Economic Impact Analysis
Virginia Department of Planning and Budget

12 VAC 30-10; 20; 40 –Long-Term Care Partnership Insurance
Department of Medical Assistance Services
February 1, 2007

Summary of the Proposed Regulation

Pursuant to §32.1-325(A)(24) of the Code of Virginia enacted by the 2006 General Assembly, the proposed regulations will implement a Medicaid long-term care (LTC) partnership insurance program in the Commonwealth.

Result of Analysis

There is insufficient data to accurately compare the magnitude of the benefits versus the costs. Detailed analysis of the benefits and costs can be found in the next section.

Estimated Economic Impact

LTC partnership insurance programs have surfaced in 1980s after a grant by the Robert Wood Johnson Foundation provided start up money for developing programs that would integrate public-private partnerships in LTC financing. California, Connecticut, Indiana, and Massachusetts were the recipients of this seed grant and all of them implemented LTC partnership programs that are still in effect today. After the initial four states obtained waivers from the Centers for Medicare and Medicaid (CMS) to implement different eligibility rules, 1993 Omnibus Budget and Reconciliation Act prohibited CMS to issue any more waivers. However, in 2005, a significant change occurred. The Deficit Reduction Act of 2005 allowed, but did not require states to implement a LTC partnership program. Following the removal of this federal legislative barrier, House Bill 759 from the 2006 Virginia General Assembly (now §32.1-325(A)(24) of the Code of Virginia) required the Department of Medical Assistance Services (DMAS) to implement a LTC partnership insurance program in accordance with federal guidelines.

The proposed regulations set out the criteria that LTC partnership insurance policies must contain to be eligible for benefits the regulations will provide. These benefits include: 1) being able to disregard assets equal to the pay out of a LTC partnership insurance policy while determining Medicaid eligibility and 2) being able to protect assets equal to the pay out of a LTC partnership insurance policy from estate recoveries. For example, if an individual purchases a qualifying LTC partnership insurance for $100,000 in payout benefits, gets LTC coverage for two years after which he applies for Medicaid eligibility, he would qualify if his assets are less than $102,000.[1] Also, the $100,000 in assets would be exempt from estate recoveries if the recovery process is initiated.

The economic literature[2] on LTC partnership insurance is limited. The financial effects of LTC partnership insurance on Medicaid are currently debated with a somewhat limited scope and there is no empirical research offering concrete findings due to lack of data that can be used to answer pertinent questions. The current research is useful however for providing demographics information from the experiences of a few states that have had an active LTC partnership insurance since 1980s. The table in the Appendix provides some relevant information from California and Connecticut experiences.[3] This report discusses the potential and likely effects of the proposed regulations on the three entities that will be affected in an abstract setting.

The implementation of LTC partnership insurance will affect the individuals who are likely to receive LTC from Medicaid, the LTC insurance companies offering qualified policies, and the Medicaid program that is often the provider of last resort for those who cannot afford LTC by any other means (i.e. the safety net for LTC).

The proposed regulations will provide individuals an option to protect a portion of their assets should they need LTC later in their lives. Economic principles suggest that individuals who are most likely to gain from asset protection would have stronger incentives to purchase a LTC partnership insurance. At the least, individuals with significant assets, individuals with ability to afford monthly premiums, individuals with strong desire to pass on assets to their heirs are expected to have stronger incentives to take advantage of this option than those without.

[1] Currently, an individual must have assets less than $2,000 to qualify for Medicaid.
[2] See References section for studies reviewed.
[3] The data from New York and Indiana models are not provided as their programs offer total asset protection and a hybrid model providing dollar-for-dollar and total asset protection, respectively.

Additional factors that may affect individual's decision to participate include the private knowledge of individual's health status, perceived likelihood of needing LTC, and the individual's propensity to take compliance avoidance actions in order to protect his assets if this option were not available. The knowledge of most of these factors by the individual is asymmetric in the sense that it is not known by the LTC carrier or Medicaid. The information asymmetry gives the individual an opportunity take advantage of the new option if perceived benefits to him are greater than perceived costs.

The presence of individuals with stronger incentives to purchase LTC is likely to have a positive effect on the demand for such policies. Increased demand will likely help insurance companies to sell more of these policies and help grow their businesses. Unlike Medicaid, private LTC companies have discretion over the premiums they can charge and the term of coverage they offer for a given premium level. With ability to change these factors, LTC insurance carriers are expected to offer policies that would maximize their profits or returns from their businesses. So, it is expected that the premiums would contain a mark-up for profits. Also, private carriers may be relatively more efficient in delivery of LTC services.

