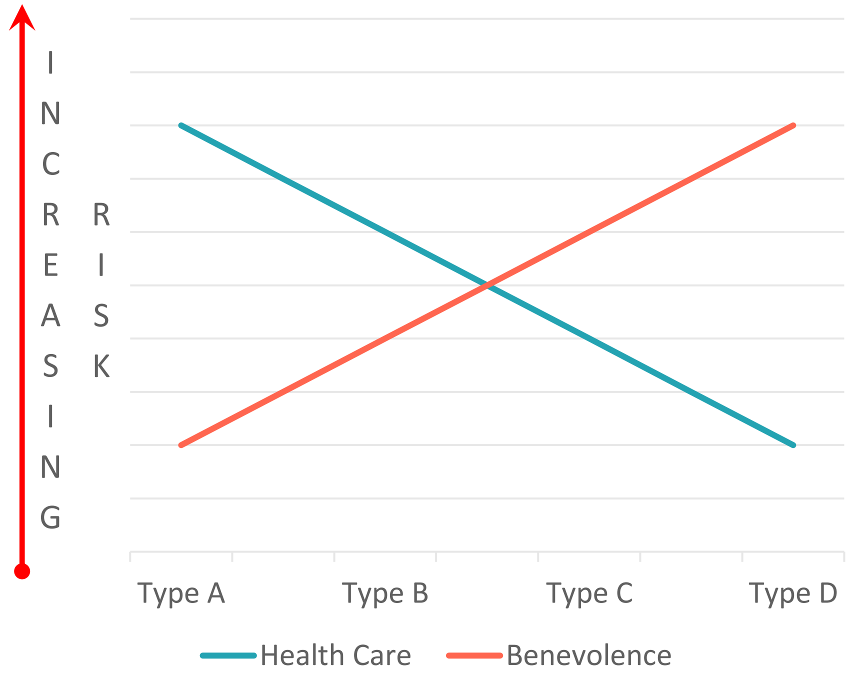

What are your residents most concerned about?
56
Lower fee increases
71%
Ensuring the community doesn't go bankrupt
25%
Caring for other residents who can no longer pay their bills
0%
Passing a healthy and beautiful community on to future generations
4%
What Vanna White will be wearing tonight
0%

How are LPC finances different than other businesses?

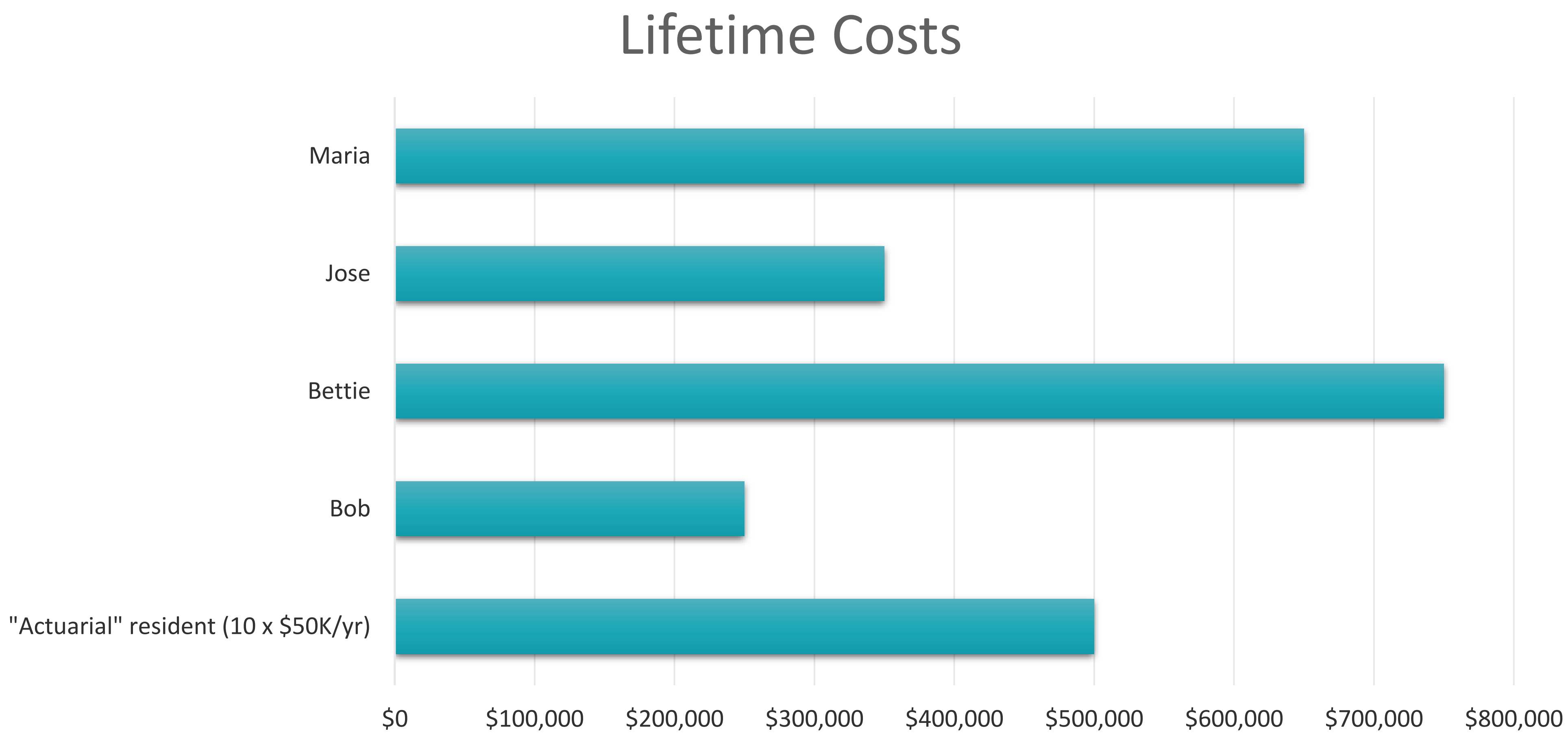
A Life Plan Community has long-term, insurance-like risks for which they must plan and save.

