Seeking Alternatives to Long-Term-Care Insurance

by Tom Nawrocki

One of the biggest challenges many advisers face is preparing their clients for long-term-care needs, which can wind up being hugely expensive—or nothing at all. For those who need long-term care, the costs are taking up an increasing amount of our medical spending. According to the latest study[1] from the National Health Policy Forum (NHPF) at George Washington University, Americans spent $207.9 billion on long-term services and supports for the elderly and disabled in 2010—that's nearly 8 percent of all health-care spending. The NHPF found that 12 percent of all Americans turning 65 in 2005 will personally end up incurring long-term care expenses between $25,000 and $100,000. Another 6 percent will incur expenses of more than $100,000.

Many people are used to relying on government assistance to help them meet their old-age medical needs, but the consensus of financial planners seems to be that long-term-care insurance (LTCI) is the best way to prepare for these expenses. Although Medicare Parts A and B are presumed to cover all "reasonable and necessary" medical expenses for senior citizens, including hospital stays, doctor visits, nursing facilities, and home health care, the Kaiser Family Foundation has estimated that for the average enrollee, Medicare covers only about 48 percent of these health-care expenses.[2]

Given that landscape, you might think the market for long-term-care insurance would be growing by leaps and bounds, but LTCI is still far from universal. A 2007 study released by America's Health Insurance Plans noted that the number of policies sold grew from 1.9 million in 1990 to 5 million in 2005.[3] More recent figures from NHPF pegged the rate in 2009 at about 7 million LTC insurance policies in force.[4] By contrast, there were 45 million Americans enrolled in Medicare as of 2008, and that number is expected to grow to 78 million by 2030.[5]

What Will It Cost Me?

One of the difficulties in preparing for long-term care is the unpredictability of the costs. An important place to start is to understand what the current charges are. Here are some 2010 national averages as reported by the National Health Policy Forum:

Nursing home care (annually)	$75,000
Assisted living facility care (annually)	$39,000
Home health aides (hourly)	$21
Adult day care (daily)	$67
Prescription drugs (annually)	$2,810

The LTCI Option

This is despite the fact that advisers generally recommend that not only should their clients buy some form of LTCI, they should do so by their 50s. "You know when to buy it?" asks Chris Cooper, CFP®, the president of Chris Cooper & Company and Eldercare Advocates in San Diego, California. "Birth. Long-term-care planning begins at birth. Most people don't realize that a good 35 percent or so of people who are utilizing nursing homes and long-term-care services are under the age of 65." Most planners aren't that extreme, but they do like to at least initiate the conversation when clients cross over the line of 50.

In addition to the age factor, there can be a prime amount of investable assets that make LTCI work. Evelyn Zohlen, CFP®, founder and president of Inspired Financial in Huntington Beach, California, finds that clients with less than $500,000 can't really afford a good policy to begin with, and those with more than $3 million or so can set up their assets such that they can self-insure. "Then we've got that sweet spot, that half million to $2.5 million range where they can afford it and they've got the most to lose," she says.

Most planners report that despite their best efforts, fewer than half of their clients end up carrying long-term-care insurance. "They go naked because they've had mini strokes, they've had heart attacks, whatever, or they go naked due to sticker shock," Zohlen says. "They are appalled at the cost of LTCI, yet the specter of long-term-care costs doesn't seem to be enough to move them."

Those costs increase the longer a client waits, of course, although older people are still generally able to get LTCI. Bruce Moon, ChFC, CLU, CASL, a vice president of marketing at OneAmerica Life Insurance in Indianapolis, Indiana, notes that his company has found the average age of someone buying an LTCI policy has stayed steady around 68, within a year or two, over the past 15 years. He says OneAmerica accepts 78 percent to 81 percent of all applicants for LTCI, regardless of age.

