Approved Feb. 28, 1983
Date

MINUTES OF THE HOUSE COMMITTEE ON INSURANCE

The meeting was called to order by Vice-Chairman Dennis Spaniol at
Chairperson

3:30 ~~a.m.~~/p.m. on February 24, 1983 in room 521-S of the Capitol.

All members were present except:
Chairman Rex Hoy and Rep. Blumenthal, who were excused.

Committee staff present:
Wayne Morris, Legislative Research
Gordon Self, Revisor's Office
Mary Sorensen, Committee Secretary

Conferees appearing before the committee:
Robert Eisler, Health Services Director for Prime Health in Kansas City
Rep. Jessie Branson, Sponsor of HB 2411
Jim McSwain, Lawrence, KS, Fire Chief
Casey Jones, for Kansas State Firefighters Association
Rep. Edgar Moore, Sponsor of HB 2189 and HB 2251
Tim McCoy, Columbian Title Company
Tim Underwood, Kansas Association of Realtors
Wm. L. Mitchell, Hutchinson, KS
Eugene Hackler, Attorney, Olathe, KS
John Anderson, Attorney, Olathe, KS
Sylvia Hoagland, Secretary on Aging of the Department of Aging
Stu Entz, Attorney, Topeka, KS
Dick Brock, Kansas Insurance Department

Former Governor John Anderson was welcomed back to the State House as the meeting was called to order.

First to testify was Robert Eisler, Health Services Director for Prime Health in Kansas City, which is a Health Maintenance Organization. He said he did not want to be recorded as being in opposition to HB 2247, but he would like to make some observations about the bill.He did not believe it included a definition of uncovered charges; and he did not feel it dealt with organizations such as his, which operated across state lines, and where there are reserve requirement in both states. Vice Chairman Spaniol announced that former Rep. Griffiths was representing the Family Health Plan of Newton, KS, and had asked for a few minutes on Monday to express concern about the bill.

Dick Brock, of the Kansas Insurance Department, then spoke on HB 2436, which was requested by the Insurance Department, and he explained their reason for the request. He said that for many years a portion of the premium tax collected for fire insurance across the state had been put into a special fund for the benefit of the Fireman's Relief Association, and the insurance department thought that a small portion of those funds could be allocated by the legislature to pay administrative expenses within the insurance department for administering those funds. Casey Jones then spoke for the Firefighters Association, in opposition to HB 2436. He said they felt the money could be better used for relief for firefighters who were injured, and for training programs, than to use it for administrative expenses in the insurance department.

Rep. Branson then spoke for HB 2411, and explained her reasons for introducing the bill. She passed out a memo of explanation, with a proposed amendment to HB 2411 (Attachment 2). Jim McSwain, Fire Chief of the City of Lawrence, KS, then spoke in favor of the bill and the amendment. He gave further explanation of the problem that had arisen in Lawrence, and passed around a letter stating that the City of Lawrence is in support of HB 2411 (Attachment 3). Casey Jones, of the Firefighters Association, then spoke on the bill.

Next to be heard was HB 2189, and Rep. Edgar Moore explained the bill. He, and David Webb as co-sponsor, urged passage of the bill. Tim McCoy, of the Columbian Title Companies of Topeka, spoke in opposition to the bill because it would only apply to companies incorporated in the State of Kansas, not to all title companies licensed and doing business in the State.He said that, as far as he knew, the only two incorporated in the State were his company and one in Wichita, but there were about a dozen other companies licensed and doing business in the State who should be affected by the bill but would not the way it was presently written. Wm. L. Mitchell, of Salina, said that SB 189 covered the same subject, including the objections presented by Mr. McCoy, and it had passed out of the Senate. He thought this committee should look at it, possibly to replace HB 2189. Tim Underwood

Unless specifically noted, the individual remarks recorded herein have not been transcribed verbatim. Individual remarks as reported herein have not been submitted to the individuals appearing before the committee for editing or corrections.

CONTINUATION SHEET

MINUTES OF THE House COMMITTEE ON Insurance,

room 521-S, Statehouse, at 3:30 a.m./p.m. on February 24, 1983.

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spoke for the Kansas Association of Realtors, and said he had testified on the Senate side in favor of SB 189 and their association thought it was a good bill, but might require a little clean-up.

