Ensuring the Survival of Life Plan Contracts

The Actuarial Creed

The work of actuarial science is to substitute facts for appearances and demonstrations for impressions by analyzing the financial costs of risks and uncertainty.

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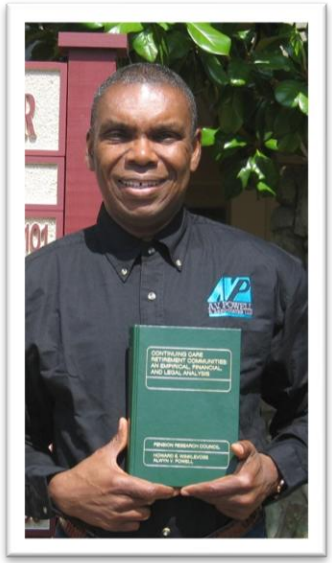
Presenter



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Learning Objectives

1. Identify the risk pooling components embedded in continuing care contracts.
2. Analyze the challenges industry practices present for funding refundable entry fee contracts.
3. Evaluate whether GAAP metrics substantially align with actuarial standards.

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Complex Contracts that Many Don't Understand

1. Pay-as-you pricing dominates practice, i.e., "cash is king", but
2. Collect 30%+ in upfront monies

3. Consumers risk a significant portion of their nest egg
4. Provider solutions to address financial difficulties are to rewrite contracts to shift risks to consumer, such as
    a. Previous use of contingent refundable contracts
    b. Trend toward reduction of long-term care benefits

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What is a Life Plan aka Continuing Care Contract?

1. Promise a **lifetime set of services** as contractholder **transitions among wellness levels**
2. Enrollment/purchase subject to underwriting criteria
3. Includes “managed” care coordination
4. Monthly fees, additional charges, and reimbursements fund a portion of these **costs/expenses**
5. **Entry fees must fund “costs – monthly fees”**
6. Pricing philosophy of generational self-supporting fees
7. Do contractual obligations for refunds obviate moral considerations for providers?

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Contract Misconceptions

1. Industry terminology is misleading
2. Types A, B, C (so-called fee-for-service), and D
3. Categories have been used to avoid financial regulation
4. Fee-for-service with an entry fee is a **misnomer**
5. Possible renaming of contracts to reflect fact that variations are different levels of copayment and not risk mitigation

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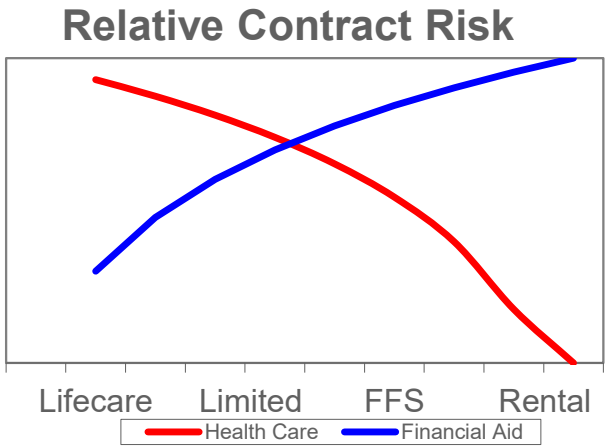
Best LTCi Option for Late Adopters

Contract design appeals to “planner” senior who wants to:

1. Protect themselves from costs of excessive health care usage
2. Protect themselves from depleting their financial resources
3. When fees don’t match costs, then risk pooling is embedded



