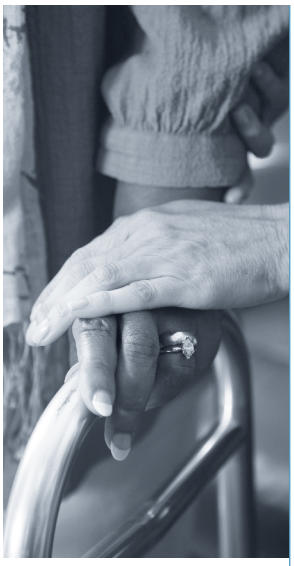
HBKS® Wealth Advisors

Long-Term Care Insurance

A Lot You Need to Know



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What do you associate with the phrase, "long-term care"? The first thing you think is probably, *expensive*. And then, *I need to think about buying a long-term care policy*.

Long-term care is a pressing concern for many families. And perplexing. It's hard to know what to do about it or even find out what your options are. Even when you make the effort to work through the issues, finding someone independent and able to comprehensively think through your financial picture and how long-term care applies to you can be difficult. There are many people happy to sell you a long-term care policy, but few who can help you buy a policy that reflects your current and long-term finances. What is right for you will depend on your situation and circumstance, but here are some independent thoughts, some education to help you begin the journey with your wealth advisor.

First things first: Why do you need long-term care? Take for example a married couple with a $1 million portfolio and a home valued at $250,000. They draw $40,000 per year from their portfolio and receive social security in the amount of $30,000 per year. They are living comfortably on $70,000 a year, so what is the risk? For one, one spouse may require an extended period of time with home or facility care, while the other spouse remains perfectly healthy. If the spouse requiring care has Alzheimer's, the average cost of a home health aide is $3,813 per month. In Florida, the average cost of a private room in an Alzheimer's care facility is $8,882 per month (rates vary by country and state). Medicare will not help. The basic rules on Medicare coverage for long-term care is that it only provides coverage for short stays in a skilled nursing facility IF you have had a hospitalization admission with an inpatient stay of at least three days and admitted to a Medicare-certified nursing facility within 30 days of that inpatient hospital stay AND you need skilled care such as skilled nursing services, physical therapy or other types of therapy. IF you meet all of those conditions, Medicare will pay for up to 100 days of benefits in some form. The first 20 days Medicare pays 100%, from days 21 to 100 you pay $164.50 in a copay and Medicare pays the excess. After day 100 Medicare pays $0.00

Medicaid will not help until the couples' assets are exhausted, though it does allow for a "community spouse resource allowance," meaning the couple can, for example, retain

$120,900 in exempt assets as well as their home as long as their home equity is less than $840,000. They also allow the spouse to keep a car. Still, the bottom line is that the spouse does not qualify for Medicaid until after a very large spend down of their assets, specifically those assets the surviving spouse needs to live on.

Now let's do the math. Let's reduce their annual spend from $70,000 to $50,000 a year, given the spouse's illness. Their new long-term care costs of $106,584, plus the $50,000 now totals a need for $156,584 a year. Their $30,000 annually of social security reduces the drain on the portfolio to $126,584 a year. If we assume three percent inflation and a five percent return on the portfolio, they will have depleted their assets to Medicaid levels in seven and a half years. This does not sound like a great plan so far. So what happens to the spouse who isn't requiring care after seven and a half years? Despite the spousal impoverishment clause, it would seem the surviving spouse IS impoverished. Even if the ill spouse dies after three years in the facility, the impact on the financial wherewithal of the surviving spouse is devastating.

It is important to note that long-term care inflation is different from regular inflation. In 2017, a Genworth study found that the cost of long-term care increased thee times the standard inflation measurement. So in reality, the financial outcome for the surviving partner is even worse than portrayed in our example.

THE STATS

So what are the statistics? Here are some interesting facts — and their sources — about long-term care:

- 47 percent and 58 percent — anticipated percentage of men and women, respectively, turning 65 who will have a long-term care need during their lifetime
- 10 percent — percentage of Americans over age 65 who have Alzheimer's dementia
- 33 percent — percentage of Americans over age 85 who have Alzheimer's dementia
- 15.2 percent — percentage of individuals turning 65 between 2015 and 2019 who will spend more than $250,000 on long-term care

Source: Morningstar "75 Must-Know Statistics About Long-Term Care: 2018 Edition"https://www.morningstar.com articles/879494/75-mustknow-statistics-about-longterm-care-2018-ed.html

- 49 percent of all insurance claims lasted one year or less; claims that lasted over 1 year averaged 4 years in total

Source: American Association for Long-Term Care Insurance http://www.aaltci.org/short-term-care-insurance/

- 2 Years — Average number of years that an individual age 65 or older will have a HIGH long-term care need
- $0 — Median household wealth for people who have lived in a nursing home for 6 years or more

Source: Morningstar "75 Must-Know Statistics About Long-Term Care: 2017 Edition"

The moral of these statistics is twofold: long-term care is expensive and it is likely you or your spouse will need long-term care. As well, the risks are normally extreme, not average. For example, half of all claims lasted one year or less, the average stay is three

years. Those requiring extremely long care skew the curve. At the end of the day your risk is that you are one of the 50 percent who will more than a year or, worse yet, five-plus years.

IS IT FOR YOU?

Now that you know the risks, what are your choices to contend with them?

OPTION 1 — Do nothing and roll the dice.

OPTION 2 — Insure you have adequate financial resources to self-insure.

OPTION 3 — Secure some level of long-term care insurance.

