WEALTH MANAGEMENT / RETIREMENT PLANNING

What Investment Advisers Need to Know About

Long-Term Care Insurance

BY MICHAEL BROWN

When I was a paramedic, I spent a lot of time in and out of nursing homes and assisted living facilities. In fact, it took me all of a month of zooming around the Washington, DC, metropolitan area in an ambulance to come to this conclusion: Long-term care (LTC) is big business. I was amazed at how many of my patients required some form of routine LTC. It’s no wonder that several years later, when I started working in the financial services industry, I was drawn to long-term care insurance (LTCI) sales. I was surprised to find that many of my LTCI clients already had well-qualified financial advisers. But I was even more surprised that I won their business because these advisers had never talked with their clients about LTC.

LTCI is easier to broach with clients now that the insurance industry has launched a significant public-awareness campaign. Baby boomers in particular are seeing the impact of longevity as they watch their parents deal with LTC. But don’t just assume that, at the very least, your clients want a better understanding of the subject. Gordon (2005) pointed out, more importantly, that you may leave yourself exposed to lawsuits by not exercising due diligence in addressing LTC.

What then do you tell your clients about LTC?

First tell them exactly how LTC is paid for in the United States. Their choices are welfare, their pocket-books, or LTCI. Second, make sure they are aware of how LTCI works. Finally, make sure they know when it’s the right time to buy LTCI.

Funding long-term care

The first option for funding LTC is to rely on the government. Most people are shocked to find that Medicare plays almost no role in LTC. Medicare was designed as a safety net and provides only about 50 percent of health-care needs in retirement. This safety net was created during the Johnson administration primarily to prevent the exclusion of millions of elderly from quality health insurance. Caseel et al. (1999) concluded that even with the advent of Medigap and the recent prescription drug benefit, Medicare at best is fragmented and favors acute care. Typically, Medicare may cover the first 100 days of LTC, and even then we are talking only about specific acute treatments such as emergency room visits, admissions to a hospital as needed, and perhaps rehabilitation. If a client needs an extended stay in an LTC facility, Medicaid takes over.

Medicaid is a state-run, federally funded entitlement program. It is a welfare system for those who no longer can afford health care, or in this instance, long-term care. As such it is extremely difficult for a client to qualify for Medicaid without spending down almost all assets. A Medicaid qualifier is left with his or her house while alive (home equity later can become part of a Medicaid claim), and $2,000 in cash and other assets. The Medicaid qualifier quite literally is left in poverty. For years the affluent have played the Medicaid game by trying to plan when they will need LTC and reappropriating their assets in a desperate ploy to elude auditors. This has become more difficult since the Omnibus Reconciliation Act of 1993, which mandated that states must recover Medicaid costs from estates. The Deficit Reduction Act of 2005 contained specific language limiting the federal government’s fiscal liability for the looming LTC crisis, further limiting government funding for LTC.

The second option for funding LTC is to self insure, an option available only to the upper and upper-middle classes. Clients considering this option must understand the cost of LTC, and this cost varies across the country. A Metropolitan Life (2005) survey found that the least-expensive region in the United States for a private nursing home was Shreveport, LA, at $115 a day. The most expensive region is Alaska at $531 a day. New York, NY, was $320 a day; Louisville, KY, $189 a day; and Salt Lake City, UT, $155 a day. Overall, the average cost for a private room in a nursing home in the United States was approximately $74,000 per year or $203 a day.

A recent study from AARP (2005) found that the lifetime cost of at-home care for disabled people after age 65 was approximately $174,000, compared with the lifetime cost of care in a nursing home, which was $179,000. While it may seem that these costs are nearly identical, in reality at-home care tends to be less expensive but lasts longer than nurs-
Personalizing Long-term Care Insurance

The final method for funding LTC is with LTCI. Many insurance companies carry this product, and policies vary significantly. The following are common themes in all LTC policies:

1. **Daily benefit.** How much does the client’s selected region average per day?
2. **Benefit period.** Does the client want to provide for one year of coverage? Two years? Perhaps unlimited coverage?
3. **At-home care.** Some policies consider at-home care to be an additional option. Many clients may prefer at-home care as opposed to nursing-home or assisted-living care. Most policies provide this option as a percentage of the daily benefit (100 percent, 90 percent, etc.). At-home care has the potential for lower daily costs depending on the needs of the client. Some clients may want to sacrifice 100 percent at-home coverage for greater nursing-home coverage. The affluent may elect for quality at-home care to maximize their comfort late in life if skilled nursing is needed.
4. **Inflation protection.** This perhaps is the most critical aspect of an LTC policy. A quality LTC policy should have stable rates, much like a whole life-insurance policy. But, an additional option for the client also should be protection from the cost of inflation. Again, this protection varies but usually will consist of a simple increase (say a $5 daily benefit increase each year), a compounded increase (perhaps 5 percent compounded annually), or a consumer price index (CPI) increase. CPI increase usually allows the client to save money up-front with the option to increase the premium and the benefits of the policy to stay in step with national cost-of-living increases.

