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OLDER AMERICANS

Continuing Care Retirement Communities Can Provide Benefits, but Not Without Some Risk

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Mr. Chairman and Members of the Committee:

I am pleased to be here today to discuss continuing care retirement communities (CCRC), the risks they and their residents face, and their regulation. A growing population of older Americans is seeking options for ensuring that their assets and income in retirement will cover the cost of their housing and health care needs. One option for meeting these long-term care needs is to enter a CCRC, which aims to provide lifelong housing, household assistance, and nursing care in exchange for a sometimes sizable entrance fee and ongoing monthly fees. These communities may appeal to older Americans because they offer an independent lifestyle for as long as possible but also provide the reassurance that, as residents age or become sick or frail, they will receive the care they need within the same community. But choosing to enter a CCRC can be a difficult decision and is not without risk. Moving to a CCRC generally involves a significant financial and emotional investment. Many older Americans sell their homes, which are often their primary assets, to pay the required fees, and, as a result, their ability to support themselves in the long run is inextricably tied to the long-term viability of their CCRC. Further, many CCRCs may be financially vulnerable during periods of economic decline—such as the recent downturn—that can result in tight real estate and credit markets.

My testimony is based on our June 2010 report, which is being publicly released today and addresses four issues: (1) how CCRCs operate and what financial risks are associated with their operation and establishment, (2) how state laws address these risks and what is known about how adequately they protect CCRCs' financial condition, (3) risks that CCRC residents face, and (4) how state laws address these risks and what is known about their adequacy.[1]

To address these questions, we reviewed CCRC statutory provisions from eight states—California, Florida, Illinois, Ohio, New York, Pennsylvania, Texas, and Wisconsin—and interviewed regulators from those states. We selected these states based on a number of criteria, including extent of regulatory requirements, size of CCRC population, and geographic location. We also reviewed summary information found in an industry

[1]GAO, *Older Americans: Continuing Care Retirement Communities Can Provide Benefits, but Not Without Some Risk*, GAO-10-611 (Washington, D.C.: June 21, 2010).

study on laws and regulations across all states.[2] In addition, we also we interviewed officials from eight CCRCs and obtained relevant documentation to understand their specific experiences developing and operating CCRC facilities. Finally, we interviewed national industry associations, actuaries specializing in CCRCs, attorneys specializing in senior issues, CCRC providers, national and state residents' associations, and officials involved with CCRC finance and debt ratings. A full description of our scope and methodology is included in appendix I of our report.

We conducted this performance audit from June 2009 to July 2010 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Mr. Chairman, the following summarizes our findings on each of the four issue areas discussed in our report:

- CCRCs can benefit older Americans by allowing them to move among and through independent living, assisted living, and skilled nursing care in one community. They offer a range of contract types and fees that are designed to provide long-term care and transfer different degrees of the risk of future cost increases from the resident to the CCRC. However, developing CCRCs can be a lengthy, complex process and CCRCs, like other businesses, face a number of risks both during their development and after they become operational. First, actual construction costs and consumer demand may not match developers' forecasts. To attract financing from lenders and ensure adequate underwriting for CCRC projects, developers need to generate sufficient presales and deposits prior to construction to show a tangible commitment from prospective residents. In addition, facilities in the start-up stage need to reach full occupancy as quickly as possible in order to generate income that will not only cover operational costs once built but also help pay down construction loans. As a result, accurate projections of future revenues and costs are important as a CCRC becomes operational. Once operational, risks to long-term viability include

[2]American Association of Homes and Services for the Aging (AAHSA) and American Seniors Housing Association (ASHA), *The Assisted Living and Continuing Care Retirement Community State Regulatory Handbook, 2009*.

declining occupancy, unexpected cost increases, slow real estate markets, and declining equity and credit markets. While few CCRCs have failed, challenging economic and real estate market conditions have negatively affected some CCRCs' occupancy and financial condition.

