CLASS' UNTOLD STORY: Taxpayers, Employers, and States on the Hook for Flawed Entitlement Program

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INTRODUCTION

The Patient Protection and Affordable Care Act[1] (PPACA), the Obama administration's keystone health care legislation, established a new long-term care insurance entitlement known as the Community Living Assistance Services and Supports (CLASS) Act. Documents uncovered through a bicameral congressional investigation show that well before the law's passage, warning flags were raised within the Department of Health and Human Services (HHS) about the CLASS program's sustainability in the long-term. The documents also describe the extent to which the Administration may shift costs and administrative burdens for the program onto states and employers.

The CLASS Act created an optional, government-backed, long-term care insurance program that would pay a daily or monthly benefit to enrolled subscribers if they become unable to perform activities of daily living, such as dressing, meal preparation, and personal grooming. Because the program requires a five-year vesting period before subscribers can collect any benefits, the Congressional Budget Office (CBO) calculated that in the first 10 years of the program, the CLASS Act would account for $70 billion in deficit reduction. This calculation was based on the premise that during the initial years of the program, it will take in more revenue in premiums than it pays out in benefits, including the first five years of the program in which no benefits are paid at all.

This $70 billion in CBO-scored "savings" was crucial to garnering support for passage of the health care law. CBO did not make public any estimates on what would happen as the population of subscribers to the program age and the CLASS Act requires increasing amounts of money to be paid out in benefits.

It is now widely acknowledged that the alleged savings from the CLASS Act are illusory. The month after PPACA passed, Rick Foster, Chief Actuary of HHS' Centers for Medicare and Medicaid Services (CMS), released a report indicating that the CLASS Act was not fiscally sound.[2] The chief actuary is a non-partisan, high-ranking official in CMS whose estimates are critical in understanding current health care law and proposed changes to the law.

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[1] P.L. 111-148; P.L. 111-152

[2] Foster, Richard. "Estimated Financial Effects of the 'Patient Protection and Affordable Care Act' As Amended." Office of the Actuary, Centers for Medicare and Medicaid Services, April 22, 2010. https://www.cms.gov/ActuarialStudies/Downloads/PPACA_2010-04-22.pdf

Senate Budget Committee Chairman Kent Conrad, a supporter of the PPACA legislation, publicly called the CLASS program "a Ponzi scheme of the first order, the kind of thing Bernie Madoff would be proud of."[3] In testimony before Congress, HHS Secretary Kathleen Sebelius conceded that the CLASS program is "totally unsustainable" in its current form.[4]

But these concessions came long after PPACA had been signed into law. As a result of this investigation, it is now clear that some officials inside HHS warned for months before passage that the CLASS program would be a fiscal disaster. Within HHS the program was repeatedly referred to as "a recipe for disaster" with "terminal problems." As this report will show, the chief actuary stated on numerous occasions that the program was not fiscally sustainable and would result in what he referred to as an "insurance death spiral."

According to emails and other documents obtained pursuant to this investigation, senior leadership of HHS and Democratic staff in the Senate and House reviewed these warnings but did not change the law and did not inform the public of the doubts about the CLASS Act. Instead, the officials continued to claim that the program would be sound, sustainable, and actually produce budget savings that could help pay for other parts of the health care law.

While there has been little public discussion of the costs PPACA imposes on employers and states, this investigation revealed for the first time the extent to which HHS both anticipated these costs and yet tried to impose even more burdens. The documents we have obtained demonstrate that officials at HHS knew that the CLASS Act would saddle employers and states with, at minimum, a heavy administrative burden. The emails also reveal discussions inside HHS about combating low participation in the program by *requiring* employers to participate. HHS anticipated this mandate could be imposed at some future date, and it is possible they will still attempt to impose such a mandate through regulation.

The documents that were produced as part of this investigation were reviewed and analyzed by a working group of Republicans in both houses of Congress. This report is the product of our joint investigatory research and analysis.

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[3] Montgomery, Lori "Proposed Long-Term Insurance Program Raises Questions." Washington Post, October 27, 2009.
http://www.washingtonpost.com/wp-dyn/content/article/2009/10/27/AR2009102701417.html
[4] Roy, Avik. "Sebelius: CLASS Act is 'Totally Unsustainable,' Mandate Possible," Forbes, February, 23, 2011.
http://www.forbes.com/sites/aroy/2011/02/23/sebelius-class-act-is-totally-unsustainable-mandate-possible/

Internal HHS Documents Questioned Fiscal Viability of CLASS

While PPACA established the long-term care program, it left many of the important details about the CLASS Act to be decided by HHS through regulation. HHS is required to issue those regulations by October 1, 2012. Until HHS issues those regulations, the public does not know how much subscribers will have to pay in premiums to enroll in the program, what benefits they will receive if they become disabled, or what level of disability will trigger the benefits.

