February 13, 2024

SUBJECT: ACTUARIAL ANALYSIS ON INITIATIVE-2124 – 2024 SESSION

The Office of the State Actuary (OSA) currently contracts with an outside consultant to provide most actuarial analysis for the Long-Term Services and Supports (LTSS) Trust program, also referred to as the WA Cares Fund. We prepared this Actuarial Fiscal Note (AFN) to summarize and provide context related to this initiative relying on our consultant's (Milliman's) actuarial analysis and other resources.

Background on Current Law Program

The WA Cares Fund is self-funded through a premium rate of 0.58 percent – applied to covered wages of covered wage earners. The benefits provided by the program under current law are defined in the Revised Code of Washington (RCW) 50B.04. Outside of past, one-time, and ongoing limited exemptions provided under current law, the program is mandatory for W-2 workers and provides guaranteed coverage (e.g., near-universal coverage with no underwriting or denials for pre-existing health conditions).

Milliman's *2022 WA Cares Fund Actuarial Study* (Milliman 2022 Study) analyzed the estimated premium rate needed to pay full program benefits and expenses under various scenarios. See the Milliman 2022 Study for a summary of the scenarios tested and a description of benefits assumed to be provided under current law as of October 2022.

For background and summary information on the actuarial status of the WA Cares Fund, see the *Executive Summary of 2022 Actuarial Analysis* on OSA's website.

Per Chapter 50B.04.030 RCW, OSA is responsible for providing recommendations to the LTSS Trust Commission and the Legislature on actions necessary to achieve and maintain trust solvency. We interpret this statutory requirement to include providing such recommendations on proposed changes to the program including this initiative.

Summary of I-2124

This initiative would change the LTSS Trust Program from a near-universal coverage to a fully voluntary program while retaining the guaranteed coverage provided under current law. In this summary that follows below, we only include changes to current law pertinent to our AFN, focusing on the components that could impact actuarial modeling and program fund solvency. See the legislative report for a complete summary of the initiative.

- Requires employees and self-employed persons to elect to keep coverage in the WA Cares Fund program. Additionally, it allows all employees and self-employed persons the option to opt out at any time.
- It repeals the limited, program exemption for individuals who had purchased a private Long-Term Care (LTC) insurance policy prior to November 1, 2021.

Actuarial Analysis

Summary of Actuarial Analysis

- If this initiative is approved, we recommend conducting additional assessments to integrate risk-management best practices from voluntary programs. This would help mitigate potential unintended consequences related to program sustainability or affordability, to the extent possible.
- Changing the WA Cares Fund from near-universal coverage to a fully voluntary program while retaining guaranteed coverage may have unintended consequences on the fund's solvency.
- Those unintended consequences include scenarios where the program may have insufficient assets to pay full program benefits or where premium rates become unaffordable over time.
- If premium rates become unaffordable, the ongoing voluntary nature of the program and who participates could further lead to increased premium rates that could ultimately lead to an unsustainable program.

Background

In the following discussion, we summarize how the initiative may impact fund solvency. Subsequent analysis following enactment of this initiative would be required to quantify the expected impacts. Given the ongoing voluntary nature of this proposal, the ultimate impact of this initiative may take years to materialize.

We anticipate Milliman would publish an updated actuarial study ("updated baseline") in the fall of 2024, which would include any program changes made via legislation since the last study as well as other relevant updates. If this initiative passes, or if other legislation is contingent upon the outcome of this initiative, we would reflect those impacts in a subsequent actuarial report after the outcome of this initiative is known.

Neither the analysis below, nor the initiative, changes the premium rate in statute which is set at 0.58 percent of covered wages.

The analysis of this initiative does not consider any other proposed changes to the WA Cares Fund program. The combined effect of changes to the program from this initiative and other legislative proposals could exceed the sum of each proposed change considered individually.

Analysis of Changes Proposed in I-2124

As noted in the American Academy of Actuaries 2016 Issue Brief, *Essential Criteria for Long-Term Care Financing Reform Proposals*, establishing or revising an existing LTC program requires careful consideration of many issues. One of those issues is the defined coverage of the program. As noted in the Academy's issue brief, the total number of people covered and the attributes of those covered will be affected by whether the program is mandatory (near-universal coverage) or voluntary. According to this issue brief, voluntary programs also require additional risk-management considerations in their program designs that are not typically required under a mandatory program.