HB 2251 was next for consideration, and Rep. Moore spoke for his bill. Mr. Eugene Hackler, an attorney from Olathe, a consultant in life care contract matters, and past president of the American Association of Homes for Aging, then spoke for the bill. Attachment 4 and Attachment 5 were passed around for the committee. Mr. Hackler gave examples of some of the problems encountered by older people with life care homes in Kansas, and said he thought that many had been furnished misleading information or insufficient information, and were hurt financially if the home had financial problems. Former Governor John Anderson said that he was here on request of Rep. David Miller as he was now, as an attorney, involved in a lawsuit in Johnson County that had a relationship with the problems contemplated by this bill. It concerned Clearview City, which is the housing area of the old Sunflower Ordnance Works. Later three residents of Clearview City--John Yeager, Richard Jones, and Kirk Gardner, spoke very briefly to complain about conditions there. Mr. Anderson suggested the committee members read "Health Care Review" (Attachment 6) furnished by Touche Ross, a CPA firm in Kansas City, as he thought their organization was very knowledgeable about the problems, as they were involved in the John Knox Village case there.

Sylvia Hoagland, Secretary on Aging of the Department of Aging, spoke in favor of the bill. Stu Entz spoke for the Kansas Association of Homes for the Aging, said they had no major opposition to the concept of the bill, but might be opposed to a large reserve requirement. Dick Brock, of the Insurance Department, said the bill provided for administration by the insurance department so he presented several suggestions for changes to the bill.

The meeting adjourned at 4:55 PM.

GUEST LIST

Attachment 1

COMMITTEE: House Insurance

DATE: Feb 24, 1983

NAME	ADDRESS	COMPANY/ORGANIZATION
James A. Todd	2946 So Eliz Wichita KS 67217	Ks State Firefighters Assn
JERRY MARLATT	RR1 EMMETT, KS 66422	KSCFF
Gordon Fry	Rt# Bx 63 A4 Coffeyville Ks	SEK Fire Chiefs assn
RICHARD SINGER	2812 S.E. 31st	TOPEKA FIRE DEPT
Chuck Peterson	RR1 Buhler Ks	Reno County Fire Dept
Audie D Heller	Box 593 Nickerson Ks	Ks St Council Fire Fighters Hutchinson Fire Dept
Jim McSwain	745 VERMONT - LAWRENCE	LAWRENCE FIRE DEPT
Casey Jones	Topeka	Ks St Firefighters Assn
John Hendrix	Hutchinson	Ks State Firefighters Assn.
John Anderson	Olathe, Ks	Attorney
Sylvia Hoagland	Topeka	Dept of Aging
Rep. Edgar Moore	Olathe Ks	
Page 1		

Atch. 1

GUEST LIST

COMMITTEE: House Insurance DATE: Feb 24, 1983

NAME	ADDRESS	COMPANY/ORGANIZATION
[illegible]	Topeka	Kansas Bar Assn
W. L. [illegible]	Hutchinson	KLTH Alliance
W. L. Roach	Topeka	Kansas Ins. Dept.
Gene Hackler	Olathe	—
Stu Entz	KAHA	Topeka
Fran Edson	KAHA	TOPEKA
Vera Sutton	Topeka	KLTA
Michael [illegible]	Topeka	ADA
Robert E. Eisler, Jr.	Overland Park	Prime Health

Page 2

Attachment 2

JESSIE M. BRANSON
REPRESENTATIVE, FORTY-FOURTH DISTRICT
[illegible]
LAWRENCE, KANSAS 66044

STATE OF KANSAS

TOPEKA

HOUSE OF
REPRESENTATIVES

COMMITTEE ASSIGNMENTS
MEMBER: COMMUNICATION, COMPUTERS AND TECHNOLOGY
PENSIONS, INVESTMENTS AND BENEFITS
PUBLIC HEALTH AND WELFARE

TO: Representative Rex Hoy, chairman, and the members of the House Committee on Insurance

FM: Representative Jessie Branson

RE: House Bill 2411

House Bill 2411 would amend K.S.A. 40-1707 to authorize the fireman's relief association to use monies from the fireman's relief fund for the payment of legal expenses necessary to carry out the purposes of the act.

K.S.A. 40-1707, Section 1, spells out the various benefits to be provided when a member of the association dies from injury or disease contracted by reason of the member's duties as a fireman, including death benefits, funeral expenses, etc. It also spells out who the beneficiaries can be.

However, when there are complications in determining who the beneficiaries are to be, for example, there is no provision to allow use of the relief fund to pay necessary legal services.

The amendment proposed would correct this discrepancy.

Atch. 2

<u>Proposed Amendment to House Bill 2411</u>

Be amended:

On page 4, in line 146, by striking all after "(g)"; and by striking all of lines 147 and 148 and inserting in lieu thereof the following:

"If litigation arises upon the question of whether money is being used in accordance with the objects and purposes of this section, the firemen's relief association is authorized to make payment from the fund for the cost of necessary legal expenses related to such litigation."