- Long-term care
- Charitable care
- Refunds
- Fairness Issues
- CCaH

All Contracts Have Risks!



LPC's Pool Risks



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Actuaries are trained to assess these risks

1. Managing a Life Plan community is complex
2. GAAP metrics are useful, but insufficient
3. An outside viewpoint is valuable
4. Actuaries have expertise
5. AVP has data
6. The best tool for determining solvency is an actuarial study.
   - ✓ This includes the AVP actuarial compilation report
   - ✓ An FSO report is not an actuarial study

Can an actuary quantify risks credibly and reliably?

1. Assumptions, Assumptions, Assumptions
2. Trends in ILU occupancy
3. Relationship between revenues, expenses, and earnings
4. Plans for capital renovations
5. Greenfield and rebuilding occupancy

Who wants to see an actual study?

Internal Stakeholders

- LPC management
- Residents and Resident Groups
- Boards

External Influencers

- Regulators
- Bondholders and Investment Bankers
- Rating Agencies
- Accreditation agencies
- AVP Seal

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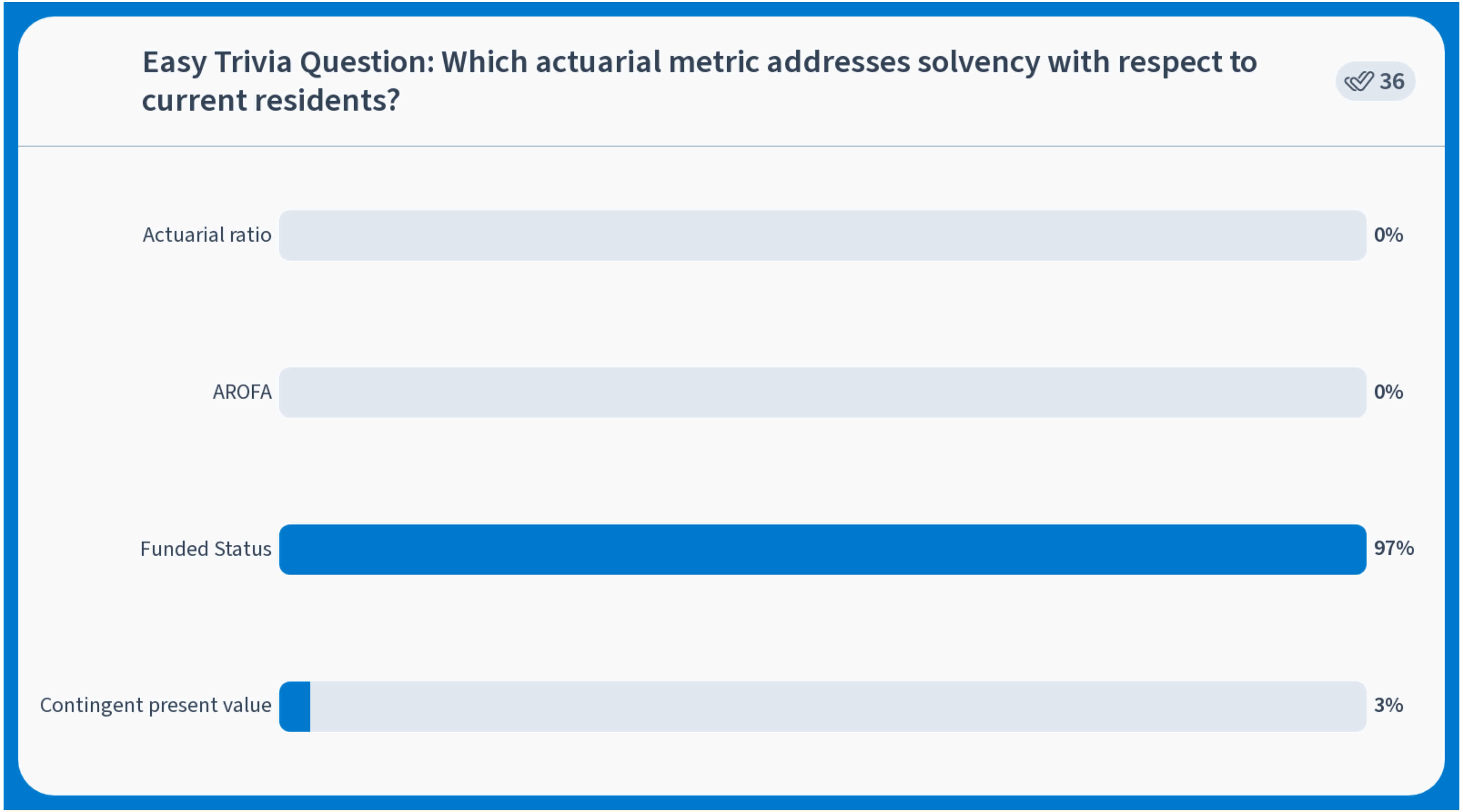
Easy Trivia Question: Which actuarial metric addresses solvency with respect to current residents?
36
Actuarial ratio
0%
AROFA
0%
Funded Status
97%
Contingent present value
3%