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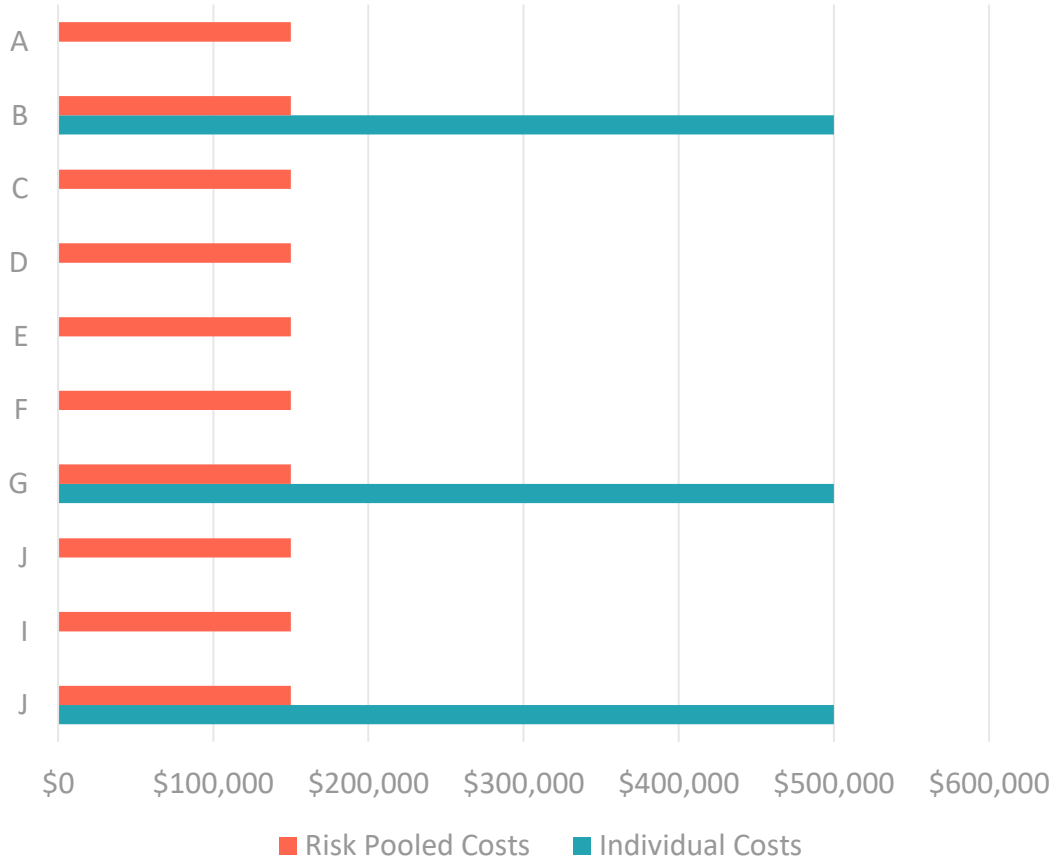
What is “Risk Pooling?”

1. Assume 10 homogeneous people
2. 30% chance of loss
3. 3x lifetime costs of $500,000
4. 7x lifetime costs of $0
5. Risk pooling costs = $150,000



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Will Continuing Care Contracts Go Extinct?

1. Publicity over bankruptcies
2. Lack of consumer knowledge and appreciation of benefits
3. Consumer moving away from entry fees with desiring equity
4. Growth of other senior housing concepts like Villages

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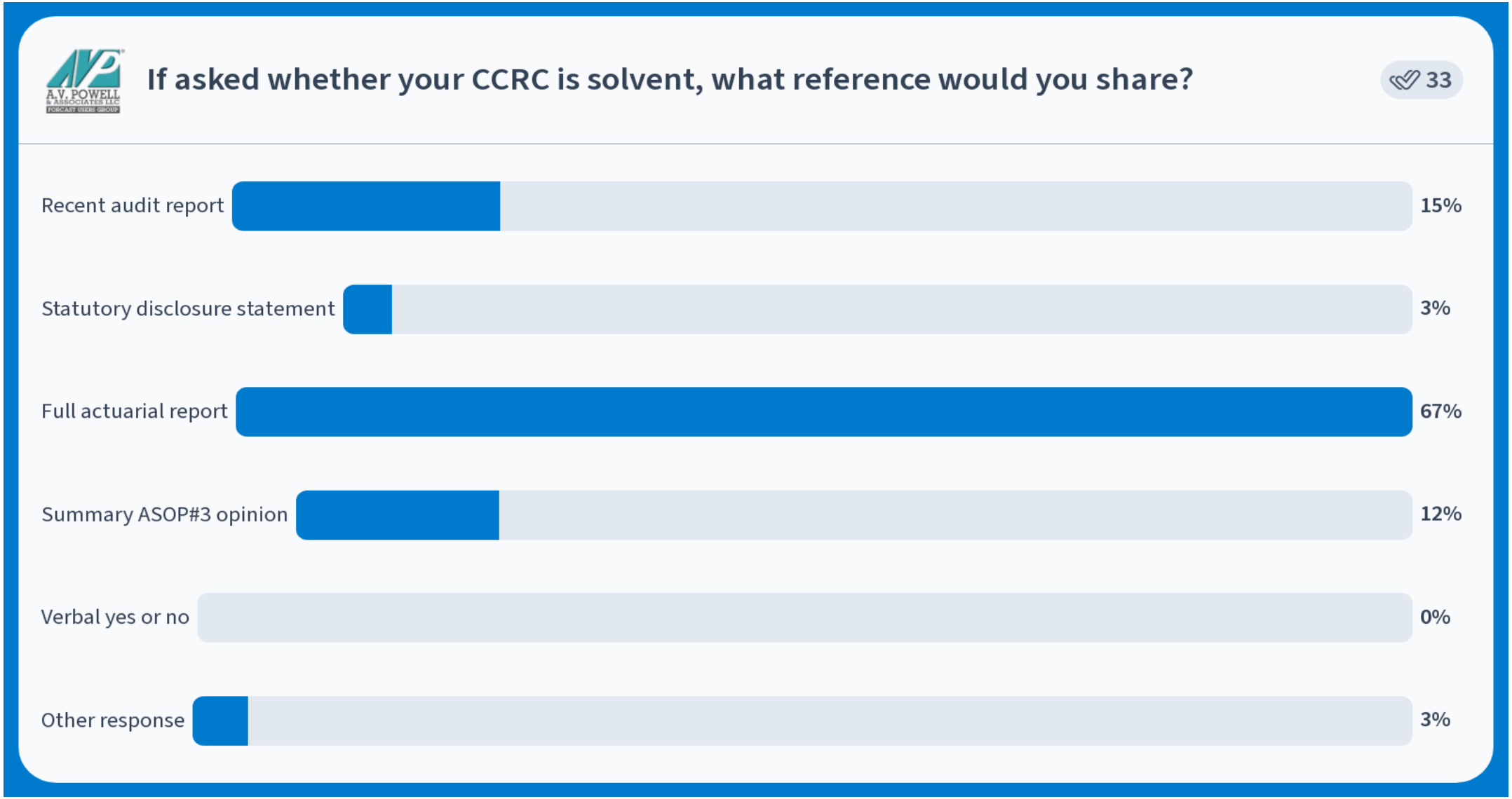
If asked whether your CCRC is solvent, what reference would you share?
33
Recent audit report
15%
Statutory disclosure statement
3%
Full actuarial report
67%
Summary ASOP#3 opinion
12%
Verbal yes or no
0%
Other response
3%