Attachment 3

City of Lawrence
KANSAS

BUFORD M. WATSON, JR., CITY MANAGER

CITY OFFICES 6 EAST 6th
BOX 708 66044 913-841-7722

CITY COMMISSION

MAYOR

MARCI FRANCISCO

COMMISSIONERS

DONALD BINNS

BARKLEY CLARK

TOM GLEASON

NANCY SHONTZ

February 24, 1983

Fire Department

Chairman Rex B. Hoy
Insurance Committee
House of Representatives
State of Kansas
Topeka, KS 66612

Dear Chairman Hoy:

The City of Lawrence is in support of House Bill Number 2411.

This bill would allow legal and administrative expenses relating to the Fireman's Relief Fund, to be paid by the fund. Payments could only be authorized by the members of the appropriate local association. This bill would allow officers of the association to obtain needed assistance in legal and administrative matters when conditions warrant.

The committee's consideration of this bill is appreciated.

Sincerely,

James A. McSwain
Fire Chief
LAWRENCE FIRE DEPARTMENT
Lawrence, KS 66044

JAMc/af

Atch. 3

Attachment 4

TESTIMONY ON HB-2251
TO HOUSE INSURANCE COMMITTEE
By Kansas Department on Aging
Feb. 24, 1983

Bill Brief:

Provides for protection of citizens who enter into continuing care contracts.

Summary Provisions:

1. Defines continuing care agreements.

2. Requires registration and review by the Insurance Commission.

3. Provides full disclosure to the prospective buyer:

   a. Financial condition
   b. Fees to be charged
   c. Affiliations
   d. Management
   e. Services to be provided
   f. Transfer and termination provisions.

4. Requires an escrow fund to protect contractees' entrance fees during construction.

5. An escrow fund to 1 year's debt service to cushion against sudden change in case of bankruptcy or insolvency.

6. A grandfather clause for existing homes on escrow funds.

7. A 7 day cooling off period.

KDOA supports HB-2251. This bill is designed to provide consumer protection for senior citizens entering Life Care facilities and is developed after model legislation proposed by the American Association of Homes for the Aged. A continuing care home agrees to provide services for a specified period of time, often life, in exchange for a sum of dollars.

The purpose of the bill is to assure older people who enter into continuing care contracts that their investment is protected. The average enrollment fee is estimated by a AAHA representative to be about $25,000.

Atch. 4

Continuing care homes (which are sometimes called life care homes) differ as to the services they offer. When a person enters a continuing care facility, he or she signs a contract that spells out what shelter and services the home will provide for an established time period, usually for the rest of the resident's life. The contract also states the financial and other legal obligations the resident will have to the home for the length of time specified. Most homes offer arrangements whereby residents, upon entering the home, pay a one-time accommodation fee in addition to regular monthly charges.

Existing law provides no safeguards for this investment if the home becomes insolvent. Because the older person may be committing his or her entire assets to the continuing care agreement, safeguards are essential. HB-2251 provides those safeguards:

1. Full disclosure including affiliations, identity and solvency of owners, management, etc.

2. Registration and oversight by the insurance commissioner.

3. A construction escrow account to ensure that an older resident's fees are protected against insolvency during the construction.

4. A one year's debt services in escrow after construction.

5. A 7 day cooling off period allows the potential resident time to reconsider.

The 12 retirement homes in Kansas that now offer continuing care contracts, all members of the Kansas Association of Homes for the Aged, will have their current continuing care agreements grandfathered in and be exempt from escrow account requirements.

This bill is adopted from model legislation from the American Assocation of Homes for the Aged, the national counterpart of KAHA.

KDOA endorses this bill to prevent the very real possibility of serious problems for older people in the future.

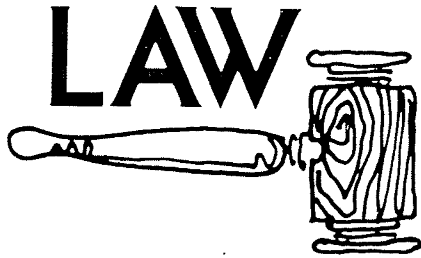
SH:pal
KDOA
2/23/83

FE ARY — MARCH 1976
VOL. II, NO. 4

Attachment 5

concern

/2



Life Care Contracts — Problems?

THOMAS M. JENKINS

Some of the complex legal problems which life care contracts present are summarized in Tom Jenkins' article. Whether or not your facility uses the life care contract arrangement, the article makes significant reading for administrators of non-contract facilities and offers general information about these contracts to all administrators.

A subject of major discussion at the meeting of the Legal Section of the American Association of Homes for the Aging, held in San Diego on November 18, 1975, was "Problems in Life Care Contracts." Former AAHA President Eugene T. Hackler of Olathe, Kansas, the initial speaker, outlined six general areas which are of major interest and concern.