When balancing premiums collected against benefits paid, internal HHS documents show that regulators have long been concerned about the problem of "adverse selection." If CLASS suffers from adverse selection (also called "antiselection"), a high proportion of people with long-term care needs enroll in the program and initial premiums will need to be very high to cover costs. Those high premiums will encourage healthy people to drop out of the program, causing premiums to rise again for the sicker individuals who remain. This could result in what is called a premium "death spiral" and massive taxpayer losses.

Internal emails from HHS and CMS show a number of officials raised alarm about the sustainability of the CLASS Act program. Between May and September of 2009, the CMS chief actuary repeatedly stated his concerns to CMS leadership. It appears from the documents that he was later cut out of the discussions regarding the CLASS Act. CMS and Democratic staff on the Senate Committee on Health, Education, Labor and Pensions (HELP) instead turned to CBO, which produced more favorable estimates than the chief actuary. But others within HHS continued to question the viability of the CLASS Act.

What follows is a timeline of how these discussions progressed.

May 2009

The Chief Actuary Predicted "Insurance Death Spiral"

The CMS chief actuary first analyzed the adverse selection problem in a May 19, 2009, email. (See Exhibit A.) Commenting on a draft legislative proposal from Senator Kennedy's office, the chief actuary said, "let me offer a few preliminary comments:

> I didn't see any provision for a Federal subsidy of this program; in other words, the intention appears to be that it would be financed solely through participant premiums and interest earnings. Nonsubsidized, voluntary insurance programs generally involve substantial "antiselection" by those who choose to participate. As summarized below, ***this could be a terminal problem for this proposal.***[5]

[5] Bold/italic emphasis throughout this report not necessarily in the original.

> ***The program is intended to be "actuarially sound," but at first glance this goal may be impossible.*** Due to the limited scope of the insurance coverage, the voluntary CLASS plan would probably not attract many participants other than individuals who already meet the criteria to qualify as beneficiaries. While the 5-year "vesting period" would allow the fund to accumulate a modest level of assets, all such assets could be used just to meet benefit payments due in the first few months of the 6th year.
>
> The resulting substantial premium increases required to prevent fund exhaustion would likely reduce the number of participants, and ***a classic "assessment spiral" or "insurance death spiral" would ensue.***
>
> Alternatively, suppose that a significant number of people without any limitations in [activities of daily living] could be persuaded to participate in the program. How many people would be needed to cover the benefit costs for those qualifying as beneficiaries? For the sake of illustration, suppose 10 million people qualify for benefits of $50 per day (annual cost of $182.5 billion). About 234 million people, paying premiums of $65 per month, would be needed to cover this cost (ignoring administrative expenses). The size of the U.S. population aged 20 and over is about 225 million, and about 165 million of these are employed. This rough—but probably not unrealistic—example further calls into question the feasibility of the maximum financing versus the minimum benefits."

The problem identified by chief actuary at the earliest stages of the bill's consideration remained in the legislation through subsequent drafts. The chief actuary's concern was that it would not be possible to attract enough people to the program to maintain it as a self-funding program.

The chief actuary's email does not include the text of the draft language from Senator Kennedy's office, but it appears from the premium and benefit example used that the first draft of the statutory language may have required $50 a day in benefits and/or premiums of $65 per month. The final version of the CLASS Act gives the Secretary of HHS discretion to set the premiums and benefit levels as long as premiums allow the program to be fiscally sound over 75 years and benefits are at least $50 per day.

June - July 2009

The Administration Supported the CLASS Act Based on Budgetary Gimmicks, Not Long-Term Actuarial Analysis

In the summer of 2009, a series of email exchanges between the chief actuary and the CMS Office of Legislative Affairs show that support for the long-term care program was growing within the Obama administration and among Democrats in Congress, while the chief actuary's concerns were becoming more emphatic. Despite these concerns,

supporters of the CLASS Act continued to rely on budgetary gimmicks and flawed modeling.

On June 29th, a staffer in the CMS Office of Legislative Affairs forwarded a news story to the chief actuary that discussed how the CLASS Act allegedly would save money. The email noted, "Bottom line, the CLASS Act was scored by CBO with a savings of $58 billion over 10 years, including a $2.5 billion savings in Medicaid." A follow up email from CMS Legislative Affairs on July 8 said, "the Administration is now officially on record supporting the CLASS Act." (See Exhibit B.)

