



November 25, 2009

Honorable Tom Harkin  
Chairman  
Committee on Health, Education,  
Labor, and Pensions  
United States Senate  
Washington, DC 20510

Dear Mr. Chairman:

In response to several questions that CBO has received, this letter provides additional information on the budgetary effects of proposals to establish the Community Living Assistance Services and Supports (CLASS) Program.

H.R. 3962, the Affordable Health Care for America Act, as passed by the House of Representatives, and the Patient Protection and Affordable Care Act proposed by Senator Reid contain very similar proposals regarding a new federal program for long-term care insurance. Both proposals would establish a voluntary program for such insurance, termed the Community Living Assistance Services and Supports program. The key difference between the two proposals is in the population eligible to enroll: H.R. 3962 would allow both active workers and nonworking spouses to enroll, while the Senate proposal would allow only active workers to participate. For both the House and Senate versions of CLASS, the Congressional Budget Office (CBO) estimates that the cash flows under the new program would generate budgetary savings (that is, a reduction in net federal outlays) for the 2010-2019 period and for the 10 years following 2019, followed by budgetary costs (an increase in net federal outlays) in subsequent decades.<sup>1</sup> Because participation in the program would be voluntary, collections of insurance premiums under CLASS would be recorded as offsetting receipts (a credit against direct spending).

On balance, CBO estimates that the version of CLASS specified in H.R. 3962 would reduce deficits by \$102 billion over the 2010-2019 period, while the version contained in the Senate proposal would reduce deficits by \$72 billion over that period. The following discussion provides additional information on CBO's estimates for those proposals, including information on their longer-term effects.

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<sup>1</sup> See Congressional Budget Office, cost estimate for H.R. 3962, the Affordable Health Care for America Act (November 20, 2009); and cost estimate for the Patient Protection and Affordable Care Act (November 18, 2009).

### **Description of the CLASS Proposals**

The Community Living Assistance Services and Supports proposals in H.R. 3962 and under consideration in the Senate would each establish a voluntary federal program for long-term care insurance that would be administered by the Secretary of Health and Human Services (HHS). Under both proposals, individuals could purchase coverage that would provide specified future benefits, with premiums set so that the program would be in actuarial balance over 75 years. (Actuarial balance means that expected insurance premiums plus the interest earned on such premium income would equal or exceed the expected cash payments for future benefits and the administrative costs of operating the program.) Premiums would vary only according to the enrollee's age when he or she enters the program. Once enrolled, an individual's premium would generally remain the same for as long as that individual remained in the program. H.R. 3962 would allow active workers and their nonworking spouses to enroll, while the Senate proposal would allow only active workers to participate.

In general, enrollees would have to pay premiums for five years to be vested in the program (that is, eligible to receive benefits in the event they become functionally disabled). Vested enrollees who need assistance performing at least two or three common daily activities such as dressing, bathing, and eating would receive cash benefits to pay for support services in a community setting. Severely impaired enrollees could apply their benefit toward the cost of residential care in a nursing home facility. The benefit would be at least \$50 per day (indexed for inflation); the Secretary of HHS would set benefit levels based on the extent of enrollees' impairment. CBO assumed that the Secretary would initially establish an average daily benefit of about \$75 (indexed for inflation). That figure includes an average benefit of \$50 per day for impaired enrollees living in the community and larger amounts for enrollees who become institutionalized. Benefit payments made through the CLASS program would not be considered as income in determining an enrollee's eligibility for Medicaid.

Both the House and Senate legislation would provide considerable authority to the Secretary to adjust premiums for both current and future enrollees and to reduce benefits to the daily minimum of \$50 in order to maintain the solvency of the program.

### **Budgetary Effects Over the Next 10 Years**

CBO's estimates of the CLASS provisions in H.R. 3962 and in the Senate proposal differ because of the treatment of nonworking spouses in the two proposals. CBO estimates that the inclusion of nonworking spouses in the House proposal would increase expected future benefit payments (and would increase premiums correspondingly) because nonworking spouses who enroll in the program would be expected to be less healthy, on average, than active workers, and therefore more likely to become functionally impaired in later years and qualify for benefits.

**H.R. 3962.** CBO estimates that under the House-passed version of the CLASS program, the average monthly premium in 2011 would be about \$146 (premiums for new enrollees would increase with inflation in later years). Expected enrollment in the program would reach slightly more than 10 million people by 2019 (or about 4 percent of the adult population). The estimated premiums are calculated to be adequate for the program to remain solvent for 75 years, taking into account the interest income that would be generated on unspent balances in the program’s trust fund. (Because most enrollees would not receive benefits for many years, the fund would accumulate significant balances in the early years of the program.)