1. Admissions Criteria

This involves at least two subjects -- the physical and the fiscal. Criticism has been leveled that physical admissions criteria are too stringent in many facilities. There are a variety of reasons why different physical standards are necessary.

Thomas M. Jenkins is an attorney and member of the firm of Hanson, Bridgett, Marcus & Jenkins, San Francisco, California. He is a past President of the American Association of Homes for the Aging; former Vice President and a member of the Board of Governors, State Bar of California. He is a charter member of the Society of Hospital Attorneys. Mr. Jenkins is on the Judicial Council, State of California and was recently appointed Judge for the Superior Court, State of California, in and for the County of San Mateo.

Certain states (e.g., California) by law have minimum standards such as the requirement that a person be ambulatory in order to enter into a life care arrangement. Certain facilities do not have the staff, or the buildings and equipment, necessary for particular physical ills. There must be the recognition of the right and duty of our Home to set limitations, recognizing its obligation not to promise to give care for which it is not qualified. This may and does result, for example, in the exclusion at times of persons with severe psychiatric or mental problems. These aged have a need; our field must come to grips with it; in the meantime, we must explain and clarify to others our duty *not* to cause problems for existing or potential residents by admission of those we are not qualified to handle.

In the financial field, prior articles have commented on the criticism leveled at those admissions criteria which require "all assets" to be turned over to the home. This is a practice which has now been changed in large measure, as it becomes more and more apparent this is not only of major disadvantage from both a psychological and a fiscal standpoint to the resident, but also to the home. Pennsylvania has outlawed this type of admissions criteria, and it is anticipated that either by law or by practice it will, in a fairly short time, be essentially discontinued.

Comment is also made at times about "high entrance fees." (See Butler "Why Survive? -- Being Old in America -- 1975"). Again, recognition must be given to the needs of the elderly and to the needs of facilities which propose to serve them. Assurances must be made that funds received from the elderly are spent for them, and that there is a reasonable and rational program for meeting those needs. If an appropriate level of service is set and maintained, then the need for capital, in the absence of government financing and philanthropic contributions, can

utilize the source of the elderly who are able to pay. With ever-increasing costs of construction and replacement, emphasis should be placed not on the "high fees" requested from those who have those resources, but upon the requirement for capital, and the validity of the concept that those who can afford to pay should do so. At the same time, we must assure that there are admissions criteria which also provide for those with lesser financial means, so that we can achieve an ultimate goal of our facilities being neither a ghetto of the poor nor the rich, but a continued cross-section of the society in which we live.

2.Misleading Information on Entrance

Elderly applicants for residence in our various facilities are at a major disadvantage at the time of entrance, and there is an obligation to insure that they are protected, as well as the home. Sometimes through inadvertence, sometimes through lack of knowledge, sometimes through over-promotion, statements are made prior to entrance, by administrators or others engaged in the admissions process, which do not accurately reflect the levels of care, the kind of services to be rendered, or all of the fiscal arrangements. Overstatements and exaggerations are obviously those which create the difficulties.

"...we must assure that there are admissions criteria which also provide for those with lesser financial means, so that we can achieve an ultimate goal of our facilities being neither a ghetto of the poor nor the rich, but a continued cross-section of the society in which we live."

All "promotional" material which is used in the obtaining of new residents should be carefully examined. The administrator should check carefully to assure that, in fact, each of the statements is a true one relating to the services proposed to be given. Any oral presentations made by administrators or others engaged in the admissions process should be gone over in detail. The services to be rendered should be spelled out with specificity, as well as all of the rules and regulations and the extent of medical and other services which will be given. The responsibilities of both the resident and the home, and the position of relatives of the resident should be discussed. "Pie in the sky" does not belong in the field of life care contracts — the more accurate and misleading the information given at the time of entrance, the more frequent will be the challenges in a court of law.

"Sometimes through inadvertence, sometimes through lack of knowledge, sometimes through over-promotion, statements are made prior to entrance, by administrators or others engaged in the admissions process, which do not accurately reflect the levels of care, the kind of services to be rendered, or all of the fiscal arrangements."

3. **Financial Management**

Allegations are now being raised throughout the country about mismanagement of homes by administrators and boards of directors. There are claims of misuse as to funds, and inadequate and improper accounting. Requests are being made for examination of financial information; concern is being expressed about whether or not the facilities are adequate in monitoring the use of their fees and making information available as requested.

Most states have no regulation relating to the requirements of an audit. In some, such as California, audits are required and a flow of financial information to the State Department of Health is a continuing prerequisite to license to operate. In the light of recent decisions relating to the responsibility of directors of nonprofit corporations, as well again as our own recognition of our duties to the elderly, all facilities should require management to present a regular budget, should examine into the expenditure of funds to insure that they are properly spent, and should require that there be an annual audit by an independent, outside accounting firm.