The chief actuary responded with a critique of two studies that had been offered in support of the insurance program:

> I've finished reviewing the two studies provided by Sen. Kennedy's staff regarding the CLASS proposal. ***I'm sorry to report that I remain very doubtful that this proposal is sustainable at the specified premium and benefit amounts.***
>
> The actuarial study conducted for AARP assumed participation rates based on a portion (40% to 100%) of current rates for 401(k) plans. In practice, I think current experience for participation in employer based long-term care plans would be much more applicable, and such participation is far lower than for 401(k)'s (for fairly obvious reasons). The AARP study emphasized the sensitivity of premium levels to the number of healthy participants. Although the actuaries didn't model a plan with participation in the few-percentage range, I strongly suspect that the resulting premiums would be so large as to further diminish the number of participants and to fail to achieve the critical mass of participants in average health needed to cover the selection and subsidy costs.
>
> All the analysis in the Moran study is based on an assumption that the CLASS program would be mandatory. The results look legitimate for such a program, but they are not applicable to the voluntary plan proposed for CLASS.
>
> I haven't been able to talk to CBO yet regarding their participation assumptions. Unless they have a compelling reason to expect greater-than-[long-term care] levels of participation, however, I can't see how there would be enough workers participating to cover the selection costs for those with existing [activities of daily living] limitations plus the costs for the internal subsidies for students and low-income persons. ***Thirty-six years of actuarial experience lead me to believe that this program would collapse in short order and require significant federal subsidies to continue.*** (See Exhibit B.)

The comments by the chief actuary demonstrate that any reduction in the federal budget deficit identified by CBO would be a function of budgetary time-shifting rather than true savings. While programs like Social Security are often analyzed on a 75-year basis of long-term actuarial solvency, congressional rules require CBO to analyze legislative proposals, like the CLASS Act, over a 10-year budget window.

But the CLASS program likely will not even begin collecting premiums until 2013, and five years of participation are required before subscribers are vested in CLASS, so the program is not likely to begin paying out any benefits until 2018. CLASS was therefore scored as a revenue raiser. Using this budget gimmick, the true costs of the program—the subsequent benefit payments—were essentially ignored, because only a few years of benefit payments were within the official 10-year CBO scoring window of 2010-2019.

CLASS Supporters Relied on Flawed Modeling

The internal documents show that advocates of the CLASS program relied on strikingly unrealistic participation estimates. One study noted above, commissioned by AARP and dated March 3, 2008, assumed nearly 50 million Americans would join the program, a level well above current participation in private long-term care insurance. The second, by the Moran Group, assumed participation would be mandatory for everyone.[6]

As the chief actuary pointed out, those are completely invalid assumptions on which to base estimates of a long-term care insurance program. CBO's own estimate also assumed participation rates that were higher than long-term care insurance currently has, and higher than the chief actuary believed could plausibly be expected. By relying on unrealistic estimates of how many people would participate in the CLASS program, its supporters masked the program's underlying viability problems.

Even with these unrealistic assumptions, the AARP-commissioned analysis also concluded that the program's design flaws "will ultimately lead to … an unsustainable situation with respect to the premiums." (See Exhibit C.) Emails between Obama administration officials and congressional staff show that AARP, which publicly supported PPACA, has refused to release the entire study. (See Exhibit D.)

To further rebut the AARP and Moran studies, the chief actuary also forwarded to CMS Legislative Affairs staff a report by the American Academy of Actuaries and the Society of Actuaries that substantiated his concerns about the long-term viability of the proposed

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[6] The documents provided did not include the study completed by the Moran group despite it being referenced by the chief actuary and a senior democrat staff member for the Senate Health, Education, Labor, and Pensions Committee. The senior democrat staff member referenced the Moran report on October 20, 2009 at the Kaiser Family Foundation event "The Sleeper Issue: Long-term Care and the CLASS Act," page 78.
http://www.kff.org/healthreform/upload/102009_KFF_CLASS_Act_Transcript_Final.pdf

CLASS program. (See Exhibit E.) The American Academy of Actuaries provided their report to the Senate HELP Committee on July 22, 2009. (See Exhibit E.)

August - September 2009

CMS and Senate HELP Democrats Ignored Warnings about Actuarial Soundness and Pressed Forward with CLASS as a New Entitlement

The chief actuary remained concerned about the soundness of the CLASS program throughout the summer of 2009, and he sought to ensure that his concerns were communicated to the senior people working on health care reform inside HHS as well as the chief architects of the program in Senator Kennedy's office. On August 14, 2009, the chief actuary sent another email to the CMS Office of Legislative Affairs in which he said:

> "***As you know, I continue to be convinced that the CLASS proposal is not 'actuarially sound,' despite Sen. Kennedy's staff's good intentions***. I assume you've conveyed these concerns to the staff but, if not, let me know and we can express the concerns in a memo."