Although the price goes up, it still makes sense for some older people to invest in LTCI. "It gets expensive," notes Mike Johnson, CFP®, J.D., of Executive Wealth Management in Lincoln, Nebraska, "but you haven't been paying into it all along, either." As Moon explains it, if a younger adult could have bought $200,000 worth of coverage for $100,000, that same person 10 years older might be able to buy $150,000 worth for that same $100,000, and five years later maybe $130,000. It may seem expensive at that point, but you're still potentially receiving an extra $30,000 in coverage above what you paid.

"Long-term-care planning begins at birth."

– Chris Cooper, CFP®

Planning Beyond LTCI

But there will be people who resist, for good reasons or bad, and those people still need some form of self-insurance. The first step is to estimate their ultimate long-term costs. The problem is there's virtually no way to determine what those costs will be—whether the client will be in a nursing home for 15 years or drop dead of a heart attack on their last day in the office before retirement. "You have to expect the worst," says Cooper. "If you need LTC sometime in your 80s, what's it going to cost then? There's no way to say."

The first step is to determine what the costs are in your area. Geography plays a huge part in this. "Where do you live—Boston, San Francisco, or Oklahoma?" asks Zohlen. "Long-term care in San Francisco is about as ugly as it gets."

The costs for assisted living as opposed to a nursing home can be very different, and there's no way to anticipate what the clients' needs will be until the day arrives. According to Cooper, in California, assisted living can cost about $6,000 a month for the residence, with another $3,000 on top of that for such things as medical care, transportation, and prescriptions. But a nursing home can run somewhere between $8,000 and $10,000 a month, with another $2,000 to $5,000 for additional expenses. Someone who ends up on a ventilator can spend as much as $10,000 *a day*.

So there are not a lot of solid expectations that can be planned for. Moon has come up with a rough guide for estimating future long-term-care costs. The average person requires about two and a half years of care, so Moon recommends that people multiply their local annual rate for care times a reasonable inflation factor, then multiply that figure by two and a half. "As long as I've got that kind of nest egg, I've got a 50/50 chance of being covered," Moon says. "But you can't predict averages or where you're going to be on that chart."

For a more sophisticated approach, there are financial planning software packages that let you spin out scenarios based on various long-term-care variables, which you can then show to a client. Mike Johnson uses Financial Profiles software from Zywave (formerly EISI). "We don't create a totally separate long-term-care bucket," Johnson says, "but in our planning software we can run LTC scenarios and make sure [clients] understand that's coming out of their assets."

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For those people without LTCI, there are several ways to build some long-term insurance into their overall portfolio. One obvious strategy is to establish a separate account with funds earmarked for long-term care. These should include conservative vehicles, such as intermediate-term bond funds. The client will need to sacrifice some long-term appreciation to reduce the volatility of the instrument, but that strategy does preserve some liquidity in case an emergency arises. Another idea is to buy a single bond intended to fund long-term care. The length of the bond can be calibrated to the distance the client is from the likelihood of serious care. In either case, the asset can be funded and set aside, reducing the temptation and ability to withdraw the money before it's actually needed for its intended purpose.

Other, more solid assets work as well. Zohlen has clients who own two homes, and they have decided that one of the homes is their long-term-care insurance. If and when the couple runs into a situation requiring long-term care, the plan is to sell the house and finance it that way. Although this does set aside a discrete part of the portfolio, it also puts the couple at the mercy of the housing market. They could be forced to sell their house at a time when its value isn't strong.

If you do earmark a specific asset or vehicle for long-term care, it makes sense to ensure that the client appreciates the setup. Zohlen very carefully established a long-term-care vehicle for one of her clients apart from the rest of her assets. The account had $300,000 in bond funds, and was kept entirely out of the remainder of the portfolio. "When we made a custodian change, I asked her if she felt more secure having it in a separate account, or if she'd prefer having it in the main portfolio," Zohlen says. "She said, 'Frankly, I don't care, I never look at it, and it's a hassle to have a separate statement for it.' I said, all righty then, there's my answer. Who am I really trying to make feel better here?"