Such audit is not only for the protection of the elderly, but will also assist the facilities to insure that they maintain an adequate source of income to meet increasing costs, particularly in these inflationary times. Adjustments of fees and charges to meet accruing costs is a responsibility which must be maintained.

4. **Inadequate Reserves**

Only a relatively few jurisdictions have any requirements relating to the reserves which must be maintained by homes for the aging. Most homes have either no reserves or else very limited reserves for taxes, maintenance, interest or mortgage payments. Yet in our life care arrangement, we have agreed to give such care for the balance of the life of the resident. This is a serious problem and must be addressed by our boards of directors. Most of our facilities are "church sponsored." This sponsorship, however, is generally not fiscal in nature but is philosophical and religious. To date, we have been fortunate throughout the United States. There are very few instances in which promises of life care have not been met, and parent church bodies have been cognizant of their responsibilities. We must, however, insure that there be more careful monitoring of assets by boards of directors and trustees, a closer relationship with the parent denominational body, and the setting up of reserves to the extent possible to insure that the elderly resident on a life care arrangement is, in fact, taken care of for the rest of his or her life.

5. **Increase in Life Care Fees.**

As our facilities have moved away from the concept of assignment of all assets or one lump sum payment, most life care arrangements now provide for an entrance fee plus another fee on a monthly basis to meet the cost of "continuing care." Many contracts which have been written over the past fifteen years, while recognizing the need for these "continuing care fees," have placed unrealistic prohibitions on the amount of such an increase. In many circumstances, increases were limited to 5% per year, with maximum limitation of 25% for the life of the contract. Other contracts permitted no increase in the monthly care fees. Over the past several years, our facilities have been faced with extraordinary increases in costs, both by reason of inflation and in many instances by the changes in the labor market and unionization. Some states, such as California, seek to maintain that kind of prohibition on increases.

This is not only unrealistic, but can cause severe damage to our facilities. It fails to recognize that there are increases in the fiscal resources of those of even very limited means. Increases in social security, the increase in private pension plans, cost of living increases in retirement benefits, all provide sources of income which should be utilized by the elderly for their own care. It is inappropriate to suggest that increased costs by our homes must be met by some other source, which in fact is not available as governmental programs continue to be curtailed. It is also unfair to suggest that newly admitted residents be brought in at a higher level of monthly fee while those who have earlier entered into a contract continue to enjoy the same benefits, and keep their resources for their own or other uses. It is strongly recommended that residents recognize that cost increases will be required, that they be related directly to increased operational costs, and that that be an element of any life care contractual arrangement. This should be coupled with a provision in every instance that the resident will be taken care of, if his or her own financial position is such that he or she cannot meet ultimate increases. Neither the resident nor the home is served by an unrealistic limitation in the monthly care payment.

6. **Termination of Rights**

An area of increasing legal concern is the matter of termination of contracts. These include two areas: (a) the rights of a resident who desires to terminate and change his relationship with the home, and (b) rights upon death. Again, these are matters which should be carefully worked out by each facility. Adequate provision should be made in each instance for the type of refund, if any, and a careful explanation be given to the resident at time of entrance. Although there is disagreement in the field, strong support can be given to refund provisions which are different in the case of withdrawal and those involving death. In the former situation, the resident makes a voluntary determination that he needs other services or a different mode of living, and should be assisted by our homes in accomplishing that. In the case of death, if there is a prior clear recognition that the obligation of the home would continue whether that person lives only a short

"It is strongly recommended that residents recognize that cost increases will be required, that they be related directly to increased operational costs, and that that be an element of any life care contractual arrangement."

time or far exceeds his life expectancy, then refunds to the estate or relatives can be severely limited or curtailed, and those funds used for the continued support of those without adequate resources.

The foregoing are six major problem areas which Mr. Hackler addressed, and which other attorneys commented on, during the AAHA Legal Section meeting in San Diego. One other significant discussion ensued with reference to life care contracts.

