

Long-term care (LTC) insurance is a key component of the social safety net. But most organizations have offered long-term care as an individual benefit rather than as a group benefit. Through savvy benefit design, employers can provide a benefit that will be more attractive and affordable to employees, making long-term care a major pillar of an organization's benefits strategy. For employers, the cost is reasonable and containable—about the same price as a dental benefit.

True Group Long-Term Care Insurance

Leaders Wanted

by Jonathan Shreve

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Anyone who is involved in employee benefits—actually, just about anyone who watches the news—knows that employer-funded benefits are in crisis. Rising costs and tough new accounting rules challenge even the most progressive firms. Last summer's Pension Protection Act (PPA) was the most significant pension legislation since the Employee Retirement Income Security Act of 1974 (ERISA). PPA fundamentally changes the benefits landscape in ways that are only beginning to come into focus. As the job market tightens, employers may find it difficult to attract and retain top talent unless they can offer quality benefits.

Clearly, employers have a role to play. If they can offer LTC coverage at a reasonable cost to themselves and their employees, they can diversify struggling benefit portfolios while helping to address one of the most challenging problems faced by contemporary society.

Currently it is uncommon for employers to offer LTC coverage as anything but an employee-pay-all program. But the environment may be changing. The LTC market has been consolidating, and some carriers have exited the market—even as the need for LTC coverage continues to grow. As commercial options become less readily available, self-funded LTC may be-

of service—or whether the employee is even interested in the coverage—fail to reward and help retain loyal workers. This results in either low benefit levels or high costs to the employer, further reducing the “bang for the buck.” Finally, these plans can lull participants into a false sense of security: Employees may think they have adequate coverage when, in reality, the amount provided is usually quite small, and the additional coverage is not necessarily affordable.

The major problems with both of the aforementioned strategies are that, while they are certainly easy on the employer's bottom line, no real benefit is conferred on employees; and low participation rates reduce any good the plans might do. Why offer a benefit that really isn't a benefit? Meaningful LTC coverage is too important to remain in the realm of mere convenience—And the potential benefit to the employer of offering it is well worth the investment.

Still, that monetary investment must be made, because a salient feature of true group insurance is that the employer subsidizes it. Without this commitment, any insurance product, whether it is life, health or LTC insurance, is simply offered at the place of employment, not by the employer. It may be a convenient place for employees to obtain coverage with some savings on commissions, but that is far from compelling when a cornucopia of similarly priced plans are just a few mouse clicks away. The firm's contribution is essential in bringing the cost of meaningful coverage low enough to encourage widespread participation among the workforce; that is clear from the current state of affairs.

“Acorns were good until bread was found.” **—Francis Bacon**

What do we mean by “quality”? *Quality benefits* are those for which the employer pays either all or a substantial portion of the premium, and employees are able to carry a meaningful benefit into retirement. In this article we will use the term *true group* to describe such benefits as we look at true group LTC insurance.

LTC is one of the most neglected areas of the social safety net—and therefore one of the most promising areas for human resources (HR) executives and insurers wanting to fill in the gaps left by the decline in traditional benefits.

Even a cursory glance at the facts demonstrates the severity of the issue:

- 43% of those over the age of 65 will require some LTC.¹ As the population ages, the total number of users will grow substantially.
- The U.S. average cost is \$62,532 annually for a semiprivate room in a nursing home, with a private room coming in at \$70,912.²
- Medicare does not cover LTC. Medicaid requires that an individual or couple spend down assets to almost nothing before it will pay for LTC.
- Even so, only about 3% of Americans have LTC coverage.³
- A five-year nursing home stay costs more than \$300,000 in today's dollars. At that rate, such an event could devastate the average worker's retirement savings. Even if employers provide generous retirement plans, LTC insurance is necessary to protect those savings.

come a valuable component of any organization's overall benefit package.

When Is a Benefit Not a Benefit?

Almost all LTC insurance sold through employers today requires the employee to pay the entire premium. The employer does not contribute financially to the plans, and employee participation is purely voluntary. They are *group* plans only in the loosest sense of the term.

Since the employer contributes nothing, the cost to insureds is similar to what they would pay for an LTC plan on the open market, even taking into account somewhat lower agent commissions on “employer-provided” plans. Employees get little more than the convenience of a payroll deduction. Consequently, participation in these plans is usually extremely low. What is worse, the choice between plans offered through the company agent and those offered by unrelated providers creates confusion, leading many workers to purchase no coverage at all and leaving them unprepared should they need LTC.