What's in an Actuarial Study?

Solvency Criteria – The Heart of an Actuarial Study

Criteria 1	Are reserves adequate to meet obligations to **current residents**?
Criteria 2	Are fees charged to **new entrants** adequate to cover their lifetime costs?
Criteria 3	Will projected **cash flows** be positive and meet any bond or statutory covenants?

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ASOP #3 Terminology

Criteria 1	100% + funded status
Criteria 2	Pricing margin > 0%
Criteria 3	Project positive cash balances and meet debt covenants

Unified funded status "UFS" combines criteria 1+2

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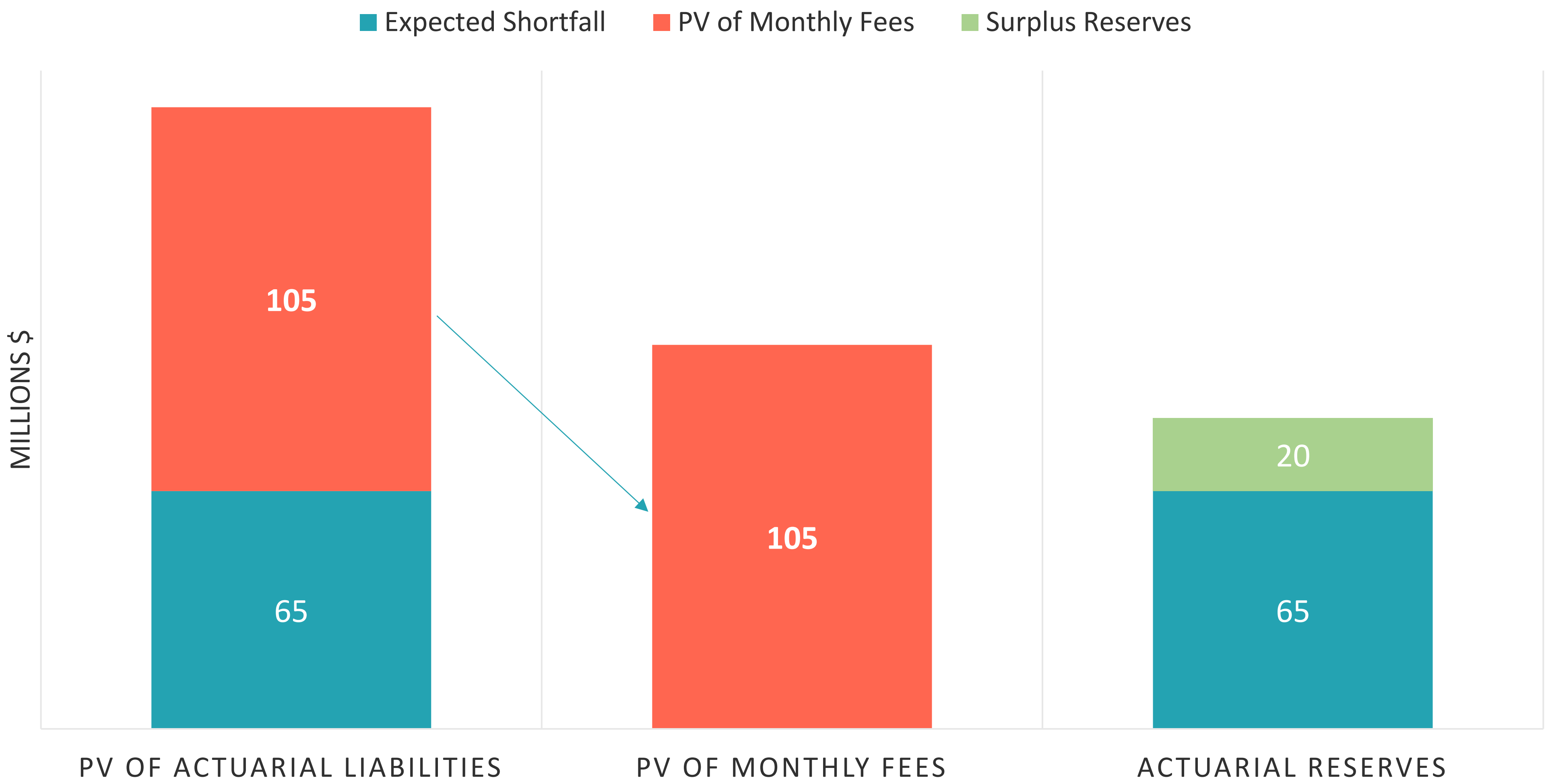
For the existing resident cohort, we expect future liabilities to be greater than future monthly fees