The net effect on Medicaid as the safety net depends on whether the asset protection will qualify additional individuals who would not otherwise qualify for LTC through Medicaid and whether the level of protected assets will be greater than the assets the individuals would have to spend down to qualify for LTC coverage through Medicaid. In addition, the Bureau of Insurance, the Department of Social Services, and DMAS are expected to incur approximately $17,500 in on going administrative costs to develop and maintain reporting and tracking procedures to process applications. Moreover, DMAS and the Department of Social Services are expected to incur approximately $187,500 in one time costs for programming expenses to develop, test, and implement changes to the eligibility file.

In the framework composed of individuals, private LTC insurance carriers, and Medicaid, likely net financial effect of the proposed regulations may be assessed under a few simplifying assumptions in an abstract model. In such a model, the first relevant question becomes whether the LTC partnership insurance would create additional net financial burden or benefit for the three entities combined. If there is no additional net financial gain or loss to the all entities combined, this situation in economics is referred to as a "zero-sum-game." In a zero-sum-game,

there is no net combined gain or loss in that the economic effects are purely distributional among the parties involved. That means net gains and losses for all parties sum to zero.

It appears that with a few caveats, the interactions between the individuals, private LTC insurance carriers, and Medicaid resulting from the implementation of the LTC partnership insurance could be considered as a zero sum game. Once the program is implemented, the first action will be taken by the individual. He will decide whether to purchase private LTC insurance to protect his assets in the event he needs Medicaid coverage. However, the decision to purchase LTC coverage now has no impact on the actual LTC coverage he will actually need in the future. In other words, whether he will fall frail and need nursing home care ten years later has nothing to do whether he purchased LTC insurance today. However, purchase of LTC partnership coverage today will determine who provides and pays the care when he is frail.

The main differences between providing LTC insurance through Medicaid or private carrier would likely stem from the relative efficiency by which the service is provided and the presence of profits in private delivery model. The net of efficiency savings in private delivery model minus carrier profits would represent an addition or subtraction to the zero sum game described above. Given that private carriers would not be able to sustain their business if their profits are less than the efficiency gains, it is highly unlikely, at the aggregate, for them to incur a net economic loss as a result of the proposed regulations.

The consumers could also change the nature of this zero sum game if some would no longer devote resources for compliance avoidance actions in attempts to shift their assets to other individuals to protect them from Medicaid program as they will have an option to do this legally now. Financial resources that would have been otherwise devoted to illegally shifting assets should be considered as an addition to the zero sum game. Individuals could also be willing to pay a premium to be able to protect their assets. Equipped with the private knowledge of own propensity for compliance avoidance actions and the willingness to pay for such attempts and the private knowledge of own health status and the likelihood of needing LTC, individuals would not purchase LTC partnership insurance plans if the perceived benefits does not exceed the costs. Thus, it is highly unlikely, at the aggregate, for them to incur a net economic loss as a result of the proposed regulations.

In a zero sum game with three players, if two parties are unlikely to incur net losses, by definition, the third player would be unlikely to incur net gains. However, this conclusion would not hold true if there are injections into the game from outside as discussed. For example, private carries may be able to offer LTC insurance at very competitive rates by delivering services efficiently and taking minimum profits. For all parties to gain, however, the sum of efficiency gains from delivering LTC by private carriers minus the private carrier profits plus the savings from eliminating compliance avoidance actions plus the value of being able to legally pass on assets to heirs minus the additional resources need to cover individuals with significant assets who would not otherwise qualify minus the additional administrative costs, must be a positive number.

Another provision in the proposed regulations could also create economic effects. The federal guidelines require states to have a compound inflation protection in the LTC partnership plans, but do not dictate what the compound rate must be. The proposed regulations do not specify the rate of compound inflation protection as DMAS is currently evaluating what would be the best option. Currently, some states require five percent standard compound inflation protection in LTC partnership policies. Despite the popularity of a fixed compound inflation protection among the states with partnership programs, a fixed compound inflation protection would not be economically optimal.

The optimal compound inflation protection rate would be the one that adjusts the pay out value of the policy as the cost of LTC changes in order to provide the same term coverage regardless of the changes in LTC inflation. If the rate is set too high, the cost of policy would increase and result in higher premiums than necessary. If the rate is set too low, the individuals face the risk of not being able to obtain the services for the term they are signed up for. It appears that the optimal compound inflation protection would be a variable rate indexed to the prices of goods and services that accurately reflects the LTC service delivery inflation.

Businesses and Entities Affected

These regulations will primarily affect the private insurance carriers selling LTC policies, individuals who would purchase these policies, and the state agencies that will be involved in the implementation of this program. Currently, there are approximately 36 companies offer LTC insurance policies for sale in Virginia. Also, approximately 3% of Virginians or approximately

219,000 individuals currently hold LTC insurance policies. However, the number private insurance carriers that may participate or the number of individuals who may purchase LTC insurance coverage as a result of the proposed changes are not known.