The Office of Legislative Affairs responded, "Yes, both Amy and the HHS Office of Health Reform have been in communication with [a senior democrat staff member] of the HELP Committee relaying your concerns about the actuarial soundness of the CLASS Act." (See Exhibit F.)

A few weeks later, on August 24, 2009, the chief actuary again asked CMS to consider the American Academy of Actuaries report questioning the CLASS Act's viability. (See Exhibit B.)

HHS Officials Effectively Silenced the Chief Actuary and Stopped Soliciting His Input

After receiving consistent negative information from the chief actuary about the financial viability of the program, Senator Kennedy's staff moved to cut out the chief critic of the CLASS Act within HHS from providing any further analysis of the bill. On September 10, 2009, the Director of Policy Analysis in the Immediate Office of the Secretary of HHS emailed the Deputy Assistant Secretary for Planning and Evaluation saying, [a senior democrat staff member] "got back to me, and decided she does not think she needs additional work on the actuarial side." (See Exhibit G.)

An email the following week, September 16, reiterated Democrats' position: [a senior democrat staff member] "at HELP has done a lot of work changing the program and per CBO it is now actuarially sound." (See Exhibit H.) There had been a clear shift from relying on the chief actuary's 36 years of experience in favor of the flawed 10-year timeframe of CBO.

Despite the shift, the chief actuary continued to be involved in discussions as late as September 23, 2009, when he attended a meeting with CBO in which the structure and cost of the CLASS Act were discussed. (See Exhibit I.) After this date, there were apparently no other email communications from the chief actuary regarding the CLASS Act. There is no indication in the documents that the drafters of the legislation in Congress or HHS ever again sought the chief actuary's opinion on the program before the law was enacted. However, his questions about the sustainability of the program continued to be raised in published actuarial reports.[7]

CBO Produced Long-Term Analyses of CLASS; Models Have Yet to Be Made Public

At the same time CLASS supporters began to marginalize the warnings from the chief actuary about the long-term viability of the program, Democratic staff on the Senate HELP Committee worked with CBO to come up with an alternative model to analyze CLASS. On September 9, 2009, an HHS official e-mailed that HELP staff "had CBO do lots and lots of runs out to 50 years to ascertain solvency. [The HELP staff member] is going to send to me to forward on." (See Exhibit J.)

Congress relies on CBO to estimate the economic impact of proposed laws and in this role it is vital that CBO's models be completely transparent. The formulas, algorithms and assumptions should be explicitly defined so that Congress and the public can fully understand the basis for their estimates. Yet two years after it was providing analyses to HELP Committee staff, CBO has declined to disclose the models it developed to analyze the CLASS program's long-term solvency. CBO staff now say that they do not have the capacity to analyze the CLASS Act's long-term solvency, despite apparently undertaking that analysis for congressional Democrats before the bill's passage.

On August 15, 2011, HHS did provide an analysis by CBO that congressional staff gave to CMS in September 2009. That analysis is one page of a spreadsheet projecting net premium collections of $59 billion through 2019 – a 10-year budget estimate, not the 50-year solvency estimates referred to by Senate HELP Committee staff. The document does not disclose what participation rates it assumed or how it established the assumed $65 premium rate. (See Exhibit K.)

September – December 2009

HHS' Office of the Assistant Secretary for Planning and Evaluation Began To Question CLASS but Also Was Ignored

[7] Foster, Richard. "Estimated Financial Effects of the 'America's Affordable Health Choices Act of 2009' (H.R. 3962), as passed by the House on November 7, 2009, November 13, 2009. http://www.cms.gov/ActuarialStudies/downloads/HR3962_2009-11-13.pdf
Foster, Richard. "Estimated Financial Effects of the 'Patient Protection and Affordable Care Act' As Amended." Office of the Actuary, Centers for Medicare and Medicaid Services, April 22, 2010. https://www.cms.gov/ActuarialStudies/Downloads/PPACA_2010-04-22.pdf

Despite the chief actuary's email silence after September, others within HHS began to raise red flags about the soundness of the CLASS program. On September 25, 2009, just two days after the CBO meeting with the chief actuary, the Office of the Assistant Secretary for Planning and Evaluation (ASPE) prepared talking points for the CLASS program, including the concern that the program "***is still likely to create severe adverse selection problems***." (See Exhibit L.)

On October 22, 2009, ASPE again questioned the viability of the program. One staffer wrote in an email:

> "You can get a policy through the [Federal Long-Term Care Insurance Program] (albeit underwritten) with a higher benefit, better inflation protection, and lower premium [than CLASS]. I don't see any reason why anyone would opt for CLASS if they could pass the underwriting. And if you couldn't make it through underwriting, you could simply enroll in CLASS to cover some of your current or likely future [long-term care] costs. ***Seems like a recipe for disaster to me…***" (See Exhibit M.)