Trust Principle

This relates to the trust theory under which life care payments are received. There is an acknowledgement of a requirement that persons who make payments on a life care contract have the right to receive the services enumerated in that contract. Some would suggest that all funds received from a resident must be spent only for the care of that resident. It is the author's firm belief that this is a negation of many of the principles under which our homes can and must operate. Our residents are a part of the total community in which they live. We are not "islands unto ourselves" and there would in many instances, be little justification for our continued existence, and for the continued work and efforts of many thousands of unpaid volunteers on our boards of directors, if these funds received from each resident were spent only for that resident. There would be little justification for our tax exemption, as pointed out in the *Oregon Methodist Homes vs. Horn* case, where the court there denied such exemption upon the theory that a group of people had simply gotten together, paid a founder's fee, and built a residence essentially for themselves. This obviously could not be considered a "charitable organization" under these circumstances. Ultimately any trust principle which assumes that the fees of a resident can be spent only for a resident, will run afoul of that charitable exemption requirement. Residents in our facilities are a part of a "community" and care must be taken to explain to each upon entrance and prior to execution of their life care contracts, that they will be taken care of, but that their funds will be used with those of others to meet the needs of the elderly which the Home proposes to serve, both inside and outside the physical facility. It should be noted that this concept has been recognized by the Supreme Court of Texas (November 12, 1975) is affirming the appellate court decision in *Evangelical Lutheran Good Samaritan Society vs. City of McAllen, Texas* (Tex. Civ. App. 13th Dist. Jan. 1975). This is an emerging doctrine and one which will be fully explored by AAHA attorneys.

In our next article, specific suggestions will be made as to detailed language in proposed life care contracts to meet the issues addressed by Mr. Hackler and others.

Attachment 6

TOUCHE ROSS/WINTER 1981

HEALTH CARE REVIEW

Life Care—A New Component in the Health Care Delivery System

by J. Emerson Hartzler

Many health care institutions are looking to Life Care to expand the scope of their traditional acute care services. But what is Life Care? How does it operate? What are its advantages and disadvantages?

In our society, the elderly face the future with increasing concern for their health, safety and security. For persons living alone in neighborhoods with changing population demographics, Life Care communities have rapidly developed as an attractive alternative. For those able to afford it, the choice may not be difficult since these communities offer a secure retirement setting, a busy calendar of social events, and a wide range of health care services, from emergency medical attention to permanent skilled nursing home care.

The concept of Life Care is a growing part of the health care delivery system, and may offer a unique opportunity for current health care providers to expand their traditional mission. Thus, health care professionals should be aware of the Life Care concept and its place in the overall system of providing care to our senior citizens.

Concept of Life Care

The basic concept of Life Care, or Continuing Care as it is often called, is the combining of residential retirement living with the availability of health care services. Life Care communities provide for an active social life in pleasant, secure surroundings with access to physician and nursing services. This includes admission to an on-site nursing facility or acute care hospital, should the resident become unable to care for himself.

How Life Care Operates

A Life Care community offers to prospective residents an occupancy agreement, which is similar to a long-term (lifetime) rental contract, with prepayment of a portion of the rent. After an initial payment or entrance fee, the resident is granted the privilege of living in an apartment or a single-family dwelling for the remainder of his or her lifetime, or until he is unable to care for himself. In the latter circumstance, he is entitled to admission to the community's nursing facility.

In addition to the entrance fee, a community charges a monthly service fee to cover the ongoing costs of operations, such as security, maintenance, utilities and transportation. The fee may vary according to the

Atch. 6

Because of the rates charged—entrance fees range from $10,000 to $100,000 or more and monthly service fees range from $300 to $1,000 of more—Life Care communities attract individuals in the higher income brackets.

number of individuals living in each apartment or home and the size and cost of the living unit. Most occupancy agreements allow for periodic increases in the service fees to cover inflationary cost increases. Should the resident be moved to a nursing facility, the service fees may increase to offset the higher cost of providing this care. Because of the rates charged—entrance fees range from $10,000 to $100,000 or more and monthly service fees range from $300 to $1,000 or more—Life Care communities attract individuals in the higher income brackets. However, in the event that a resident's resources are depleted over a lengthy period of residence, provisions for charity may be made.

Reasons for Success

Why are people willing to pay large sums of money for Life Care? The major hypotheses suggested by industry experts are:

- Longer life expectancy.
- Physical security.
- Social activity.
- Access to health care.

Longer Life Expectancy

While longer life expectancy is postulated as one reason Life Care communities enjoy a high degree of popularity, the industry is too new and fragmented to have developed actuarially sound life expectancy statistics. Yet, it is interesting to note that many communities planned for a mortality rate much higher than actually experienced. For example, in a ten-year-old community with a resident population of 2,600, the mortality rate over the past several years has been 5 to 6 percent: much less than anticipated. Ironically, a low mortality rate may cause the community financial difficulty, because a significant amount of income is generated through the resale of the living unit contracts of residents who die.

In attempting to predict life expectancy of Life Care residents, some actuaries are using mortality tables for select groups, such as persons who choose to purchase single payment annuities, and adding 2-3 years of life expectancy. Whether Life Care communities actually add years to one's life or merely attract the type of people with longer life expectancy could be argued; however, the advantages of physical security, social activity and health care should at least make life more pleasant.

