

# WebMemo



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## Secretary Sebelius Cannot Fix CLASS

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Among Obamacare's hundreds of pages was tucked a new government-run long-term care program, the Community Living Assistance Services and Supports (CLASS) Program.<sup>1</sup> CLASS was poorly designed, and actuaries criticized it as being unsustainable well before the passage of Obamacare.<sup>2</sup> It appears from three recent congressional appearances by Health and Human Services (HHS) Secretary Kathleen Sebelius that the Obama Administration has caught up with the actuarial analysis.<sup>3</sup>

While the Secretary now acknowledges that CLASS is fundamentally flawed, she has argued that the law grants her flexibility to make changes that ensure its solvency. However, HHS does not have the legal authority to make significant changes to CLASS. Even if it had the legal authority to make the changes she has suggested, these would not fix the inherent problems in CLASS. According to the Secretary's own statements, CLASS should be repealed since it cannot be fixed.

**CLASS Is Unsustainable.** Section 8002 of Obamacare amends the Public Health Service Act by adding Title XXXII: CLASS. These provisions create a government long-term care (LTC) insurance program administered by HHS. Under Section 3202(6)(B) of CLASS, an individual is eligible for participation in the program if he earns taxable wages in excess of the amount necessary for Social Security coverage (\$1,120 for 2010) for three calendar years of the first 60 months for which the individual paid premiums.

The main problem is that the program's design will result in a badly skewed pool of participants. This is primarily because health status cannot be a factor used for calculating premiums. This means healthy individuals are less likely to participate because they do not receive credit in the form of a lower premium, like they would if they purchased LTC insurance in the private market. Instead, CLASS participants are likely to be disabled individuals who are able to work part-time and individuals who anticipate future LTC needs.

Moreover, the adverse selection problem is exacerbated because individuals earning below the poverty line are subjected to only a \$5 monthly premium, and less healthy people are much more likely to be below the poverty line. The artificially low premium for them means that premiums will have to be much higher for others, which will diminish overall enrollment in the program and worsen its long-run solvency. The poor design of CLASS almost guarantees that the program will collapse or need a bailout.

This view is endorsed by the American Academy of Actuaries: "Given the way the [CLASS] program is structured, severe adverse selection would result

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in very high premiums that are likely to be unaffordable for much of the intended population, threatening the viability of the program.”<sup>4</sup> The Academy also warned that “taxpayer funding and/or benefit reductions may be required.”<sup>5</sup>

More recently, President Obama’s Deficit Commission recommended revamping or repealing CLASS, stating: “The program’s earliest beneficiaries will pay modest premiums for only a few years and receive benefits many times larger, so that sustaining the system over time will require increasing premiums and reducing benefits to the point that the program is neither appealing to potential customers nor able to accomplish its stated function. Absent reform, the program is therefore likely to require large general revenue transfers or else collapse under its own weight.”<sup>6</sup>

**HHS Cannot Fix CLASS.** Secretary Sebelius now understands that CLASS, as enacted, is a prescription for failure. Last month before the Senate Finance Committee she was asked whether she agreed with the Deficit Commission’s recommendation for CLASS. She responded, “I do agree with the reform or repeal (of CLASS), which is why we were pleased to have been given administrative flexibility in the law. While the law outlined a framework for the CLASS Act, we determined pretty quickly that it would not meet the requirement that the Act be self-sustaining and not rely on taxpayer assistance.”

The Secretary broadly outlined three areas she said HHS could target to improve CLASS: automatic enrollment, premium increases, and changes to

eligibility. In fact, however, the Administration does not have much “administrative flexibility” in these areas. Even if it did, the changes Secretary Sebelius has suggested are filled with contradictions and would do nothing to change the fact that the program is unsustainable.

**Automatic Enrollment.** Secretary Sebelius said at the House Ways and Means Committee hearing: “First of all, there is no program that is together yet. There is no automatic enrollment. That is one of the considerations being discussed, but there is no framework yet for the CLASS Program. One of the issues is how to get a take-up rate that is a sustainable program. But there is no mandate for auto-enrollment.”

**Reality.** Section 3204(a)(1) directs the Secretary of HHS along with the Secretary of the Treasury to design a mechanism under which each individual “may be automatically enrolled in the CLASS program by an employer” as well as an alternative mechanism for self-employed individuals or individuals whose employers do not participate. Section 3204(b) indicates that people who are automatically enrolled have the right to opt out. Therefore, although the Secretary suggests there is not a mandate for auto-enrollment, the statute clearly states otherwise.