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New Entrant Pricing
Breakeven EF = Costs minus Monthly Fees

Total Lifetime Costs	=	$1,126,000
ILU Monthly Fees	=	691,000
ALU Monthly Fees	=	122,000
SNF Monthly Fees	=	81,000
Sum of Monthly Fees	=	894,000
Break-even Entry Fee	=	232,000
10% margin Entry Fee	=	344,600

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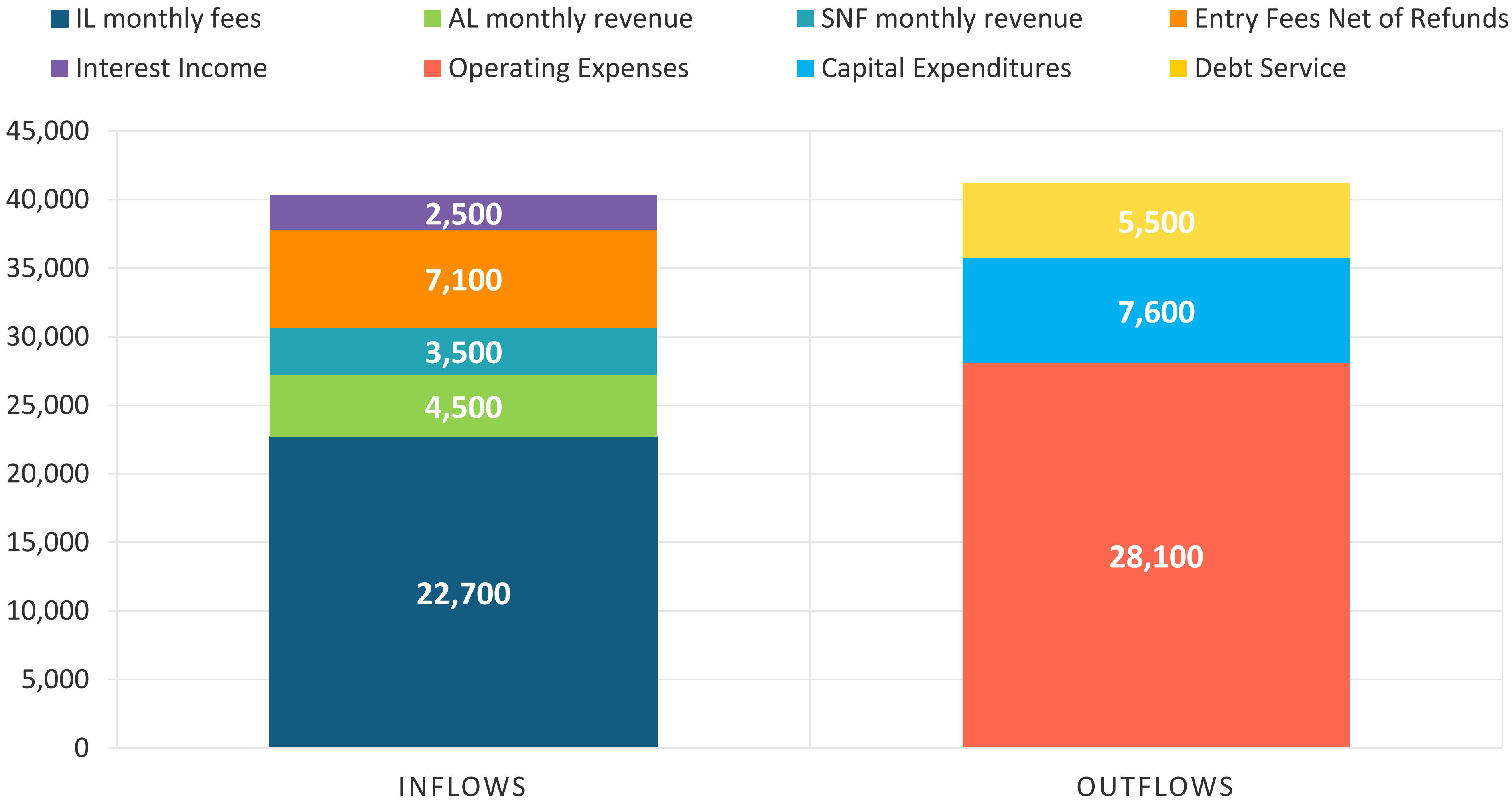
Year 1 Cash Flows: a $900K reduction in reserves