Physical Security

Physical security is a major concern of the elderly and those near the age of retirement, many of whom live alone in single-family dwellings they purchased years previously. For some, homes are located in changing neighborhoods where once-peaceful suburban settings now present safety and security problems.

To these people, Life Care communities offer the security they seek in a number of areas. Residents live in a restricted facility or neighborhood with a private security force for protection, and emergency call buttons in their apartments so that on-site medical assistance can be summoned immediately in case of emergency.

Social Activity

The gradual loss of business and social contacts can cause feelings of isolation and loneliness for the individual of retirement age. The lack of social activity among the elderly can be a major cause of their health care problems.

In contrast, living among persons of similar circumstances creates a bond among Life Care community residents. Further, Life Care communities place a strong emphasis on social activities. These activities—clubs and recreational facilities of various types, classes and individual instruction in arts and crafts, and other events—are designed to promote good health among the residents and to prolong the time during which they are able to remain in an independent living setting.

Access to Health Care

Possibly the most traumatic experience an elderly person can undergo is a sudden change from independent living to dependent living in a nursing home, cut off from friends and family. Often, this is the only choice many of our elderly have. In contrast, Life Care communities provide a continuum of health care so that the individual retains all of the characteristics of independent living that his circumstances will allow. If skilled nursing care is eventually required, the resident can remain in personal contact with friends and neighbors who continue to live in close proximity. Feelings of loneliness and despair that can accompany the move to a nursing home are mitigated by the

The Life Care industry has been marked by a number of business failures, the most notable being Pacific Homes . . . the major reasons for this: insufficient capital resources, inflation, and unsophisticated management.

Life Care community's close-knit social environment.

Why Life Care Communities Fail

The Life Care industry has been marked by a number of business failures, the most notable being Pacific Homes, a large operation with facilities in California and Hawaii. There are several major reasons for these business failures:

- Insufficient capital resources.
- Inflation.
- Unsophisticated management.

Insufficient Capital Resources

Most Life Care communities are financed through initial entrance fees paid by first generation residents, and long-term debt in the form of a conventional mortgage loan or tax-exempt bonds. After the initial start-up, the only significant sources of revenue the communities have are the monthly fees paid by first generation residents.

Theoretically, the majority of communities are set up so that their monthly fees pay ongoing operating costs; the long-term debt is serviced by the entrance fees collected from future generations of residents or funds set aside from the entrance fees paid by the first generation of residents. However, the theory fails in actual practice because of a variety of reasons:

- **Extended longevity.** First generation residents are living longer than the actuarial life expectancy tables predicted. Consequently, second generation residents are unable to move into the communities. This means that revenues from second generation residents are delayed. Unfortunately, compensating delays in expenditures are often not possible.
- **Marketing attracts more couples than anticipated.** Life expectancy projections are complicated and extended when two lives are involved instead of one. If more living units are occupied by couples than planned, the second generation of residents may enter at a later date than expected.
- **Residents may become unable to pay.** An extended life span, especially if nursing or health care costs are significant, may result in a resident being unable to continue paying the fee. In such circumstances, the community may have to continue to provide services to the resident without receiving commensurate payment.
- **Inflation and interest rate changes.** A financial plan involving reserves against future costs must include assumptions about inflation and interest rates. When interest rates decline, reserves earn less than anticipated. If inflation is less than expected, fees paid by second and subsequent generation occupants may fall short of forecast amounts. If inflation is greater than expected, residents may have increased difficulty in paying the inflated monthly service fees.

Most facilities charge each resident a substantial entrance fee which, when aggregated, can generate a staggering amount of cash flow. However, the potential liability of caring for residents throughout their lifetime is also staggering, and many Life Care communities have not established even a fraction of the reserves necessary to sustain them through unexpected difficulties. Facility managers have difficulty justifying increases in monthly service fees to cover inflationary costs while maintaining millions of dollars in reserves. However, an imprudent facility manager who uses up his reserves often faces tremendous financial difficulty when the depleted reserves are needed.

Then, too, Life Care communities generally have been not-for-profit organizations without an extensive source of "equity" capital. Many have been sponsored by church-related or other organizations that have financial problems of their own. Consequently, when financial difficulties occur, there may be literally no place to turn for additional resources.

Inflation

Until recently, few people thought in terms of prime interest rates in excess of 20 percent, or predicted double-digit inflation. However, both are factors of the current economic situation faced by Life Care communities. Of the two, inflation seems to have been especially unkind to facility managers. Health care,

What is needed now is for professionals to . . . invest the time and effort to become knowledgeable in the Life Care industry, and lend their management talents to make retirement living as satisfying and carefree as it should be.

utilities (energy), and real estate represent major cost components of a community's operations. They also have been leading factors in higher inflation rates. Many communities that had anticipated a long and prosperous future when inflation was at 6 percent, have become financial disasters with recurring 12 percent annual inflation rates. To a retirement population living on "fixed incomes," these events have been extremely traumatic.

