How Will Your Clients Pay for Long-Term Care?

The odds of requiring long-term care may be higher than some people think (Table 1). These odds are far greater than those of losing a home to fire or being in a major auto accident, for which our clients buy insurance. Interestingly, few advisors would condone letting clients go without auto or homeowner's insurance, but they completely overlook the need for clients to mitigate their financial risk with long-term care insurance.

What Are the Odds?

- Probability of losing a home to a fire: 1 in 1,200
- Probability of having a major car accident: 1 in 240
- Probability of a hospital stay costing $30,000: 1 in 15

*T. Kesy, **Trusts & Estates**, 2000*

Table 1
Probability of Needing Long Term Care

Age	Probability
55	10%
65	40%
75	60%

(Source: New England Journal of Medicine, 1992)

The recent bear market underscored just how little people can really tolerate risk. An extended stay in a nursing home could be far more devastating to an investment portfolio than a typical market correction. At least the markets have a chance of going up again, whereas long-term care costs can keep eroding a portfolio indefinitely.

In addition, the threat of long-term care affects the way people live during retirement. If people believe that they will have a huge financial liability down the road, they are likely to be more frugal in retirement. Thus at a time when people should be enjoying their golden years, they are actually taking fewer and less expensive trips, not purchasing what they really want, and not giving as much to grandchildren and charities as they desire.

So, short of a decisive heart attack, quick cancer, or a fatal car wreck, the question is not necessarily **if** any of us will need long-term care, but more likely **how** to pay for it. There are really only three choices: 1) rely on family-provided care, 2) self-insure or 3) purchase a long-term care insurance policy. Since relying on family members for care is something that most of us would like to avoid, let's look at options 2 and 3.

Self Insurance

If clients are going to self insure, they need to have an adequate amount of capital set aside for that purpose – and be willing to use it when the time comes. This should not be done blindly. Instead, it should include an analysis of the client's personal and financial resources, various methods of funding, and a lifetime cash flow projection showing the possible impact of a long-term care need. The self-insurance fund can remain part of an overall semi-liquid portfolio of stocks, bonds and mutual funds.

Long-Term Care Insurance Policy

The purpose of insurance is to transfer an unacceptable risk to another entity in exchange for a premium. Because not everyone will need long-term care immediately or at all, the premiums are small in comparison to the potential benefit. For example, a $100 per day lifetime benefit plus inflation rider with a strong company costs about $780 per year for a 40-year old; $1,000 for a 50-year old; and $1,300 for a 60-year old. Rates go up quickly after that, so locking in the rate at an earlier age can make more sense than trying to accumulate a self-insurance fund.

Keep in mind that it's a jungle out there. There are good and bad companies, and many carriers without significant experience are getting into the business. Policy options, benefits, definitions, agent knowledge, and agent integrity differ significantly, so it is best to seek the advice of an independent agent not tied to any particular company.

Here are some basic facts about long-term care. If you or a loved one needs to move into a nursing home, it could cost from $85 to $150 a day or more. The same goes for skilled nursing care you may receive at home. And the only way to get help paying the bills is to go broke — and thus qualify for Medicaid — or buy long-term care (LTC) insurance. The goal of a standard LTC package is to cover most or all of the bills if the client needs nursing care for an extended period.

There are also some optional riders you may want to consider:

Return of Premium. Like other kinds of health insurance, standard LTC policies provide peace of mind but pay off financially only if the policyholder actually gets sick. With the return-of-premium rider, the benefits paid out are deducted from the total of all premiums paid in and the balance is refunded to the policyholder's estate. Because premiums may cost $25,000, $50,000 or more over an individual's lifetime, this can provide a significant bequest for the client's heirs.

Shared Benefit. The shared benefit option is a less expensive alternative for married couples than buying a separate policy for each spouse. They can pool coverage at a cost slightly higher than it would take to insure one partner, but at a discount to the premiums on two stand-alone policies. Because fewer than half of all couples need more than two years of LTC benefits between them, this can be a good option.

Inflation Protection. This rider isn't new but it remains crucial. Chances are, benefits purchased today won't be used for several years, by which time nursing home costs will probably be higher. While known as an "option," inflation protection is something that most people should consider.

End of Life Benefit. Around-the-clock care can be much more expensive than regular nursing home care. Some policies raise the benefits they pay in the event of terminal illness, for either hospice or in-home care.

Of course, not all insurance companies offer every option, and not all of these benefits are available in every state. Moreover, if any of these LTC innovations makes the client more receptive to buying a policy, it is important to make sure that the coverage fits into the client's overall financial plan.

If the client would rather explore other options, keep your eyes open — some life insurance policies (called "life contracts") now offer the option of using the dollars that would otherwise fund a death benefit to pay LTC expenses, and a few annuity contracts are tailored to play a similar role. With some of these products, the client can potentially cover the risk of long-term care with a single deposit into an interest bearing account and still have access to the funds.

Tax Credits and Deductions

In recent years, both the federal government and the states have taken steps to make it easier for individuals to purchase private long-term care insurance. The federal Health Insurance Portability and Accountability Act (l996) allows individuals to apply long-term care insurance premiums and out-of-pocket expenses toward the 7.5 percent base for medical expense deductions. To get the deduction, the policy must be tax-qualified. This law also provides that benefits received from qualified long-term care policies are not taxable.

There are also tax incentives for C corporations and self-employed individuals (visit the Journal of Accountancy for related articles and information).

The need for long-term health care is no longer a rarity, but a probability. Even affluent clients need to mitigate the realities of long-term care and its potentially catastrophic costs. Long-term care insurance may offer more than financial benefits. It can provide peace of mind.

More than Nursing Homes

Long-term care is not just nursing home care. It includes an ever-changing array of services aimed at helping people compensate for limitations in their ability to live independently. Long-term care should meet the individual's medical needs, as well as their social, financial and housing needs. It can range from assistance with household chores, to assistance with activities of daily living, to highly skilled medical care. Long-term care services may be provided in a variety of settings such as the home, community sites (adult day care centers) or nursing homes.

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