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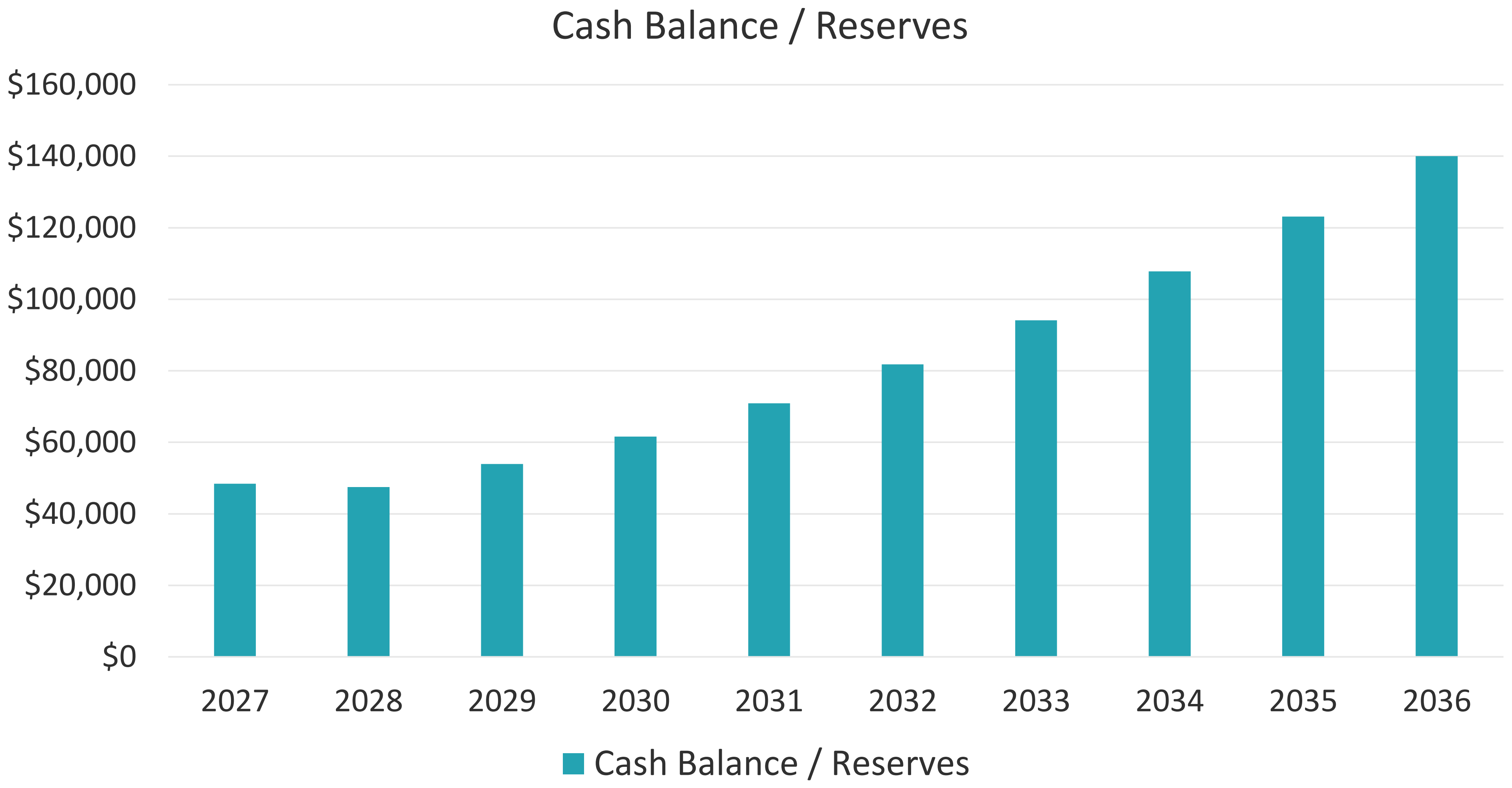
Cash Flows lead to growth after Year 1



Satisfactory Actuarial Balance (SAB)