- With respect to financial oversight of CCRCs, states we reviewed varied in the extent to which they ensured CCRCs addressed their risks, and some focused more on long-term viability than others. Most of the states we reviewed required CCRC providers to maintain some level of financial reserves to address financial challenges. In addition, most of the states we reviewed required CCRCs to annually submit audited financial statements that reflected financial performance for the past year. However, only four of the states required information that could help them assess each CCRC's long-term viability, and three states had conducted financial examinations. Three of the states we reviewed required certain CCRCs to perform actuarial studies at regular intervals and one used financial information submitted over the years to assemble trend information including financial ratio trends.[3] Actuarial studies, according to industry participants, can help CCRCs plan for contractual obligations and set appropriate housing and care prices. Without them, they noted, a CCRC may appear financially stable in the short term yet still face threats to long-term viability. The lack of a long-term focus creates a potential mismatch with residents' concerns over their CCRC's long-term viability. CCRC bondholders and rating agencies, which focus on long-term viability, often place requirements on CCRCs that go beyond state licensing and oversight activities. While we did not survey all 50 states as part of our review, according to an industry study, 12 states and the District of Columbia do not have CCRC-specific regulations, meaning an entity in 1 state may be subject to such regulations while a similar entity in another state may not. Regulators and CCRC providers we spoke with generally believed that current CCRC regulation was adequate, however, some CCRC residents' association officials expressed the need for financial oversight that focused on the long-term viability of CCRCs.

- While CCRCs offer long-term residence and care in the same community, residents can still face considerable risk. For example, CCRC financial difficulties can lead to unexpected increases in residents' monthly fees. And while CCRC bankruptcies or closures have been relatively rare, and residents have generally not been forced to leave in such cases, should a

[3]Florida regulators said that they maintained a spreadsheet containing financial information on CCRCs dating back over a decade and used the data to develop trends of financial ratios for each CCRC.

CCRC failure occur, it could cause residents to lose all or part of their entrance fee, which may amount to hundreds of thousands of dollars. For example, residents of one CCRC in Pennsylvania lost the refundable portion of their entrance fees in 2009 when the facility became insolvent after a change in municipal tax policy made the CCRC liable for unanticipated local taxes. Ultimately, it was sold to a new operator. Residents can also become dissatisfied if CCRC policies or operations fall short of residents' expectations or there is a change in arrangements they thought were contractually guaranteed, such as charging residents for services that were previously free. In addition, residents also face the risk of being transferred involuntarily from one level of care to another or of not being able to obtain assisted living or nursing care on-site.

- Most of the states GAO reviewed take steps to protect the interests of CCRC residents, such as requiring the escrow of entrance fees and mandating certain disclosures. For example, a number require contracts to be written in clear and understandable language, though some industry participants questioned residents' ability to fully understand them. In addition, not all review the content of contracts. Also, states we reviewed varied considerably in the type of financial and other disclosures required of CCRCs. For example, some states required disclosure of fee schedules and a history of fee increases, but other states did not. Also, not all require disclosure of policies likely to have a significant impact on residents' satisfaction, such as policies for moving between levels of care. In addition, regulations in some states require that residents of a CCRC be allowed and encouraged to form groups in order to communicate with management, while other states had no such requirement. As noted above, 12 states and the District of Columbia do not have CCRC-specific regulations, meaning an entity in 1 state may be subject to such regulations while a similar entity in another state may not, and consumers in some states may not receive the same protections as those in others. In contrast, some CCRCs voluntarily exceed disclosures and protections required by state regulations.

The report we are releasing today acknowledges that CCRCs can benefit older Americans by helping ensure access to housing and health care in a single community as they age. However, choosing to enter a CCRC can be a difficult decision, and is not without significant financial and other risks. Entering a CCRC often means committing a large portion of one's assets with the expectation of receiving lifelong housing and care. Further, the stress that recent economic events may have placed on CCRC finances underscores the importance of regulators being vigilant in their efforts to monitor CCRCs' long-term viability and protect consumers. The potential financial risks to CCRCs, and the risks to residents that result from committing a considerable amount of money to a CCRC, highlight the importance of states being vigilant in their efforts to help ensure that CCRC residents' long-term interests are adequately protected. Such efforts will only become more important as the number of older Americans grows.

Chairman Kohl and members of the committee, this concludes my prepared statement. I would be pleased to respond to any questions.

GAO Contacts and Staff Acknowledgments

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