Unsophisticated Management

An irony of the Life Care industry is that many of the communities having financial difficulty are also delightful communities in which to live. While a manager may be extremely competent in developing the facilities and programs for enjoyable retirement living, he may be totally unprepared to cope with the financial aspects of the business over an extended period of time. Fortunately, the trial and error experiences of Life Care managers as they discover what will and what will not work, are helping to develop the financial management principles that can guide the industry into a more prosperous future.

At the same time, a great deal of basic data is not available. How long can this special segment of the population be expected to live? How many days of skilled nursing care will be needed by each resident in his lifetime, and what will that care cost? What prices will people be willing to pay for entrance into a community, and will that "market price" be sufficient to build the facilities, establish adequate reserves, and retire the debt? What is an "adequate reserve"? Answers to these kinds of questions are critical to the financial management of Life Care communities.

Implications for the Industry

Health care institutions striving to expand the scope of their traditional acute care services may find Life Care an attractive opportunity. These communities serve a segment of the population that has the highest incidence of health care needs. It is also a segment whose percentage of the total U.S. population will increase in the coming years. The traditional health care provider has at least three alternative approaches to involvement in Life Care:

- Expand operations to include Life Care, either by developing a facility or purchasing an existing facility.
- Develop the expertise to manage such a facility and procure management contracts in much the same manner as is now done in the acute care hospital field.
- Develop formal relationships with existing Life Care facilities for outpatient services and inpatient referral.

The last point is an attractive strategy for an acute care provider operating within the same community as the Life Care facility. The first two represent a commitment on a much higher level, but they offer an excellent opportunity to develop the management expertise, especially in the financial area, that the industry needs. Experienced hospital financial managers who deal with matters such as cost reporting, third-party reimbursement, capital formation, and tax-exempt financing should be well equipped to understand the financial concepts of the Life Care industry.

Further, many of the management companies currently involved in the Life Care industry have concentrated on designing and building facilities and attracting the first generation of residents. These activities can be professionally and financially exciting and rewarding for the management company. So much so, that these companies may be more interested in developing new communities than continuing to manage mature facilities. The result is a tremendous need for ongoing management services to established communities.

This need might best be met by health care professionals who already serve the same population in numerous other ways. What is needed now is for professionals to step forward, invest the time and effort to become knowledgeable in the Life Care industry, and lend their management talents to make retirement living as satisfying and carefree as it should be.

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Health Care Review, an information service to the clients of Touche Ross & Co.

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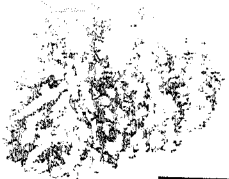

The CEDARS

William W. Hobbs
Administrator

1111 EAST KANSAS / McPHERSON, KANSAS / 67460
A Church of the Brethren Home, Inc.

February 18, 1983

The Honorable Rex Hoy, Chairman
House Insurance Committee
Room 280 West
Capital Building
Topeka, Kansas 66612

Dear Representative Hoy:

I will be unable to be present at the public hearing on H.B. 2251 on Thursday, February 24, 1983. I would like to make a statement against the enactment of this bill.

The Cedars, A Church of the Brethren Home, Incorporated, in McPherson is incorporated as a not-for-profit corporation for the purpose of providing health services to the aging. Care is provided at less than cost. Calculations are that the resident pays about 85% of the cost of his care, the other 15% being paid for by gift money. When the buildings were built funds were raised to pay for them. There are many friends of The Cedars, churches and individuals, who give regularly to The Cedars to help balance the budget.

The Cedars has had an entry fee for many years. A part of the rationale for this charge, ranging from $250 to $3000.00, now $500.00 was that The Cedars' buildings were built with gift money, therefore, the rates did not reflect the cost of the buildings but that notwithstanding, buildings needed repairs which cost money and the entrance fee was a token payment toward those repair costs.

Also, The Cedars has a waiting list containing the names of more than seventy persons who have a varying degree of desire to be in The Cedars. Each one of these persons has paid $250 of the $500 entrance fee. No week goes by without calls from many persons seeking a place in The Cedars. If there was not a way of seeking the level of desire of the person to be in The Cedars, the list would contain several hundred names and this would be unmanageable.

To summarize, the entrance fee at The Cedars serves to identify the applicant who is truly serious about becoming a resident and the fee becomes a part of the other gift money that bridges the gap between costs and what the resident pays for his care.

The Cedars favors defeat of H.B. 2251.

Sincerely yours,

Bill

William W. Hobbs,
Administrator

WWH:mr

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