	SAB with Qualification	SAB	AVP Seal
Actuarial Funded Status (ASOP#3 criteria #1)	100%	105%	>105%
Pricing Margin (ASOP#3 criteria #2)	0%	5%	>10%
Projected Cash Flows (ASOP#3 criteria #3)	1.0x	1.5x	2.00x
Unified Funded Status (ASOP#3 criteria #1 & 2)	100%	100% - 115%	>115%

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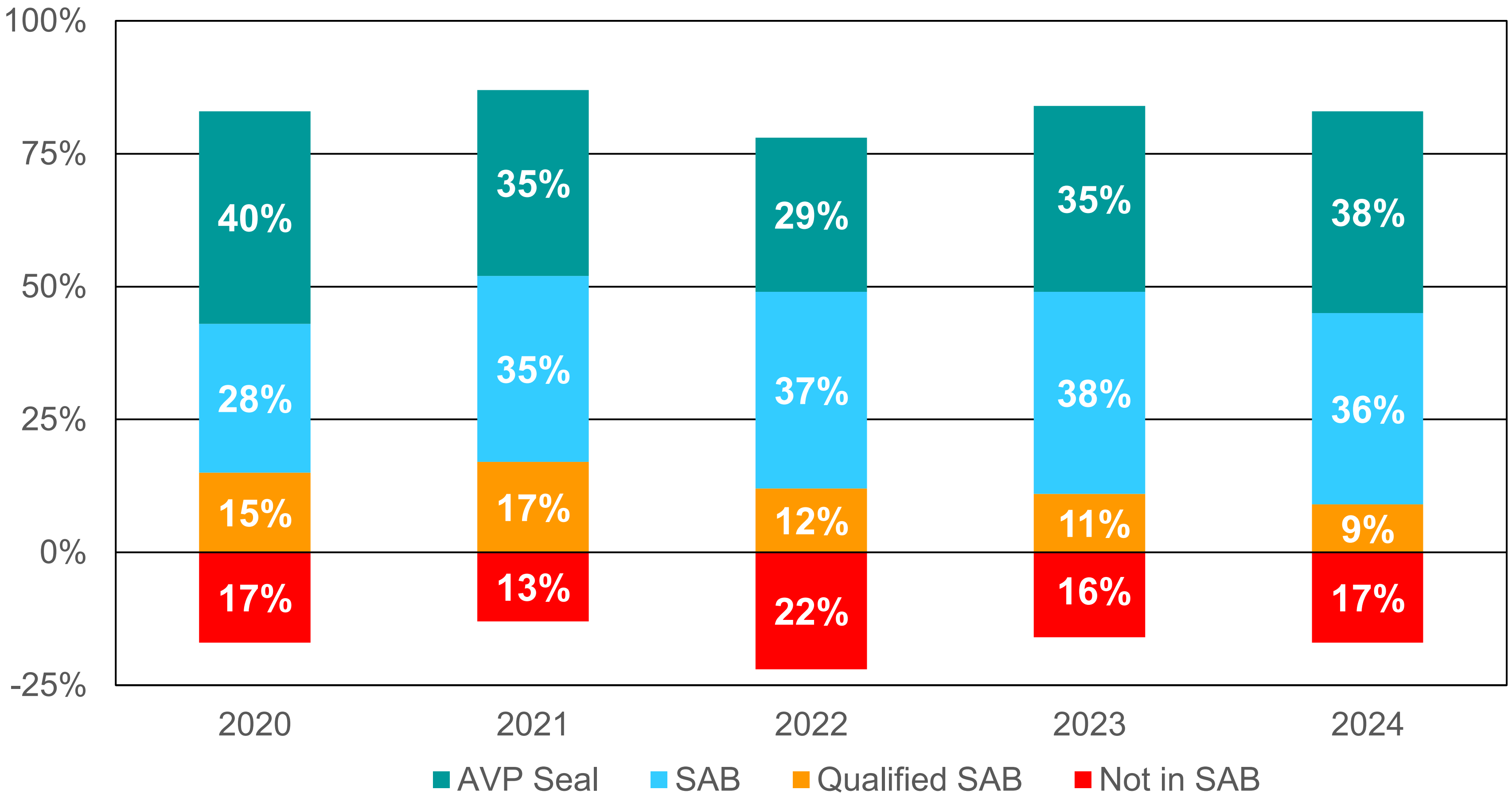
Over 80% of AVP clients are in SAB for ASOP#3



What else is in an actual study?