This initiative changes the WA Cares Fund from a mandatory to a voluntary program. Under this proposed change, the program would retain guaranteed coverage for those who elect to join but without additional risk-management or cost controls that typically are coordinated with a voluntary program. As noted by Milliman in their attached letter, such a change introduces additional uncertainty in the evaluation of the program's required premium rate, projected fund balance, and solvency.

Two key factors that will drive the impacts of this proposed program design change include (1) participation rate and (2) the level of "adverse selection" that results for those that elect to participate in the program.

> **Note**: Adverse selection in the WA Cares Fund involves the possibility of individuals with greater LTC needs and lower wage levels disproportionately participating in a fully voluntary program, leading to increased per capita program expenditures and higher required premium rates compared to the current law program. See below for further information.

Participation Rate

We do not know who will ultimately elect to remain in the WA Cares Fund if the program were fully voluntary. The demographic makeup (i.e., age, health status, income level) of those that remain may vary from the current makeup and lead to different expected program expenditures and required premium rates than what is permitted under current law.

Adverse Selection

As noted in Milliman's attached letter, individuals with current or future anticipated LTSS needs may be more likely to participate in a fully voluntary program with guaranteed coverage, as they have a greater likelihood of receiving benefits. This outcome, by itself, could lead to adverse selection by health status and increase expected per capita program expenditures relative to the current law program.

In addition to adverse selection by health status, higher wage earners may be less likely to participate in a fully voluntary program because premiums, under current law, are assessed on all wages (with no cap) while program benefits are the same regardless of wage level. This outcome, by itself, could lead to adverse selection by wage level and increase the required premium rate for the program relative to current law.

These two individual factors are typically correlated and could have combined impacts on the program. For example, those with the lowest expected likelihood of receiving LTSS benefits can be correlated with higher wage levels and have the highest likelihood of opting out of a voluntary program. In that scenario, if this cohort leaves the program, the remaining cohort will have higher expected benefits and lower wage levels per capita than under the current law program.

Scenario-Based Analysis

To illustrate the fund's sensitivity to the combination of these sources of potential adverse selection (health status and wage level), we performed scenario-based analysis to determine what minimum level of lost premium revenue, combined with an assumed retained level of short-term expenditures, could lead to program insolvency in Fiscal Year (FY) 2027 (the first year the program provides benefits) if there were no corrective actions taken. We summarize the results of that analysis in the table below.

Percent Retained Premiums*	Percent Retained Short-Term Expenditures	FY of Insolvency
35%	100%	2027
29%	90%	2027
22%	80%	2027
15%	70%	2027
9%	60%	2027

**After June 30, 2024; 100% prior.*

The first year of expected eligible beneficiaries is mostly comprised of individuals currently working who have qualifying LTSS needs under current law. Considering adverse selection based on health status, this group has a higher likelihood of electing to remain in the program because they would immediately qualify for benefits after having already made three years of premium payments by FY 2027. Near retirees (born before January 1, 1968) would also be included in this initial cohort of beneficiaries because they too could become immediately eligible for benefits (partial benefits) after making at least one year of premium payments prior to FY 2027. We would expect the level of retained benefits to decrease each year you move past this initial cohort before approaching an ultimate, retained level.

> **Note**: This scenario-based analysis does not represent best estimate analysis. It is based on data from Exhibit 2 from Milliman's 2022 Study where we modified the expected premium revenue, benefits, and expenses only, and re-calculated the associated expected investment income and fund balance based on the lower assumed premium revenue and program expenditures in each scenario. While this proposal if enacted by the Legislature would take effect on June 6, 2024, actuarial analysis has been performed on a fiscal year basis and therefore is used for these scenarios.

Each scenario noted above is one of many potential scenarios that may emerge in response to the changes proposed in this initiative. Not all scenarios would result in program insolvency in the first year the program provides benefit payments. Some scenarios, with different assumed levels of retained premiums and expenditures, would result in program insolvency later. Other scenarios would not result in short-term program insolvency.

> **Note:** We expect the model used for this scenario-based analysis to become less reliable the longer you extend the modeling period. We did not review long-term scenarios. The actual results of changing the WA Cares Fund to a fully voluntary program would be based on actual program experience, could vary from any given scenario, and may take years to materialize.