This staffer also said: "I can't imagine that CLASS would not have high levels of adverse selection given the significantly higher premiums compared to similar policies in the private market." (See Exhibit M.)

HHS Officials' Public and Private Statements on CLASS Solvency Conflict

During this entire time, public statements by HHS officials gave no hint of the internal concerns voiced within the agency. On October 20, 2009, Richard Frank, Deputy Assistant Secretary for Planning and Evaluation at HHS, gave a public speech at a Kaiser Family Foundation event in which he said:

> "We've, in the department, have modeled this extensively, perhaps more extensively than anybody would want to hear about [laughter] and we're entirely persuaded that reasonable premiums, solid participation rates, and financial solvency over the 75-year period can be maintained. So it is, on this basis, that the administration supports it that the bill continues to sort of meet the standards of being able to stand on its own financial feet."[8]

It was around this same time that internal email from Frank's staff indicated the non-public opinion that prospects for the program's solvency looked more like "a recipe for disaster."

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[8]Comments made on October 20, 2009 at Kaiser Family Foundation Event. "The Sleeper Issue: Long-term Care and the CLASS Act." Page 49-50 http://www.kff.org/healthreform/upload/102009_KFF_CLASS_Act_Transcript_Final.pdf. .

Figures from the Social Security Chief Actuary Also Lead to Questions of Anti-Selection Problems within CLASS

HHS staff acknowledged that CLASS premiums would need to be less than $100 for the program to be viable. On November 27, 2009, an ASPE staffer commented, "I suspect that these changes would decrease the premium to well under $100, which seems to be the consensus threshold needed to get decent participation and avoid catastrophic adverse selection." (See Exhibit N.)

But on December 8, ASPE analyzed Social Security Chief Actuary Steve Goss' actuarial report and noted that estimated monthly premiums were approximately $177 per month (if a certain reenrollment loophole were not closed) or $140 per month (if the loophole were closed). They also noted that after five years, premiums could increase to $332.53 per month. The office concluded its analysis by noting that adverse selection was a serious threat to the program's viability. (See Exhibit O.)

HHS Officials Question CLASS, but Their Concerns are not Addressed in the Legislation

On December 1, 2009, ASPE had prepared technical comments on the CLASS Act, in which, even before its analysis of the Social Security data, the Office pointed out:

> "Unlike most private insurance that reimburses policy holders for long-term care expenses, the CLASS benefit is a lifetime cash payment paid daily or weekly once a person meets the eligibility criteria of the program. … ***The end result could be severe adverse selection that would in turn threaten the long-run solvency of the program***." (See Exhibit P.)

The technical comments also included several recommendations from the American Academy of Actuaries to increase the solvency of the program. These included adding a waiting period before benefits kick in; reducing the benefit from lifetime to a fixed number of years; using an established list of activities of daily living to determine the trigger for benefits; and moving from a daily cash benefit to one that makes reimbursements based on services used.

None of those recommendations were adopted in the final language of the bill, and the concerns expressed by ASPE were not addressed or shared with the public.

January 2010

HHS Officials Privately Conceded CLASS May Be Unsustainable, but Failed to Disclose Their Concerns Publicly

In January 2010, HHS staff prepared a list of suggested technical corrections to the CLASS Act that the Department wanted included as the House and Senate reconciled their separate versions of health care reform. However, for both political and procedural

reasons, the House was forced to accept the version of health reform – and the CLASS Act – adopted by the Senate on December 24, 2009, and none of the corrections were made.

Chief among the corrections the Department wanted to make was a so-called "failsafe," which HHS staff described this way:

> In the current bills, the Secretary can alter the premiums in response to threats to financial stability of the CLASS program. However, ***it is possible the authority in the bill to modify premiums will not be sufficient to ensure the program is sustainable***. The failsafe provision gives the Secretary authority to alter earnings and vesting provisions of the CLASS Act to further decrease adverse selection and maintain long-run stability. (See Exhibit Q.)

The documents reveal HHS' concern that the CLASS program as written in the Senate bill – and the version signed into law – would become fiscally unsustainable. Yet at no point between the date of the document – January 4, 2010 – and the day the House voted to pass the Senate health bill – March 21, 2010 – did Secretary Sebelius or any other HHS official publicly air the Department's concerns that the CLASS program as drafted could be unsustainable.

It appears that the significant fiscal concerns surrounding CLASS may have been silenced within the Department for political reasons and the fear that publicly discussing concerns about CLASS' sustainability could have jeopardized the bill's passage in the House.