A *core/buy-up plan* is an alternative in which the employer provides a small amount of “core” coverage for all employees, who in turn have the option to “buy up” to higher levels by purchasing supplemental coverage. This is a first step toward employer-provided coverage. But such plans have their pitfalls. Benefits given to all employees without regard to length

A New Approach: The True Group LTC Plan

Keeping the cost of coverage low for employees is important to solving the LTC problem and creating a meaningful benefit. Yet costs must be reasonable for employers as well. While employee benefits fulfill an important social function, they are not charity. They are compensation for loyalty and service. The cost of providing the benefit should not outweigh the return to the employer in

Continued on next page

Vesting and Waiting Period Savings (No Employee Contribution)

Savings Over Plan Without Vesting or Waiting Period

Vesting Period	No waiting period	One-year waiting period	Two-year waiting period
Zero years	0%	12%	25%
Five years	44	44	46
Ten years	51	51	52
Twenty years	61	61	62
Ten years and age 50	55	55	55

Source: True Group Long-Term Care, Jonathan Shreve and Jill Van Den Bos, International Foundation of Employee Benefit Plans, Inc., 2004.

terms of increased employee loyalty and satisfaction.

In contrast to current “group” LTC plans, which do not save employees much money or provide much of a boost for employers, the true group LTC benefit is designed to balance the interests of both parties and provide reasonable returns for both. From the worker’s point of view, the value is obvious.

Simply because of employer contributions, employees would receive LTC coverage for significantly less than they would pay on the open market.

Keeping Costs Down

The first question employers are likely to ask is: How much will it cost? The (rather attractive) answer for LTC policies currently offered at places of work is, “nothing.” For a benefit that helps employers attract and retain employees while addressing the crisis of LTC, that answer will have to change. That said, convincing employers, most of which are already stretched to the limit in terms of providing employee health and life benefits, to subsidize yet another benefit is likely to be an uphill battle in any case. If the cost is too high, that effort will be lost before it is begun.

And employers have a point: An LTC benefit designed without cost-containment features might be prohibitively expensive. Yet with those features in place, true group LTC benefits could be affordable for both employers and employees. Best of all, benefit designers can tune the benefit to meet an employer’s specific

goals, whether those goals include improving the safety net, increasing loyalty or minimizing costs.

The key parameters in designing a cost-effective true group LTC plan are familiar to anyone who works with pensions or retiree medical plans: waiting periods and vesting. Waiting periods and vesting both limit the employer’s exposure by offering the plan only to longer term employees. This can drive down premium costs to a remarkable degree. The fact that the group is composed of reasonably healthy, working-age individuals, rather than a larger swath of the population, also reduces the cost of coverage. This is because such groups will tend to use lower benefit amounts over the life of the plan.

These tried-and-true features are usually present when a benefit is paid long after the employee is hired, making these features ideal for an LTC offering. Not only would these measures keep costs low for employers, they would also drive down overall plan costs and provide even better value for workers.

Waiting Periods

Because they reduce plan costs and complexity while rewarding loyalty, waiting periods are now fairly standard for health, life and retirement benefits in most industries. A waiting period for true group LTC coverage would work in similar fashion: New employees would be subject to a set period during which they could neither contribute to nor benefit from the company’s group LTC coverage.

In addition to rewarding loyalty and stability in the workforce, waiting periods reduce costs in two ways.

First, they avoid adding to the ever-rising administrative expenses associated with employee turnover. Simply put, hiring people costs money. Those who stay for a shorter time may not add enough value to the company to justify the administrative costs associated with starting and managing the benefit. An employee who stays for more than a year or two is likely to stay even longer. Because of reduced hiring costs, such employees will probably more than compensate for the cost of signing them up. With a waiting period, the overall cost of the plan itself may also go down, because fewer total employees participate; those who stay for a time shorter than the waiting period never enter the plan and therefore never draw any benefits from it.

Industry-standard waiting periods for pension plans range from three to 12 months (12 being the maximum allowed for ERISA qualification). The author recommends one to two years for a true group LTC plan. In a 2004 study (see Table I), a rich, fully employer-funded plan with no waiting or vesting as a baseline was used. It was calculated that adding a one-year waiting period to the plan would result in a savings of 12%, while a two-year waiting period would shave 25% off the plan cost before employees contribute a penny. (Table II shows the savings with a 50% employee contribution.)

Vesting and Waiting Period Savings (50% Employee Contribution)

Savings Over Plan Without Vesting or Waiting Period

Vesting Period	No waiting period	One-year waiting period	Two-year waiting period
Zero years	70%	74%	77%
Five years	83	83	84
Ten years	85	85	85
Twenty years	88	88	88
Ten years and age 50	86	86	87

Source: True Group Long-Term Care, Jonathan Shreve and Jill Van Den Bos, International Foundation of Employee Benefit Plans, Inc., 2004.

Table II

Vesting

The second cost-saving feature is vesting. As in a pension plan, a *vesting period* is the time an employee has to work for the employer before becoming eligible for the employer-funded portion of the plan. When vested employees depart or retire, the employer stops making contributions on their behalf.