Localities Particularly Affected

The proposed regulations apply throughout the Commonwealth.

Projected Impact on Employment

The proposed regulations will encourage some individuals to purchase private LTC partnership insurance increasing the demand for such policies. Increased demand for LTC policies will likely positively affect labor demand by private carriers. Also, there will be a slight increase in labor demand for administration of the proposed program. However, the LTC services delivered by private carriers would also have an offsetting effect on the LTC providers contracted by Medicaid. In the presence of such balancing effects on labor demand, it is uncertain what the net impact on employment would be.

Effects on the Use and Value of Private Property

The proposed regulations will likely have a positive effect on the demand for private LTC insurance policies and may improve the profitability of the carriers. If this occurs, a positive effect on the asset value of private carriers would be expected. On the other hand, any decrease in the delivery of LTC services by Medicaid providers would have the opposite effect on the asset values of their businesses.

Small Businesses: Costs and Other Effects

The proposed regulations are not expected to affect small businesses. However, if approximately 26,193 resident agents and 42,537 non-resident agents are considered as small businesses, we would expect a positive impact on them as the demand for their services will likely increase.

Small Businesses: Alternative Method that Minimizes Adverse Impact

The proposed regulations are not expected to have any adverse impact on small businesses.

Legal Mandate

The Department of Planning and Budget (DPB) has analyzed the economic impact of this proposed regulation in accordance with Section 2.2-4007.H of the Administrative Process Act and Executive Order Number 36 (06). Section 2.2-4007.H requires that such economic impact analyses include, but need not be limited to, the projected number of businesses or other entities to whom the regulation would apply, the identity of any localities and types of businesses or other entities particularly affected, the projected number of persons and employment positions to be affected, the projected costs to affected businesses or entities to implement or comply with the regulation, and the impact on the use and value of private property. Further, if the proposed regulation has adverse effect on small businesses, Section 2.2-4007.H requires that such economic impact analyses include (i) an identification and estimate of the number of small businesses subject to the regulation; (ii) the projected reporting, recordkeeping, and other administrative costs required for small businesses to comply with the regulation, including the type of professional skills necessary for preparing required reports and other documents; (iii) a statement of the probable effect of the regulation on affected small businesses; and (iv) a description of any less intrusive or less costly alternative methods of achieving the purpose of the regulation. The analysis presented above represents DPB's best estimate of these economic impacts.

References

U.S. Government Accountability Office, 2005, "Long-Term Care Partnership Program."

Congressional Research Service, 2005, "Medicaid's Long-Term Care Insurance Partnership Program."

George Washington University School of Public Health and Services, Undated, "The Long-Term Care Partnership Program: Issues and Options."

State of Connecticut Office of Policy and Management, 2005, "Annual Report for the Connecticut Partnership for Long-Term Care."

Minnesota Department of Human Services, 2005, "Public and Private Long-Term Care Financing: Options for Minnesota."

U.S. Department of Health & Human Services, 2004, "What We Know about Buyers and Non-Buyers of Private Long-Term Care Insurance: A Review of Studies."

Centers for Medicare and Medicaid, 2005, "Policy Options for Addressing Medicaid Long-Term Care, Report of the Council on Medical Service."

Appendix

Table: Selected Statistics from Existing LTC Partnership Programs

	California	Connecticut
Year implemented	1994	1992
Policies in force in 2005	64,915	30,834
Number of participating insurance companies	5	8
Average policy holder age	60	58
Policy holder age range	18-92	20-89
Policy holder gender	59% female, 41% male	56% female, 44% male
First time purchasers	94%	92%
Percent of policy holders with reported assets greater than $350,000	53%	54%
Percent of policy holders with reported income greater than $5,000	61%	62%
Number of applications received	93,577	46,564
Percent of applications denied	17%	12%
Polices that remain active	84%	81%
Percent of comprehensive coverage polices	95%	99%
Percent of nursing home only coverage polices	5%	1%
Daily benefit amount	$150 per day is most common	$187.60 per day for nursing home care and $166.91 per day for home and community based care
Benefit coverage period	Lifetime coverage is most common	2 to 3 years of coverage most common
Number of policy holders who ever received benefits	913 (1.2%)	351 (0.9%)
Number of policy holders who are currently receiving benefits	343 (0.5%)	141 (0.5%)
Number of policy holder who exhausted benefits	89	35
Cumulative asset protection earned by policy holders who have exhausted benefits	$4,958,421	$4,200,808
Per capita asset protection earned by policy holders who have exhausted benefits	$55,713	$120,023
Number of policy holders who died while receiving benefits	339	123

Source: U.S. Government Accountability Office, 2005.