**When to Purchase**

When should your client buy LTCI? Much like life insurance, LTCI is underwritten based on several factors, but age and health play the biggest roles. Underwriters, however, aren’t necessarily looking for someone who might die on them. Underwriters are concerned about the individual who might live quite long with disability.

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**Underwriting Long-term Care Insurance**

By John Timmerberg, ASA, MAAA

Today 75 percent of long-term care insurance policies are issued to individuals aged 64 and younger, yet approximately 20 percent of all applicants are denied coverage at the time of underwriting. An adviser’s relationship with his client could be impacted by an unexpected decline of coverage and it is helpful to both the client and the adviser to understand the process.

Underwriting generally has become tighter in recent years and the possibility of having an application declined increases rapidly with age. Conditions that may lead to a declined application include the following: any emerging cognitive problems, stroke or TIA (mini stroke), build, joint problems, congestive heart failure, or diabetes. The underwriting decisions on conditions such as diabetes or high blood pressure may depend on how well these conditions are controlled. Health history and medical questions are part of each long-term care insurance application, but it is possible that your client may not have a complete understanding of or fully communicate their health issues. Some suggest that the least threatening and most effective method for obtaining health information is to ask clients for lists of their medications. Other information that may be considered by an underwriter is whether or not the applicant uses tobacco or participates in activities outside the home, and whether or not the applicant is married. When both spouses apply, the marital premium discount can be 30 percent or higher.

Underwriting varies significantly by company, especially in terms of the amount of information sought. For example, Company A automatically requests detailed physician records on all applicants as compared with Company B, which automatically requests these records only on applicants 70 and older. This type of difference will tend to lead to more declines and a better risk pool (healthier policyholders) for Company A than for Company B. In this case, Company B will tend to process applications much quicker (in 15 days or less) compared with Company A, which could take 45 days or longer to process an application. But, over the long term, it may be best to get your client placed in the best risk pool available to them.

Some studies suggest that the midpoint for the length of a long-term care insurance claim is about two years. But there are significant practical limitations to the existing data. Also, current long-term care insurance policies now provide coverage for less intensive services such as assisted living facilities and some policies provide for cash payments to the policyholder instead of reimbursement for formal care, encouraging less severely disabled individuals to access benefits earlier. Depending on the client’s needs, he may be best served by a policy that provides for four years of coverage or more.

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Continued on p. 34 >>
LTCI can’t be timed. Often clients are convinced that there is a “right” age to purchase the product. It is understandable that a 40-year-old might be hesitant to purchase a living benefit that he or she might not access for another 40 years. However, your clients must understand a few basic elements of the LTCI underwriting process. First, the younger you are the cheaper LTCI is. Second, any person may develop conditions at any time that can severely impact the availability of LTCI. Remember, underwriters are concerned with morbidity, not mortality. An injury to a joint, a variety of medical conditions, and early signs of Alzheimer’s all are examples of events that could forever preclude your client from qualifying for LTCI.

Taking all of these factors into consideration, the cost of LTCI premiums becomes exponentially greater with time. The American Council of Life Insurers (1998) found that the most affordable age to purchase LTCI is 35 to 39 years old while the least affordable age is 65 and older. But no matter what the age, the sooner LTCI is purchased the greater value returned to the consumer.

Not all LTC is created equal, and the affluent have the power to choose. Most people would rather receive LTC in the comfort of their own homes. While it may seem that at-home care is less expensive, that reality is true only if skilled nursing care is not needed. At-home care can be just as expensive as nursing-home care.

Often the retired will horde their money in the early years as a way of trying to ensure that it never will run out. Why wait until the need for LTC arises and pay dollar for dollar when LTC benefits can be purchased today for pennies on the dollar? Quality private care is available at home or at a nursing facility but at great cost. LTCI allows your clients the freedom to spend money early in retirement when they are most capable of enjoying it. If it’s purchased early enough, LTCI requires a relatively small annual investment that guarantees a significant source of funds that your clients will almost undoubtedly need.

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References