OPTION 4 — Consider legal options which could include disinheriting or divorcing a spouse, Medicaid planning where you gift away assets and/or reposition assets to allow for faster qualification.

Who should have long-term care insurance? Again there is no single answer, however there are some ways to narrow it down. The first is your asset base. Generally speaking, if you have assets over $750,000 and are married, but under $5 million you are a candidate. Long-term care for those with less than $750,000 in assets could also be appropriate, but the risk you face is that the cost of the insurance often impacts the viability of your retirement. We have done a policy for someone with $250,000 in assets. She was single, had sufficient pension and social security resources, was a net saver in retirement, wanted piece of mind, and had some resources she wanted to reposition that were not "investment" dollars. People with over $5 million typically have more than enough to accomplish their goals, and thus can self-insure. We have also used long-term care insurance with these people to leverage their estate. In this case it's a simple reposition — Perhaps allocate some dollars that normally would sit in cash to a product that can provide long-term care benefits if needed or a death benefit equal to premiums paid if you don't need it. It's always a tough call, and should be made in conjunction with a financial advisor and wealth team who has a deep understanding of your resources, your investment plan, your family and your goals.

HOW DOES IT WORK?

If insurance does make sense, how does it work? There are generally three types of long-term can insurance: Traditional Long-term Care Insurance, Hybrid Life/Long-term care and Hybrid Annuity/Long-term Care. There are some general rules of the road for all of them:

- First and foremost, what does it cover? It depends on the policy. Some only cover home care; some only facility care; others, specialty care and some cover it all. The policies we typically recommend cover all three, including full skilled nursing home care, assisted living, home health care, adult day care, respite care, hospice services and others.
- Each policy also has an elimination period, which is basically a waiting period. Most policies are 90 days, but some are different and some you can tweak. We typically prefer the 90-day, as that coincides with the end of Medicare's coverage.
- To qualify for coverage you will have to be certified that you are unable to independently perform two of the six "activities of daily living": eating, toileting, bathing, transferring, dressing and continence. There can be other ways to qualify based on severe cognitive impairment.

- Once you qualify, the policy works one of two ways: Indemnity — the policy simply pays you the stated amount and you do what you want with it (these are less common and often more expensive); or reimbursement — you incur the costs and then are reimbursed from the policy. The policy structure you purchase will determine the maximum amount of your benefit per day, per month and lifetime.
- Lastly, long-term care benefits are tax free and can be deductible. The deductibility has limitations and there are some interesting approaches you can take, such as passing it through an LLC to maximize the deduction. But just know there are possible tax benefits.

The marketplace for long-term care insurance has shrunk considerably since its invention. It is generally understood that carriers came out aggressively early on with assumptions that turned out to be actuarially wrong. Carriers were absorbing far more costs than they were willing to sustain. Most of the carriers increased premiums (and continue to do so), while many others locked their book of business and no longer write long-term care insurance. There are still carriers in this space, however the prices have risen and their underwriting has become much tighter.

POLICY TYPES

Insurance has evolved over the years. The most basic form of coverage is **Traditional Long-Term Care Insurance**. Like homeowners insurance, you set your coverage limits, and every year you pay a premium. Every year you hope to stay well, and thus the premium is wasted. Every year you get a renewal and it could cost more. The benefits are that, on a relative basis, the initial costs are lower for a pure long-term care benefit. The drawbacks are that it is a non-guaranteed premium and if you don't need care, you do not get a return on your dollars. Additional carriers have entered the market to tackle these drawbacks, but as with anything there is no free lunch here; solving problems comes at a price.

Hybrid Life/Long-Term Care Insurance is essentially a life insurance policy. If you die it pays a death benefit. If you need long-term care, it allows you to, tax free, accelerate your death benefit to cover long-term care. Many of these policies also offer a continuation of benefits provision that extends the coverage even longer. Some have a return of premium component that, assuming you haven't passed away or needed long-term care, you can ask for your money back. Some also offer unlimited payout periods, which are virtually unheard of now in Traditional Long-Term Care Insurance. The major drawbacks here tend to be the up front costs although for younger clients (40-55) you could structure it to be more in line with traditional care.

Hybrid Annuity/Long-Term Care Insurance is virtually identical to the life insurance version — you are buying an annuity typically with a fixed interest rate that provides for tax free utilization of the cash value for long-term care if you need it. In most cases this is provided with a continuation of benefits for after the exhaustion of the principal. If you do not use the proceeds you simply receive the market value. In most case designs, just as in life insurance, you are effectively giving up the opportunity cost of the earnings on those dollars in exchange for a tax free, leveraged, long-term care benefit. These are typically perfect for clients whom have less than perfect underwriting files. They are also great for clients whom have old fixed annuities doing nothing with built in taxable gain. If LTC is needed, you then can convert an ordinary income taxable event into a tax free event.

As mentioned initially, none of this is easy. This is also a highly individualized decision and no two clients will treat it or view it the same. It is our job to make sure that you are aware of the options and make an informed decision about these risks which requires us to know you and your complete picture first. Then we add in our specialists and partners to provide the product and design customized to you. In the next part of this article, we will go through some case designs to better understand each of these types of coverage.

Lastly, it is important to know the major players in this space given how frequently it changes. The major carriers in the traditional long-term care space are Genworth, Mutual of Omaha, National Guardian, State Farm, Mass Mutual, NorthWestern Mutual and TransAmerica. The life insurance hybrid benefits are available from Lincoln, NY Life, State Life, Nationwide, Pacific Life, Forethought and Minnesota Life. The major player in annuity hybrid is from State Life. This is not a comprehensive list, but should give you a flavor for the carriers.

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