The technical comments on the January 2010 document raise additional contradictions between HHS' public and private statements. Throughout 2011, Secretary Sebelius and other HHS officials have repeatedly expressed – and have testified before Congress about – their belief that the CLASS Act legislation gives them the authority they need to construct the program in a fiscally sustainable manner.[9] This public assurance stands in marked contrast with the internal corrections document asserting that it is possible the Department's authority "will not be sufficient to ensure the program is sustainable."

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[9] Roy, Avik. "Sebelius: CLASS Act is 'Totally Unsustainable,' Mandate Possible," Forbes, February, 23, 2011
http://www.forbes.com/sites/aroy/2011/02/23/sebelius-class-act-is-totally-unsustainable-mandate-possible/
House Energy & Commerce Committee. Hearing entitled, "The Implementation and Sustainability of the New, Government-Administered Community Living Assistance Services and Supports (CLASS) Program," March 17, 2011.
http://republicans.energycommerce.house.gov/hearings/hearingdetail.aspx?NewsID=8332

CLASS May Leave Employers On the Hook for a Failed Entitlement

Even before PPACA became law, HHS and the law's drafters began to look for ways to pass the costs on to other parties. While it was clear that some of the future projected shortfalls in the program would add to the federal budget deficit and be borne by American taxpayers, other costs would be shifted to employers and the states. The documents show a consistent effort by HHS to impose unfunded mandates on others, so that the cost of some of the questionable decisions made by the law's drafters would not fall on the federal government.

Employer Participation Creates Compliance and Administrative Burdens

To participate in CLASS, subscribers would pay a yet-to-be-determined premium each month that would be deposited into a trust fund established by the Secretary of the Treasury for the purpose of paying cash benefits to eligible claims. Premiums would be collected either through voluntary employer payroll withholding or by a mechanism determined by the Secretary for those who are self-employed, have more than one employer, or have an employer that does not participate in the automatic enrollment process.

The critical mechanics of how an employer would withhold CLASS program premiums from employees' paychecks and then transfer those premiums to the U.S. Treasury could place a significant compliance and administrative burden on employers. The complexity and cost of any new payroll deduction and enrollment process could be substantial, especially for small employers.

Documents show that HHS knew of the program's administrative burden on employers and pressed forward anyway. In the HHS ASPE office's technical comments on the draft CLASS Act legislation from December 1, 2009, the Department acknowledged:

> "The collection of premiums is a fiduciary responsibility that requires employers to accurately collect and transmit premiums to the government. ***Collecting premiums would require a nontrivial change to existing payroll systems and additional responsibilities that employers may be reluctant to take on***." (See Exhibit P.)

HHS warned that employer participation in a voluntary enrollment program was likely to be low because CLASS premiums will be difficult for employers to calculate and "employee interest in CLASS may be minimal." (See Exhibit P.)

What was more, because employers participating in the program would be taking on a fiduciary responsibility, they could be at risk of lawsuits from their workers for calculating premiums incorrectly. Because, as HHS acknowledged, calculating

premiums will be "complex" and difficult to implement, such lawsuits could become commonplace. HHS appears to have understood that the prospect of litigation and significant liability might make employers less likely to want to get involved in the program.

The Forthcoming Regulations on CLASS Could Require Employers, at a Minimum, to Provide Enrollment Information

In December 2009, HHS staff discussed how to use the regulatory process to change the not-yet-passed CLASS Act in a way that would make it even more burdensome for employers. Staff were concerned that low participation by employers would lead to fewer people signing up for the program.

One email chain included a discussion about requiring employers to play a more active part in enrollment by requiring them to issue enrollment forms to employees.

> "A major enrollment issue that needs to be addressed is how to identify the relevant employers/employees (i.e., the self-employed, small employers, and large employers), and determine if statutory requirements are being met. The Department of Labor may be of some assistance." (See Exhibit R.)

Another email from the same month indicates that HHS tried to make last minute changes to a manager's amendment, though the language never made it into the final version of the amendment. The Deputy Assistant Secretary for Planning and Evaluation suggested:

> "Employer requirements: In the current formulation of the bill, employers have complete discretion regarding whether to participate in the CLASS program and auto-enroll employees …. The provision introduced in this amendment maintains the original optional participation in auto-enrollment, but adds a requirement that employers inform their employees about the CLASS program." (See Exhibit S.)

Nothing in the documents suggests that the Obama administration ever conducted an analysis to quantify how much these proposed unfunded mandates would cost employers in time and resources.

The Administration Considers New Mandates on Employers as a "Solution" to Low Participation

The concern inside HHS about potentially low participation by employers led to an even more burdensome suggestion: mandate that employers over a certain size offer enrollment to employees. As HHS explained, "One possible alternative is to ***move to a 'mandated offer' approach where employers over a certain size (e.g., 50 employees) would be required to offer enrollment***." (See Exhibit P.)