Potential Affordability and Sustainability Issues

This initiative provides program participants an ongoing opportunity to leave the currently defined program and retains guaranteed coverage without additional risk-management or cost-control measures. As noted by Milliman, this structure could lead to an "insurance rate [premium rate] spiral" if the cap on the program's premium rate under current law (0.58 percent) were increased. Increasing the required premium rate above 0.58 percent would be one option to attempt to mitigate the potential solvency risks noted above.

In this circumstance, the impacts of participation and adverse selection noted above could compound over time. For example, after the initial cohort opts out of the program, the program's expected obligations and required premium rate would be re-assessed for the remaining covered population. If it leads to a higher required and assessed premium rate, additional individuals may opt out if premiums become unaffordable. After those individuals leave, a subsequent program re-assessment would take place for the remaining covered population at that time. If that leads to a higher required and assessed premium rate, additional individuals may decide to leave the program. The cycle repeats.

If the cycle repeats without intervention, the program could utlimately become financially unsustainable (the inability to collect premiums high enough per person to cover benefit payments). Potential intervention in this circumstance could include modifying the ongoing, voluntary nature of the program, modifying or removing guaranteed coverage, or potentially replealing the program. This does not represent an exhaustive list of potenetial future program modifcaitons, if needed.

Providing program participants an ongoing opportunity to leave the program could also provide an incentive for individuals to leave the program after making ten years of premium payments (if they become permanently vested) or after receiving the lifetime maximum amount of benefits from the program if they continue to work or return to covered employment. Under the current law program, covered individuals are required to make premium payments while they remain in covered employment. This includes individuals permanently vested in the program as well as individuals who receive benefits and continue to work or return to covered employment. The loss of assessed premiums in these circumstances, by itself, would lead to a higher required premium rate for the program.

Recommendation

If this initiative is approved, we recommend conducting additional assessments to integrate risk-management best practices from voluntary programs. This would help mitigate potential unintended consequences related to program sustainability or affordability, to the extent possible.

The undersigned, with actuarial credentials, meet the Qualification Standards of the American Academy of Actuaries to render the recommendations contained herein. We encourage you to submit any questions you have on this actuarial analysis to our e-mail address at state.actuary@leg.wa.gov.

Sincerely,

Matthew M. Smith, FCA, EA, MAAA
State Actuary

Luke Masselink, ASA, EA, MAAA
Senior Actuary

Attachment: Milliman's *WA Cares Fund Program Fully Voluntary Modeling*

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December 21, 2023

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Re: WA Cares Fund Program Fully Voluntary Modeling

Dear Luke:

Per your request, we modeled the potential relative impact to the WA Cares Fund required premium assessment assuming the program was fully voluntary.

The estimates provided in this deliverable are prepared to assist in evaluating the impact of adjusting WA Cares Fund to be fully voluntary. Any estimates around required program revenue are for feasibility purposes only and are not intended, and should not be used, for setting the program premium assessment.

Any reader of this letter should possess a certain level of expertise and background in actuarial projections related to financing long-term services and supports (LTSS) benefits to assist in understanding the significance of the assumptions used and the impact of these assumptions on the illustrated results. The reader should be advised by, among other experts, actuaries or other professionals competent in the area of actuarial projections of the type in this letter, so as to properly interpret the estimates. The information included in this letter should only be considered in its entirety.

BACKGROUND ON MODELING APPROACH

We understand you wish to perform initial, high-level conceptual modeling of a structure where participation in WA Cares Fund becomes fully voluntary while all other program rules remain unchanged. Under this alternative conceptual structure, participation (i.e., payment of the premium assessment) in WA Cares Fund would be completely voluntary, but program coverage would continue to be "guaranteed" as long as an individual met requirements to become a qualified individual (i.e., vested).

For purposes of completing the illustrative modeling in this letter, we performed calculations relative to the 2022 Base Plan included in our 2022 LTSS Trust Actuarial Study[1] dated October 20, 2022 (2022 Actuarial Study). Given program details regarding how WA Cares Fund would be modified to make it fully voluntary are unknown, we performed modeling where we continued to assume individuals will pay into the program over a work history similar to the 2022 Base Plan, but examined different participation scenarios where the average health status or average wage level differs from the 2022 Base Plan. If the program structure using a voluntary design differed from the conceptual design modeled (e.g., where individuals can be eligible for benefits after paying into the program for less than their full work history), the results in this letter would likewise be different.