Creditworthiness ≠ Long-term Financial Solvency

1. Current CCRC financial metrics address creditworthiness
2. Debt service reserves (DSR)
3. Days cash-on-hand (DCoH)
4. Net Operating Margin (NOI)
5. Statutory minimum cash balance
6. Ratio of cash and investments to refund liabilities
7. Bond ratings

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GAAP Metrics have Low Correlation with ASOP#3

1. ASOP#3 measures whether fees + reserves for a group of contractholders are expected to cover their costs
2. Internal statistical analysis not able to identify a GAAP surrogate for ASOP#3 solvency measure
    a. 250+ client studies between FYE 2022 through 2024
    b. Individual GAAP ratios as well as combinations tested
    c. Unpublished results show very low P and R^2 values

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Comparative ASOP#3 vs. GAAP Balance Sheet

EXHIBIT A
Comparative Balance Sheets
As of December 31, 2023 and Based on Census as of December 31, 2023
Traditional Valuation Method

	ASOP#3	GAAP
CURRENT ASSETS:		
Cash and cash equivalents	3,638,090	3,638,090
Accounts receivable	238,123	238,123
Prepaid expenses/inventory	298,914	298,914
Subtotal	4,175,127	4,175,127
OTHER ASSETS:		
Board restricted assets	15,746,726	15,746,726
Deferred marketing	51,436	51,436
Subtotal	15,798,162	15,798,162
FIXED ASSETS:		
Fixed assets net of depreciation*	94,821,866	75,629,155
CIP	0	316,945
Deferred financing	0	1,035,853
Subtotal	94,821,866	76,981,953
TOTAL ASSETS:	114,795,155	96,955,242
CURRENT LIABILITIES:		
Accounts payable	588,328	588,328
Accrued expenses	1,200,061	1,200,061
Current portion of long-term debt	0	2,387,546
Accrued interest	0	133,707
Subtotal	1,788,389	4,309,642

[Comparative Balance Sheet Example]

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Refunds are Inherently Risky at Older Ages

1. Many financial difficulties lead to delays in refund payments
2. Ask if balance sheet shows any refunds due to terminated contracts
3. Providers and consumers should mutually understand
   a. Entry fee is a prepayment for future services, not a loan or equity
   b. Funding based on next-generation fees is contrary to insurance principles
4. Alternatives are
   a. Purchase a whole life insurance policy if available
   b. Change federal bankruptcy laws—long shot

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Seek Contract Future Proofing Solutions

1. Set contract benefits based on functional status
    a. Aging-in-place
    b. May mitigate “heavy-tail” long-term care risks

2. Fund/protect nonforfeiture reserves for refund options

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