Documents show that the idea that the Administration should solve its participation problem by requiring employers to offer enrollment to employees continued to be a major theme of communications regarding implementation of the program. On December 11, 2009, a staffer in ASPE commented:

> "I am writing right now about whether we should integrate employers even more into the process by moving to a 'mandated offer' approach instead of just 'mandated information.' The major problem is that mandating that employers offer information about the program probably will not yield high enough participation; we need to have employers more integrated into the enrollment process and not have them drop off once they simply provide information about the program." (See Exhibit T.)

The recipient of that email responded:

> "***I agree that there is a risk to the entire program if we don't have a sufficiently robust outreach and educational campaign and one that is specifically targeted to employers.*** This employer notification mandate makes me think of Part D, whereby … insurers are required to notify their Medicare eligibles whether their prescription drug coverage is creditable." (See Exhibit T.)

In numerous other emails, HHS staff argued that employers should bear the responsibility to enroll employees. (See Exhibit R.) HHS envisioned this requirement increasing participation in the program, but the documents do not discuss the unfunded mandate that would be imposed on employers. The final version of the CLASS Act is silent on employer requirements, but it is entirely within the HHS Secretary's discretion to impose the obligations on employers when she issues regulations for the program this fall.

Even if the Secretary does not require employer participation in the regulations to be released this fall, the email communications discussing mandatory employer participation and employer fiduciary responsibility foreshadow ways HHS could later modify the CLASS Act in a desperate attempt to make the program solvent.

CLASS Saddles States With Yet Another Mandate

In addition to the burdens placed on employers, the emails indicate that HHS believed many costs of implementation will be shouldered by the states.

HHS Knew CLASS Imposed Heavy Administrative Burdens and Unrealistic Deadlines

States will have a significant administrative role in the implementation of the CLASS program, including responsibility for establishing and helping to administer eligibility determination centers. For example, the CLASS Act requires the Secretary of HHS to establish an Eligibility Assessment System similar to the Social Security Disability Insurance (SSDI) program, to be administered by the states. That system is to be completed by January 1, 2012. The CLASS Act also requires the HHS Secretary to enter into agreements with each state's Protection and Advocacy System, which advocate for people with disabilities, and with other groups and state agencies to provide additional counseling services.

According to several internal emails, HHS and CMS staff noted the unreasonable burdens the legislation would impose on states by requiring implementation of the Act within two years. On April 19, 2010, one email said that requiring states within two years of enactment to "designate or create entities to serve as fiscal agents for CLASS beneficiaries" would "***create significant new burdens on the states.***" (See Exhibit U.)

Another email from even earlier, December 18, 2009, also warned of this problem, stating that a two year deadline for states "to build the direct care workforce capacity for CLASS enrollees" is "***flawed (and perhaps fatally so)***." (See Exhibit V.)

HHS Underestimated Administrative Costs, Leaving States to Bear Costs of Eligibility Determinations

Even if the deadlines can be met, HHS has not released any specific estimates of how much these implementation efforts will cost or how much money the federal government will be able to offer states to help pay for the services versus how much states will have to pay on their own.

It is clear from internal HHS emails that the Department always planned to impose a number of significant administrative burdens on states. The administrative costs are expected to be significant, and HHS officials pointed out several times that cost estimates of the CLASS Act did not allocate enough money to administer the program. CLASS Act estimates only allocated three percent of premiums to run the program, while the American Academy of Actuaries recommended three percent of premiums *plus* five percent of benefits. (See Exhibit P and Exhibit W.)

Rather than address inadequate funding for administrative expenses, the CLASS Act imposes many administrative expenses on already-struggling states. On March 3, 2010,

when asked whether CMS analyzed implementation costs for CLASS, one CMS employee responded:

> "Hate to tell you but I am almost certain that we did not do this. ***I really thin[k] most of the administrative costs would be in doing eligibility determinations and payments split with nursing homes and waivers, however, I think little of it is really ours versus the states***." (See Exhibit X.)

CMS Knew States Would Be Saddled With Costs But Congress Did Not Make Changes during Reconciliation

In the last few weeks before final passage of PPACA, CMS' Office of Legislative Affairs asked staff for edits to the Senate bill that CMS deemed absolutely necessary in order to implement the Act. In a March 4, 2010, exchange, CMS specifically asked for "Not 'nice to have' but 'otherwise it won't work'" fixes. One edit provided by staff read, "require the Secretary to assume responsibility for building workforce infrastructure; otherwise, ***this will impose costs and burdens on states and potentially put CLASS at risk***."