Evaluation of a program's rates and fund balance can be challenging when individual choice or a voluntary aspect to participation is combined with guaranteed coverage (e.g., no underwriting), since there is unpredictability related to participation rates and adverse selection. In our modeling herein, we analyzed two potential sources of adverse selection if WA Cares Fund were to transition to a voluntary structure:

- **Health status.** Individuals with current or future anticipated LTSS needs may be more likely to participate, as they have a greater likelihood of receiving benefits. Adverse selection by health status would influence the claims risk for the pool of covered individuals, and consequently, program expenditures.

[1] Giese, C. et al. (October 20, 2022). *2022 WA Cares Fund Actuarial Study*. Milliman Report. Retrieved December 20, 2023, from https://leg.wa.gov/osa/additionalservices/Documents/Report01-2022WACaresFundActuarialStudy.pdf

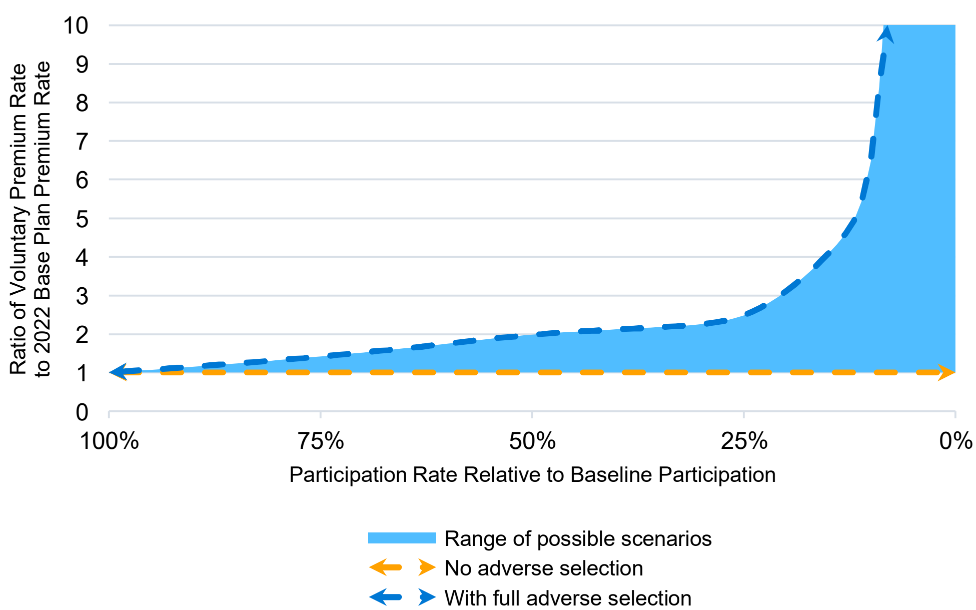
- **Wage level.** Higher wage earners may be less likely to participate because premiums are assessed to wages (with no cap) while program benefits are the same regardless of wage level. Adverse selection by wage level would impact the program revenue collected.

RESULTS

Figure 1 summarizes our modeling of the potential premium rate impact under various participation levels for a voluntary structure with guardrails requiring premium payments through an individual's full work history compared to a baseline with WA Cares Fund's current participation rules. The ratios in Figure 1 are not intended to be bounds, but rather represent a range of results under different levels of modeled adverse selection. **Depending on the participation rate and level of adverse selection, Figure 1 shows the premium rate could be similar or exceed 20 times the 2022 Base Plan estimate. In other words, if WA Cares Fund is structured to have voluntary participation and guaranteed coverage for all individuals, the premium rate will likely need to be raised significantly from current law and the interaction of the premium rate, participation, and adverse selection could lead to an insurance premium rate spiral (as discussed in the Important Considerations section).**

Please note, the results in Figure 1 assume that individuals who elected to participate would still be required to pay premiums throughout their full work history after program start (i.e., there would not be a pathway where they could pay for only 10 years, become vested, and then stop paying premiums, but remain in the program). **If a voluntary structure was created whereby individuals would only need to pay premiums for 10 years instead of over their full work histories, we would expect the required premium assessment could be more than double the premium assessments illustrated in Figure 1 (i.e., premium rates could exceed 40 times the 2022 Base Plan estimate at the lowest participation levels).**

Figure 1: Potential premium rate ratio relative to 2022 Base Plan for a fully voluntary program – individuals pay premiums over full work history



Note: Figure 1 does not provide bounds on the impact to the required premium assessment; rather, it provides a potential range of results based on modeled levels of adverse selection.