There are two kinds of vesting typically used in defined benefit plans: graduated vesting and cliff vesting. In *graduated vesting*, employees are gradually vested over a period of years. This type of vesting holds no particular advantage for LTC plans. It is also more expensive to administer and harder to explain to employees. Instead, the author recommends *cliff vesting*, in which an employee is fully vested all at once after a certain number of years of employment. A five-year vesting period is typical. Cliff vesting is more than adequate for rewarding and retaining loyal employees while keeping per employee costs low. In the previously cited study, it was estimated that a five-year vesting period (with no waiting period and no employee contributions) would reduce the total cost of the hypothetical plan by 44%.

Vesting Issues

Vesting, particularly in a highly liquid labor market such as the one in the United States, creates several scenarios that require careful thought. First of all, most LTC plans offer some protection to members immediately upon joining (that

is, before they reach the minimum age level at which full benefits are available). Employees who need LTC benefits after joining the plan but before fulfilling the vesting period should receive those benefits in full, regardless.

For employees who leave the company before they are vested but without drawing benefits, plan designers have two options. On one hand, the employee-funded portion of the benefit may be refunded in whole or in part and coverage canceled altogether. This leaves the affected individuals uninsured and, if they are reaching retirement age, possibly unable to afford the LTC coverage they need. On the other hand, they may be allowed to continue paying for their portion of the policy in exchange for a reduced benefit. Only one of these two options should be provided, however, because employees who are likely to need coverage will be more likely to stay in the plan, creating adverse selection and disproportionately increasing the overall plan cost.

Another likely scenario is that some employees become fully vested but leave employment before they retire. Here it is useful to think of the account in two parts—the employee-funded portion and the employer-funded portion—and, for simplicity's sake, split them 50/50. Those who stopped contributing to the plan after separation would be eligible for only the portions of coverage that were fully funded beforehand. Employees who continue to pay their portion after they departed could receive the employee-funded 50% of their benefit and whatever portion of the employer-funded benefit

was paid before they left. Finally, employees could choose to step up their payments to make up for the employer's contribution, making them eligible for the whole of the contracted benefit. Adverse selection among ex-employees can be a significant problem, so whichever of the three options is offered and whether or not underwriting is part of continued coverage should be carefully considered.

Finally, there is the issue of postretirement contributions. Most plans will be designed so that the employers' portion is fully funded by the time a typical employee retires, say, at the age of 65. To keep the periodic cost for employees low and encourage participation, many plans will allow employees to pay their part over their expected life span, which might be 85 years or more. When employees retire, the employer portion will be totally funded. If they choose not to continue contributing to the plan, they only lose the part of the benefit that would have been funded by their postretirement contributions.

All Aboard: Increasing Employee Participation

Participation in employer-sponsored individual plans is low—occasionally from 6% to 15%, but often as low as 1%. Of course, cost is the major barrier to participation in LTC plans. While employer contributions will make a huge difference, another feature unique to the LTC arena also

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keeps employee premiums low: The contribution periods can differ for employer and employee. LTC coverage is generally funded by premiums paid over the life of the insured (although many plans waive premiums if the insured is actually using the benefits). For an employer-funded plan, a given company would likely prefer to pay contributions only during the working life of the employee (to age 65, for example) while the employee continues to

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fund the policy after retirement, in effect spreading the employee's portion of the premiums over a longer period of time. Employer-paid benefits will be fully accrued during the employee's working life; yet, the employee's contribution remains reasonable.

Cost is one part of the equation; education is another. Getting employees to participate in 401(k) plans is difficult enough; the need for LTC seems even more remote than retirement for the average person and the notion is much less pleasant. When offering group LTC coverage, employers must commit to educating employees about the issue in a way that encourages them to participate.

Onward

All told, the author's calculations indicate that meaningful LTC coverage would cost an employer \$5 to \$25 per employee per month. This is certainly a reasonable investment for such a necessary and powerful benefit.

As it stands, insurers are quite happy to provide individual LTC plans through contracts with employers. These plans fit the commission-based revenue model of today's insurance industry and provide agents with the opportunity to sell policies to families of employees. True group LTC coverage would benefit the industry in the long run by drastically increasing the number of participants, but currently there is no strong incentive for companies to design and offer such plans.

Executives and HR personnel at companies with sufficient numbers of employees have a unique opportunity to lead the charge for LTC that is a real benefit. The innovative approach of true group

LTC represents not only a forward-thinking solution to this critical benefit for employers, but also a key market opportunity for insurers. Benefits consultants and other theorists have studied the concept of true group LTC coverage, yet it remains largely untried. This approach to LTC can revolutionize the current implementation of this vital benefit through collaboration among employers, insurers and benefits consultants. **B&C**

Endnotes

1. P. Kemper and C. M. Murtaugh, "Lifetime Use of Nursing Home Care," *New England Journal of Medicine*, Vol. 324, No. 9 (February 28, 1991).
2. Genworth Financial, *Genworth Financial 2006 Cost of Care Survey*, March 2006.
3. "America's Health Insurance Plans, Issues and Advocacy: LTC Insurance." Retrieved from www.ahip.org/content/default.aspx?bc=39|341|328 on August 24, 2006.

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