Primary

(almost always included in a study)

- Experience Analysis
- Population Projection
- Projected Debt Service
- Benchmarking

Optional

(sometimes included in a study)

- Executive Summary of SAB
- FSO
- Sensitivity Testing
- Expansion Analysis
- Refinancing Analysis
- Projected Future Metrics (Funded Status, FSO, GAAP Metrics)

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These same actuarial criteria work well to assess the solvency of Continuing Care at Home and Early Admission programs

- Funded Status
- New Entrant Pricing
- Cash Flow Projection

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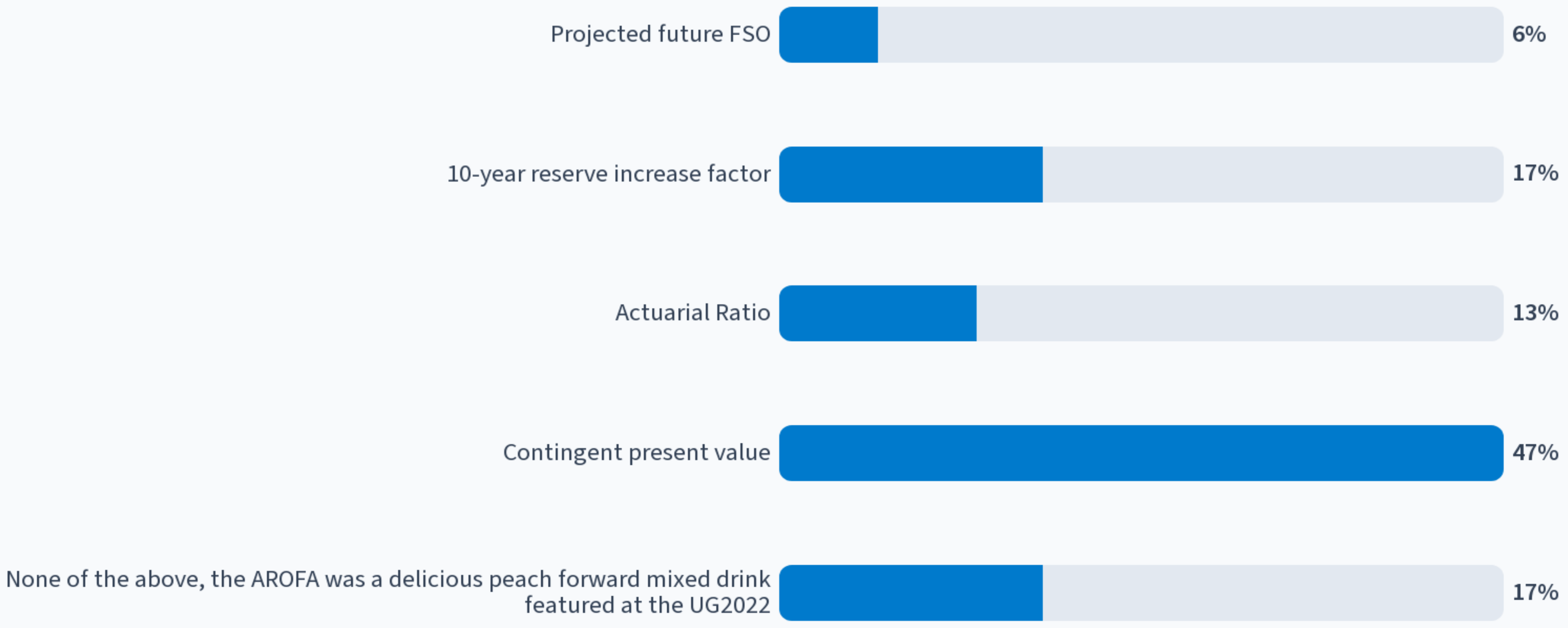
Hard Trivia Question: Which of these concepts is AROFA (Actuarial Return on Fixed Assets) associated with?

47



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Why is Satisfactory Actuarial Balance (SAB) Important?

1. Help ensure ability to meet contractual lifetime obligations
2. Promote a self-supporting fee structure
3. Provides a means to fund obligations should provider cease selling continuing contracts without external or cross subsidy
4. Minimize risks of bankruptcy
5. Is it the Board's fiduciary responsibility if selling lifetime contracts?
6. Maximize likelihood of relatively stable fee adjustments