As shown in Figure 1, if *little to no adverse selection* were to occur, the required premium assessment rate may be similar to the baseline rate (0.57% in the 2022 Actuarial Study) regardless of participation rate, as represented by the orange line. In other words, the average expected expenditures and average wage base (and associated required premium assessment) are the same for both the groups of participating and non-participating individuals. However, *with full adverse selection*, the required premium assessment may increase exponentially as the participation rate decreases (as represented by the dark blue line).

The light blue shaded area in Figure 1 represents the potential range of required premium assessments, which grows larger as participation decreases. For example, at 75% participation, the required premium assessment with adverse selection is estimated to be potentially up to 1.5x the baseline premium rate (as shown on the y-axis) – meaning the premium rate could be as high as 0.86% (calculated as 1.5 x 0.57% = 0.86%). At 25% participation, the required premium assessment with adverse selection is estimated to be potentially up to 2 to 3 times higher than the baseline premium rate (i.e., the premium rate could be as high as 1.14% to 1.71%, calculated as 2 x 0.57% = 1.14% and 3 x 0.57% = 1.71%), increasing significantly thereafter as participation decreases.

Note, "100% participation" in Figure 1 refers to 100% of the 2022 Baseline participation, which reflects projected opt-outs and exemptions.

IMPORTANT CONSIDERATIONS

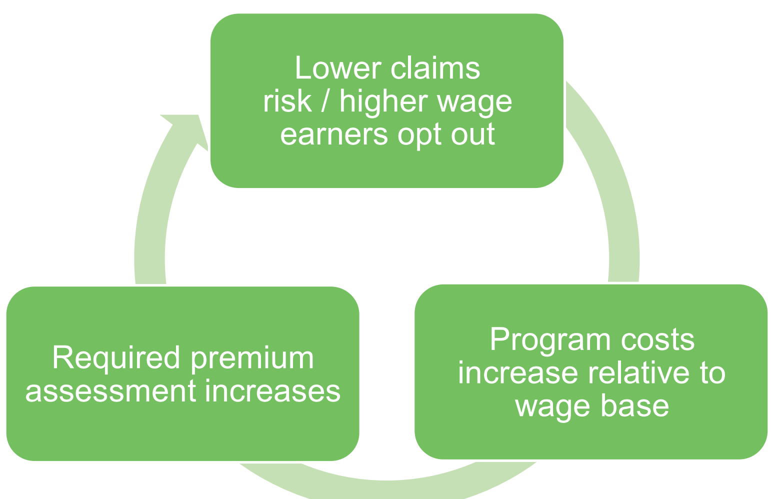
Insurance Rate Spiral

Under a voluntary structure, individuals with lower claims risk or higher wages may choose to not participate in WA Cares Fund as they evaluate their personal circumstances. If this "selection" occurs, the remaining covered individuals in the program would have higher claims risk and / or lower wages, therefore, requiring a higher premium assessment for the program. If a higher premium assessment is used, the remaining individuals would reevaluate their personal circumstances, where the next "layer" of individuals with lower claims risk or higher wages may choose to not participate.

The circular pattern of reduced participation increasing adverse selection (and required premium rates), which in turn can reduce participation starting the pattern over again, is referred to as an insurance rate spiral. An insurance rate spiral is illustrated in Figure 2 below.

Figure 2: Insurance rate spiral

In the case of an extreme rate spiral, a situation could arise where the program could not charge a sufficient rate to cover expenditures. For example, if all individuals remaining in the program are estimated to use full program lifetime benefits and their average wages are very low, the required premium assessment rate could be a large percentage of wages or even exceed wages.



Lessons Learned from Other Proposed Voluntary Programs

Voluntary programs without underwriting or other tools available to mitigate adverse selection may lack actuarial soundness (i.e., the program is more likely to become insolvent). The Community Living Assistance Services and Supports (CLASS) Act, which was introduced as part of the Patient Protection and Affordable Care Act (ACA) before ultimately being repealed, proposed the creation of a guaranteed issue and fully voluntary federal long-term care insurance program. Discussion surrounding the CLASS Act and its ultimate repeal underscores many of the challenges associated with these types of programs.