Considering Alternative Options

There are several types of asset-based products with a life insurance or annuity chassis that offer both death benefits and cash values, should the client ever need long-term care, funded with a single premium. Life-based products provide a death benefit that the policyholder can put toward qualifying LTC expenses. At death, any unused benefits pass income-tax-free to heirs, and tax-qualified long-term-care benefits are also income-tax free. Because of the Pension Protection Act of 2006, clients can withdraw money from annuity-based products income-tax-free as long as those funds are used for long-term care.

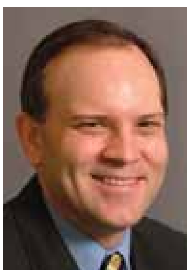
One key difference is that annuity-based products accumulate value for future long-term-care expenses, whereas the life insurance product has a day-one death benefit. There are also a lot of variations available within those two areas. The life insurance options include both whole and universal life, whereas annuities can be either fixed-deferred or variable-deferred annuities.

Zohlen structured a policy for a client of hers who wanted some form of long-term coverage. They reviewed what a long-term-care policy would cost for the 15 to 20 years before she was likely to need the coverage. The premiums cost about $5,000 a year, which over the course of 15 years became $75,000. So Zohlen asked her, "Instead of paying those premiums into LTCI, what do you think about a life insurance policy that's got a $250,000 death benefit? We can make a single-premium payment of $75,000 and be done with it, but if you were to die, your family gets the $250,000. If you get sick or have a long-term-care situation, there's a rider attached to this that allows the death benefit to be paid up to two times for long-term-care benefits." The upshot is that the client has long-term-care coverage without having to pay into something that's never going to benefit her family if she never uses it.

There are downsides, though. Regular LTCI may not cost as much as this type of coverage, and you can always quit it if you decide you don't need it. And of course, not every client has $75,000 lying around.

One area in which the planners we spoke to differed strongly was reverse mortgages. Some felt that reverse mortgages were a last resort; others use them as an integral part of long-term planning, from day one. Particularly in an era when home prices are still declining in some areas—and haven't yet started to rebound much anywhere in the United States—it might be advantageous for older people to take that value now. Especially for less-affluent people, their home can be the most valuable asset they have.

An important caveat is that if older people decide they can no longer be cared for in the home—if there are stairs they can no longer climb, or a lawn that requires more care than can be provided—and sell it, the proceeds from the reverse mortgage cease. If the home would not be suitable in a long-term-care situation, a reverse mortgage won't be ideal.



"There's a lot of planning that goes beyond just dollars and numbers."

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Another point of controversy is Medicaid planning, which some planners embrace while others consider it a last resort. "With Medicaid planning, you're effectively saying I want to plan so that I can keep my money and have my neighbors pay me," says Mike Johnson with a laugh.

But some planners consider it a necessity, a way of facing up to reality. "All financial planners need to think that all of their clients will qualify for Medicaid," says Cooper. "It sounds awful, but if they're faced with long-term care, they will need it, because they will never have enough insurance if the person lives long enough."

The basic strategy behind Medicaid planning is to transfer sufficient assets out of the client's portfolio so that they appear to be impoverished enough to warrant federal government assistance via Medicaid. That's significant because Medicaid will pay for benefits beyond what many LTCI policies will cover, such as doctor visits and prescription drugs.

One of the tricky aspects of this is that the client needs to make sure the assets are being transferred to a party responsible enough to oversee their long-term care. "Medicaid planning is in a way elder abuse, to give away all your assets just to qualify for welfare," notes Cooper. "'Here, Son, you take all this money, Daughter, you take all this money, then give it back to me if I need it.' But what if it's gone? Even if it's not gone because of their own malfeasance, they can lose it in other ways, such as by being sued."