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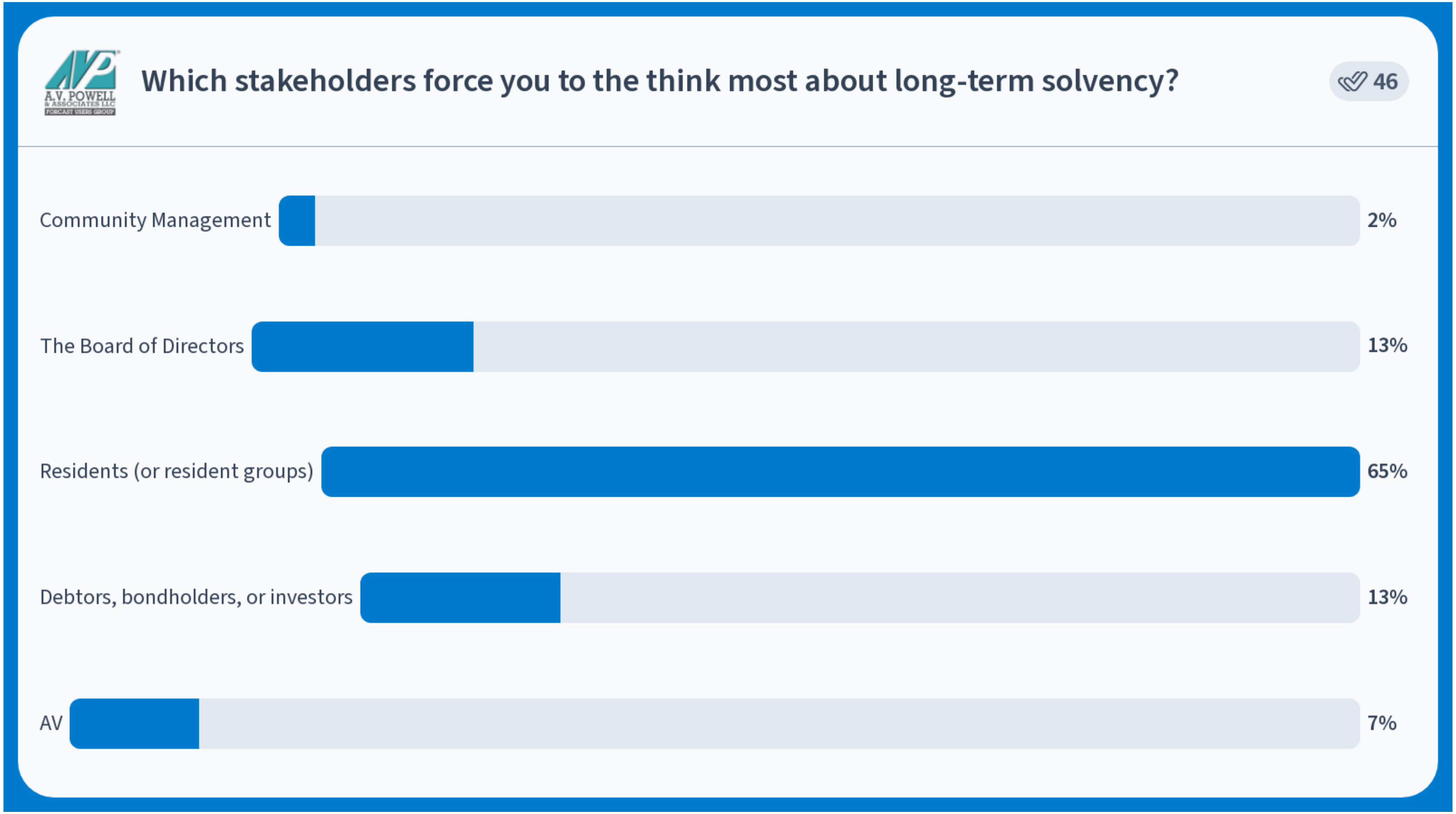
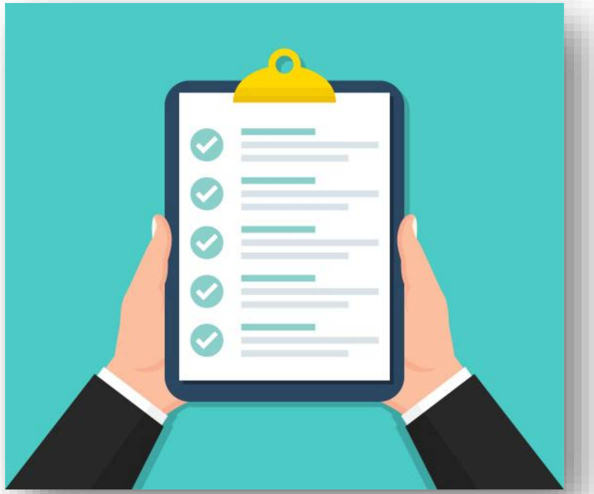

Which stakeholders force you to the think most about long-term solvency?
46
Community Management
2%
The Board of Directors
13%
Residents (or resident groups)
65%
Debtors, bondholders, or investors
13%
AV
7%

Are actuarial studies a “check box” or a valuable management tool?



- ✓ 85% of our clients are in non-regulated states
- ✓ A significant percentage of CCRCs conduct actuarial studies
- ✓ >50% do so voluntarily; best practice for entry fee contracts
- ✓ Actuarial studies do what they are designed to do…
  1. Assess financial solvency for a CCRC
  2. Determine fee adequacy & increases for all types entry fee contracts
  3. Estimate future health care needs
  4. Where needs are served based on provider & resident desires

No other financial tool can answer these questions

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How Management should use an Actuarial Study

- Fund Reserves
- Price contracts appropriately
- Monitor (and Mitigate) risks
- Plan for Capacity Needs
- Plan for Expansions and Changes
- Build Credibility

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Summary

- Solvency is Important.
- An actuarial study is the best available tool for assessing the solvency of a Life Plan Community.
- Frequent studies are best practice.
- Pass on a legacy of financial strength to future management, boards and residents.

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Questions & Answers