In particular, the American Academy of Actuaries (AAA) and Society of Actuaries (SOA) chairpersons jointly issued a letter to the U.S. Senate Committee on Health, Education, Labor, and Pensions summarizing critical issues related to the CLASS Act titled Actuarial Issues and Policy Implications of a Federal Long-Term Care Insurance Program.[2] Below we summarize several of the conclusions about the CLASS Act's voluntary design from the AAA and SOA's joint letter.

- A fully voluntary program with no underwriting at enrollment would likely result in significant adverse selection
- The ability to opt in or out at any time with limited guardrails would likely compound adverse selection
- The use of a short waiting period before enrollees can access benefits would likely compound adverse selection
- There would be an additional administrative burden to support education and marketing efforts to promote enrollment

While the structure of the CLASS Act and WA Cares Fund differ in many meaningful ways, the aforementioned cautions from the AAA and SOA are relevant and important to consider, should WA Cares Fund incorporate additional voluntary components in its program design.

METHODOLOGY AND ASSUMPTIONS

The underlying program design for the analysis presented in this letter is consistent with the Base Plan included in our 2022 Actuarial Study. All plan features, methodology, and assumptions are consistent with the modeling of the Base Plan in our 2022 Actuarial Study unless indicated otherwise. The results in this letter should be considered in their entirety in combination with our 2022 Actuarial Study.

To estimate the required premium assessment under various voluntary participation scenarios, we applied claim cost selection factors to different slices of the modeled population based on individuals' wages and morbidity. Selection factors were based on information from the Milliman *Long-Term Care Guidelines* and other industry general population prevalence studies.

For the *no adverse selection* scenario presented in Figure 1 (as shown by the orange line), we assumed the 2022 Base Plan premium assessment of 0.57% (as described in the 2022 Actuarial Study) would hold steady and did not model any additional adverse selection at any participation rate.

For the *with full adverse selection* scenario presented in Figure 1 (as shown by the dark blue line), we assumed the most adverse slice of the population under each participation rate scenario would be enrolled. To provide a specific example, take a 25% participation rate scenario. Under a 25% participation rate, for the high end of our results range, we assumed the individuals with both the 25% lowest wages, as well as the 25% poorest health status would be the only individuals to participate. By doing so, the 2022 Base Plan premium assessment of 0.57% (as described in the 2022 Actuarial Study) is recalibrated using the selection factors to the morbidity and wages for that 25% slice of the population.

[2] https://www.actuary.org/sites/default/files/files/publications/class_july09_0.pdf, accessed November 28, 2023.

CAVEATS AND LIMITATIONS

This information is intended for the internal use of the Washington State Office of the State Actuary (OSA) and Washington State Department of Social and Health Services (DSHS) and it should not be distributed, in whole or in part, to any external party without the prior written permission of Milliman, subject to the following exception:

- This report shall be a public record that shall be subject to disclosure to the State Legislature and its committees, persons participating in legislative reviews and deliberations, and parties making a request pursuant to the Washington Public Records Act

We do not intend this information to benefit any third party even if we permit the distribution of our work product to such third party.

This information provides potential impacts to the required premium assessment for WA Cares Fund assuming the program were to become fully voluntary. Scenarios are created based on variations from the 2022 Base Plan which is described in the 2022 WA Cares Fund Actuarial Study provided on October 20, 2022, which should be read in its entirety with this letter.

Many assumptions were used to construct the estimates in this letter. Actual results will differ from the projections in this letter. Experience should be monitored as it emerges, and corrective actions should be taken when necessary.

Milliman has developed certain models to estimate the values included in this letter. The intent of the models is to estimate required revenue for alternative program features of the WA Cares Fund. We have reviewed the models, including their inputs, calculations, and outputs for consistency, reasonableness, and appropriateness to the intended purpose and in compliance with generally accepted actuarial practice and relevant actuarial standards of practice.

Guidelines issued by the American Academy of Actuaries require actuaries to include their professional qualifications in all actuarial communications. Chris Giese, Annie Gunnlaugsson, and Evan Pollock are members of the American Academy of Actuaries and meet the qualification standards for performing the analyses in this letter.

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Luke, please let us know if you would like to discuss further or have any other questions.

Sincerely,

Christopher J. Giese

Christopher J. Giese, FSA, MAAA
Principal and Consulting Actuary

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