Over the 2010-2019 period, CBO estimates that the House-passed version of the CLASS program would reduce federal budget outlays by about \$102 billion (see Table 1). This deficit reduction would occur in part because no benefits would be paid out during the first five years the program was in operation. Premium receipts would total about \$123 billion over the 10-year period, and benefit payments would amount to \$20 billion, CBO estimates. For those 10 years, administrative costs associated with operating the program would be 3 percent of premiums, as specified in the legislation, or about \$4 billion. The program would generate about \$2 billion in savings (over the 2010-2019 period) in the Medicaid program because, once an individual became eligible to collect benefits under both the CLASS and Medicaid programs, a portion of the CLASS benefit would go toward offsetting Medicaid costs. Medicaid would continue to provide the full array of long-term care benefits—to the extent that the individual was eligible—but the CLASS program would defray some costs that Medicaid would have otherwise paid.

**Table 1. Estimated Budgetary Impact of Section 2581 of H.R. 3962, the Affordable Health Care for America Act**

	Outlays in Billions of Dollars, by Fiscal Year											2010-	2010-
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2014	2019	
Premiums	0	-5.3	-9.3	-12.6	-14.4	-16.2	-16.0	-16.2	-16.4	-16.5	-41.7	-123.1	
Benefit Payments	0	0	0	0	0	0	2.3	4.3	6.1	7.3	0	20.0	
Administrative Costs	0	0.2	0.3	0.4	0.4	0.5	0.5	0.5	0.5	0.5	1.3	3.7	
Medicaid Savings	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>-0.3</u>	<u>-0.5</u>	<u>-0.7</u>	<u>-0.8</u>	<u>0</u>	<u>-2.2</u>	
Net Outlays	0	-5.2	-9.0	-12.3	-14.0	-15.8	-13.5	-11.9	-10.4	-9.5	-40.5	-101.6	

**The Senate Proposal.** CBO estimates that under the current Senate proposal for CLASS, the average monthly premium in 2011 would be about \$123 (premiums for new enrollees would increase with inflation in later years), and enrollment in the program would be slightly less than 10 million people by 2019 (or about 3.5 percent of the adult population). The slightly lower enrollment expected under the Senate proposal stems from the exclusion of nonworking spouses (as would be allowed under H.R. 3962). However, a higher percentage of those eligible would be expected to enroll under the Senate proposal because of the lower estimated premium.

Over the 2010-2019 period, CBO estimates that the Senate version of CLASS would reduce federal outlays by about \$72 billion (see Table 2). Premium receipts would total about \$88 billion over the 10-year period, and benefit payments would amount to about \$14 billion, CBO estimates. For that period, administrative costs associated with operating the program would be 3 percent of premiums, as specified in the legislation, or less than \$3 billion. The program would generate almost \$2 billion in savings in the Medicaid program over the next 10 years.

**Table 2. Estimated Budgetary Impact of Section 8001 of the Patient Protection and Affordable Care Act**

	Outlays in Billions of Dollars, by Fiscal Year										2010-2014	2010-2019
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019		
Premiums	0	-3.8	-6.6	-9.0	-10.2	-11.5	-11.4	-11.6	-11.7	-11.8	-29.6	-87.6
Benefit Payments	0	0	0	0	0	0	1.6	3.0	4.3	5.2	0	14.1
Administrative Costs	0	0.1	0.2	0.3	0.3	0.3	0.3	0.3	0.4	0.4	0.9	2.6
Medicaid Savings	0	0	0	0	0	0	-0.2	-0.3	-0.5	-0.6	0	-1.6
Net Outlays	0	-3.7	-6.4	-8.7	-9.9	-11.2	-9.6	-8.6	-7.5	-6.8	-28.7	-72.5

**Effects Beyond the First 10 Years**

Projections of premium receipts and benefit payments beyond the 10-year budget window (2010-2019) are subject to more uncertainty than projections for the first 10 years, and detailed year-by-year projections of those amounts would not be meaningful. Among other factors, a wide range of changes could occur—in people’s health and disability status, in the evolution of private long-term care insurance, and in the delivery of medicine—that are likely to be significant but are very difficult to predict, both under current law and under the House and Senate proposals. As a result, CBO is only able to give a broad assessment of the potential budgetary outcomes in future decades, based on the underlying structure of the long-term care proposals.

CBO estimates that both the House and Senate versions of the CLASS program would reduce the federal budget deficit in the second decade following enactment of the legislation (2020-2029), but by smaller amounts than in the initial decade. By the third decade, the sum of benefit payments and administrative costs would probably exceed premium income and savings to the Medicaid program. Therefore, the programs would add to budget deficits in the third decade—and in succeeding decades—by amounts on the order of tens of billions of dollars for each 10-year period. The House-passed version of CLASS, which would reduce the federal budget deficit in the first 10 years by an estimated \$30 billion more than would the Senate version, would likewise add somewhat more to the deficits in the third decade and beyond than would the Senate proposal. (That is, the greater participation and poorer health status of enrollees under the House version would lead to larger benefit payments in those later years.)