The Family's Role

All the advisers I spoke with agreed that the family needs to be part of the decision-making process, whether there's an LTCI policy involved or not. It's not an easy conversation to have, but the earlier and more specific it is, the better off everyone will be. "It would be helpful if everyone did that when mom and dad were healthy, but it's an issue that even rational people with a lot of assets and a lot of college degrees don't want to confront," says Moon.

The very long-term plan itself will be determined in large part by how much familial help the client can expect to receive. Just as with the financial side of things, it may be hard to forecast where the clients' children will be in 10 or 20 years, but it shouldn't be impossible to gauge how involved they are willing to be in their parents' lives. At the very least, you can get a sense for who feels the responsibility for pitching in on their parents' care.

"If you got kids living down the street from you and engaged in your life, it's a different plan than if you have no kids at all, or kids that live on either coast when you live in the middle of the country," says Moon.

The key decision to make is which person is going to serve as a fiduciary—who will be able to handle the power of attorney from the standpoint of being able to figure out the answers to key questions. That person will have to show enough empathy and selflessness to make decisions as the parent would have wanted.

"You need to say, look, if the time comes, I want to go to these places and use these providers," Cooper counsels his clients. "They have to say, I only have so much means, so I can't go to a Ritz Carlton kind of place, I have to go to this Motel 6 kind of place. And [children] look at that and go, oh God, I don't want my mother in that, we'll keep her at home."

Cooper also recommends having a third party at the meetings between the parents and children, someone with no financial stake in the outcome (which means someone other than the financial adviser). This could be a minister, a social worker, or a family counselor—someone there simply to facilitate discussion and reach a consensus.

He's also seen something that gets glossed over in polite circles: children who aren't capable of carrying out their parents' wishes, or even worse, children who turn into thieves as soon as the power of attorney is turned over to them. A professional overseeing the process can help ferret out people who might be untrustworthy. The parent involved is more likely to take his or her assessment seriously if the person overseeing the process has no financial stake in the outcome.

Evelyn Zohlen recommends to even her clients who don't want a long-term-care policy that they buy a minimal one anyway, providing something like $50 a day worth of coverage—which would pay for no more than a home health aide to drop by for a couple of hours each day. The financial benefits are small, but the client is also then exposed to a whole raft of services that come with any LTCI policy. The insurer will provide care consultants who can help the clients review their options and varying levels of care available to them in their area. Those benefits usually come with an LTCI policy of any size.

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That's the sort of planning that must be anticipated when clients choose to, in Zohlen's phrase, go naked. Without a long-term-care policy in place, an awful lot of planning must take place. Before talking to family members, the client needs to first reach a place in his or her own mind—an ideal of what the end of life would look like. That's the vision he or she needs to present to the adviser, as well as to the family, in order to have any chance of that vision becoming reality.

"When I talk with my clients about LTCI and they get sticker shock, I often wrap up with the only-half-joking observation that you need to be nice to your children," Zohlen says. "You are blessing your family if you tell your family you've got your LTC needs covered, and even better if you give them your financial adviser's number."

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Tom Nawrocki, a former editor at Worth *magazine, is now the editor in chief of Triton Financial Newsletters, which provides communications for elite wealth managers around the country. He can be reached at Tom.Nawrocki@TritonNews.com.*

Endnotes

1. National Health Policy Forum. 2012. "National Spending for Long-Term Services and Supports (LTSS)" (February 23).
2. Kaiser Family Foundation. 2011. "Medicare Spending and Financing: A Primer" (February). The 48 percent figure is from 2006.
3. America's Health Insurance Plans. 2007. "Who Buys Long-Term Care Insurance?: A 15-Year Study of Buyers and Non-Buyers, 1990–2005" (April).
4. National Health Policy Forum. 2011. "Private Long-Term Care Insurance: Where Is the Market Heading?" Forum Session (April 15).
5. The Kaiser Family Foundation. 2008. "Medicare Now and in the Future" (October).