CMS proposed changing the implementation date to January 2015, as "states are not uniformly equipped to perform activities related to designating existing or new entities to ensure the service infrastructure is adequate to meet the needs of beneficiaries, which will likely pose significant and potentially costly administrative challenges, particularly in light of the implementation deadline." (See Exhibit Y.) None of these edits were included in the final version of PPACA.

Administrative Burden Likely to Get Worse Over Time

The SSDI program, on which the CLASS Act administrative structure is modeled, is experiencing significant problems in both fiscal and administrative areas. The aging of the baby boom generation has caused SSDI administrative costs to nearly double since 2000. According to a CBO report, the SSDI program will become insolvent in 2017.[10] In addition, the Social Security Administration anticipates nearly 3.2 million new applicants[11] for disability benefits in FY 2012. Even without those new applicants, SSDI has a huge backlog of appeals cases in which benefits have been denied. In 2007, some appeal cases had been lingering as long as 1,400 days.[12]

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[10] Congressional Budget Office, "CBO's 2011 Long-Term Projections for Social Security: Additional Information," August 2011. http://www.cbo.gov/doc.cfm?index=12375

[11] Social Security Administration. "Annual Performance Play for Fiscal Year 2012," page 21. "http://www.socialsecurity.gov/performance/2012/APP%202012%20508%20PDF.pdf

[12] Astrue, Michael, Commissioner of the Social Security Administration. Statement before the House Committee on Ways and Means, Subcommittee on Social Security and the House Committee on the Judiciary, Subcommittee on the Courts, Commercial and Administrative Law. July 11, 2011. http://www.ssa.gov/legislation/testimony_071111.html

Conditions are so unstable that the Government Accountability Office (GAO) has placed federal disability programs on a High-Risk Watch List since 2003. According to GAO, "the largest disability programs – managed by the Social Security Administration, Department of Veterans Affairs, and Department of Defense – are experiencing growing workloads, creating challenges to making timely and accurate decisions."[13]

As baby boomers start claiming CLASS Act benefits, program administrators can expect to see some of the problems of scale already being experienced by other federal disability programs, including rising administrative costs. However, the statute caps the program's administrative expenses at three percent of premiums, leaving no wiggle room for states to accommodate the increased burden from an aging population. Without sufficient capital and stability from the start, it is likely the CLASS program will eventually join the other programs on GAO's High-Risk Watch List.

The cost of administering the SSDI program state centers in 2011 was $3 billion, a cost borne exclusively by the states.[14] The burdens of CLASS implementation on the states are likely to exceed that amount, because the number of CLASS beneficiaries will be significantly larger than the number of SSDI beneficiaries due to more relaxed eligibility requirements under CLASS. While HHS has not shared estimates on the costs to states to administer the CLASS Act, we feel that $3 billion per year is a conservative estimate, one that excludes additional expected start-up costs. Over the next ten years, states will be forced to bear at least $30 billion dollars for implementation of CLASS. When added on top of the mandates from the Medicaid requirements in PPACA of at least $118 billion, it is clear that states are being forced to pay the bills that Washington refuses to pay.

State Officials and Legislators Have Grave Concerns with the Solvency and Sustainability of the CLASS Act

On August 4, 2011, leaders of a key National Conference of Insurance Legislators (NCOIL) Committee expressed "grave concerns" with the CLASS Act in a letter to the HHS Secretary. The NCOIL letter asserts that the CLASS Act program ***"fails to apply the principles of risk management that are essential to any financially sound insurance program"***. The letter went on to state, ***"The CLASS program risks being under-capitalized on the front end, paying more in benefits than it collects in premiums.*** This will drive rates up and cause adverse selection, as young and healthy consumers will not participate in the market. Also, the plan as currently configured offers little incentive for agents, brokers, and human resources professionals to encourage the enrollment needed to create a broad and stable risk pool."[15]

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[13] Government Accountability Office. Report to Congressional Committees. "High-Risk Series: An Update." February 2011, page 147. http://www.gao.gov/new.items/d11278.pdf

[14] The 2011 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds. Table VI.C5. http://www.ssa.gov/oact/tr/2011/tr2011.pdf

[15] National Conference of Insurance Legislators. Letter to the Honorable Kathleen Sebelius. August 4, 2011. http://www.ncoil.org/Docs/2007430d.pdf

The concerns of state legislators should be strongly heeded by HHS. Not only do states recognize that they will be on the hook for administering of the CLASS program, legislators whose policy expertise is in insurance markets recognize it is destined for failure at the expense of states, businesses, and tax payers.

Table of Hyperlinks to Exhibits

Exhibit	Link
A	http://go.usa.gov/0fc
B	http://go.usa.gov/0fr
C	http://go.usa.gov/0fY
D	http://go.usa.gov/0fg
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