The CLASS program would add to budget deficits in future decades even though the proposals require the Secretary of HHS to set premiums to ensure the program's solvency for 75 years. Because of the extended time horizon involved in long-term care insurance and the build-up of unspent premium receipts, income from interest on accumulated fund balances would play a large role in financing the program's benefits. Typically, enrollees pay premiums for many years before some of them become disabled and qualify for benefits. Private issuers of long-term care insurance finance benefit payments from their reserve of accumulated premium receipts and the income they derive from investing those premiums. Similarly, the Secretary would invest CLASS program premium receipts in federal securities and would incorporate that expected income into calculations of appropriate premiums to charge. However, trust fund income from investments in federal securities would be an intragovernmental transfer within the federal budget. As a result, from a budget scorekeeping perspective, the CLASS program would inevitably add to future deficits (on a cash basis) by more than it reduces deficits in the near term, even though the premiums would be set to ensure solvency of the program.<sup>2</sup>

**Key Caveats.** These estimated effects of the CLASS proposals are subject to considerable uncertainty, for several reasons. The budgetary impact would depend importantly on the number of people who would enroll in the program and the health status of those enrollees later in life. That would depend, in turn, on peoples' perceptions about their need for long-term care insurance and their comparison of the premiums they would have to pay in the CLASS program with the value of the future benefits the program would provide. CBO's estimate of the premiums that would be required to ensure the programs' actuarial soundness over 75 years is based on projections of future trends in the prevalence of disabilities and in the ways that care for people with disabilities will be provided. Though some insight can be obtained from the experience of

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<sup>2</sup> Because premium income in the early years would reduce the amount that the government has to borrow from the public, interest on the public debt would also be reduced during that period, but that type of effect is not included in the estimates used in the Congressional budget process.

private-market insurance, both of those trends are subject to substantial uncertainty. Moreover, under the CLASS proposals, the Secretary of HHS would be given great latitude in administering the program, which adds to the uncertainty about the program's cash flows because benefit and premium levels could be set at different levels than CBO has estimated and could be adjusted over time in a variety of ways.

The CLASS program could be subject to considerable financial risk in the future if it were unable to attract a sufficiently healthy group of enrollees. Relatively healthy enrollees would ensure that the program's premiums and the interest on those premiums would be adequate to pay for future benefits. However, attracting healthy enrollees could be challenging for several reasons. One reason is that the administrative costs of the program are limited to 3 percent of premiums, which might mean that the Secretary would not have sufficient funds to effectively market the program to a large number of people. A relatively small enrollment would increase the risk of adverse selection and could undermine the long-run stability of the program. (On the other hand, by keeping administrative costs to a minimum, the CLASS program might attract relatively healthy enrollees because the resulting premiums could be lower than the premiums that would be charged for many private policies that have substantially higher administrative costs and devote a share of their premiums to profit.)

Another reason why attracting health enrollees could be a challenge is that the CLASS program would have to enroll all eligible people who apply, making it likely that some enrollees would be people who were unable to obtain coverage in the private market because of their poor health status. To avoid insuring people with a higher-than-average probability of eventually receiving benefits, private insurers employ extensive underwriting of policies sold in the individual market (that is, people are charged different premiums depending on their expected future need for care), and market coverage selectively in the employer market.

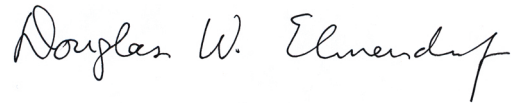
The program includes provisions that would allow employers, at their option, to automatically enroll employees in the CLASS program. That feature could help to boost participation in the program and thereby mitigate the risk of adverse selection. However, the proposals would not require employers to auto-enroll their employees, and employees would have the right to opt out of the coverage altogether, reducing the likely effects of auto-enrollment to stimulate participation in the program.

Honorable Tom Harkin

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I hope you find this information helpful. If you have any questions, please contact me. The CBO staff contacts are Bruce Vavrichek and Stuart Hagen.

Sincerely,

A handwritten signature in black ink that reads "Douglas W. Elmendorf". The signature is written in a cursive, flowing style.

Douglas W. Elmendorf  
Director

cc: Honorable Michael B. Enzi  
Ranking Member

Honorable Harry Reid  
Majority Leader

Honorable Mitch McConnell  
Republican Leader

Honorable Christopher J. Dodd

Identical letter sent to the Honorable George Miller.