The Secretary’s testimony implies she is open to removing the automatic enrollment feature. If she could change the automatic enrollment provision, it would result in fewer healthy people enrolling, which undermines her acknowledgement

1. Brian Blase, “No CLASS: How Congress Saddled Taxpayers With Another Costly Entitlement,” Heritage Foundation *Backgrounder* No. 2444, July 29, 2010, at <http://www.heritage.org/Research/Reports/2010/07/No-CLASS-How-Congress-Saddled-Taxpayers-with-Another-Costly-Entitlement>.
2. P. J. Eric Stallard and Steven Schoonveld, “Actuarial Issues and Policy Implications of a Federal Long-Term Care Insurance Program,” American Academy of Actuaries, July 22, 2009, at [http://www.actuary.org/pdf/health/class\\_july09.pdf](http://www.actuary.org/pdf/health/class_july09.pdf) (March 15, 2011).
3. Secretary Sebelius testified three times over the past month: Senate Finance on February 15—exchange with Senator John Thune (R–SD); House Ways and Means on February 16—exchange with Representative Charles Boustany (R–LA); and House Energy and Commerce Health Subcommittee on March 3—exchange with Representative Phil Gingrey (R–GA).
4. Alfred A. Bingham Jr., “Patient Protection and Affordable Care Act (HR 3590) and Affordable Health Care for America Act (HR 3962),” American Academy of Actuaries, January 14, 2010, p. 19, at <http://www.ltccconsultants.com/articles/2010/classactconcern/AAAletterReHealthCareReformJan14.pdf> (March 15, 2011).
5. Stallard and Schoonveld, “Actuarial Issues and Policy Implications of a Federal Long-Term Care Insurance Program,” p. 1.
6. National Commission on Fiscal Responsibility and Reform, *The Moment of Truth*, December 2010, at [http://www.fiscalcommission.gov/sites/fiscalcommission.gov/files/documents/TheMomentofTruth12\\_1\\_2010.pdf](http://www.fiscalcommission.gov/sites/fiscalcommission.gov/files/documents/TheMomentofTruth12_1_2010.pdf) (March 15, 2011).

that CLASS needs strong participation in order to survive.

**Premiums.** In an exchange with Senator John Thune (R–SD) about what changes could make CLASS sustainable, the Secretary stated it is “current part of the plan to index premiums to inflation.”

**Reality.** Section 3203(a)(1)(A) and Section 3203(b)(1)(B) require HHS to set premiums at a level that will ensure the solvency of CLASS, but they also limit the department’s ability to do so. First, monthly premiums cannot exceed \$5 for individuals below the poverty line.<sup>7</sup> Furthermore, the law specifies that individuals who have reached age 65, have paid premiums for enrollment for at least 20 years, or are not actively employed are exempted from any premium increases.

The Secretary is authorized to set the premiums at an appropriate level to avoid program insolvency, but she simply cannot do so. The truth is that no one knows how high the premiums will have to be in order to achieve solvency and many CLASS participants, perhaps the majority of them, will pay only \$5 monthly premiums. The reason is that the CLASS product has not been tried in the private market. A product like CLASS that is reliant on healthy people cross-subsidizing the expenses of unhealthy people would have resulted in huge losses for a private insurer.

**Eligibility.** Before the Senate Finance Committee, Secretary Sebelius stated that she is considering changing the eligibility requirements: raising the minimum annual earnings from \$1,200 to \$12,000

and changing the premium period from three years to five years.

**Reality.** Section 3202(6)(C) allows the Secretary limited flexibility to make exceptions to the eligibility requirements. The statute gives her the authority to change only the minimum earnings requirement to make it less stringent, not more.<sup>8</sup> She is not authorized to change the work period.

The Secretary’s interest in using her authority to make eligibility requirements stronger further exposes the basic problem of CLASS: the underlying eligibility provisions make nearly everyone eligible. This provision, coupled with an inability to charge actuarially fair premiums, makes CLASS unsustainable.

**Repeal CLASS.** Secretary Sebelius has pledged numerous times that CLASS will be sustainable before it proceeds. At the Senate Finance hearing, she remarked that “The program will not start unless we can absolutely be certain that it will be solvent and self-sustaining into the future.” The Secretary does not have enough legal authority to change CLASS. Even if she did, her proposed changes would not fix the central problems.

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7. The \$5 premium will be indexed to growth in the Consumer Price Index. The \$5 limit also applies to individuals age 21 or younger who are both full-time students and working, although the limit only applies when they satisfy all three of those conditions.
  8. A recent memorandum by the Congressional Research Service confirms this. For further information, see Edward C. Liu, “Authority of the Secretary of HHS to Make Exceptions to Minimum Earnings Requirement for Eligibility Under the CLASS Act,” Congressional Research Service, March 15, 2011.