Long-term care insurance

What to know to protect your wealth

Scarborough Capital Management
Resource Series

SCARBOROUGH
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Introduction

Retirement can offer the reward of leisure time for a career well spent. Vacations at the beach with family, trips abroad, and even naps in a shady hammock. These are all parts of the dream of retirement many people have.

What happens though when that dream gets put on hold or worse, completely changed due to the illness of a spouse or loved one?

If you've suddenly realized that you're not really sure what long-term care entails, let alone considered preparing for it, not to worry.

In this guide, we'll explore what long-term care is, how it works, and what you can do to be ready in the event you need to be.

What is long-term care?

As Baby Boomers, the group of the population in their early 50s to late 60s (and now starting to turn 70) are beginning to retire in greater numbers, they are certainly enjoying the benefits of not going into the office every day. However they are also starting to see some of the issues that can arise.

According to the U.S. Department of Health and Human Services, “70% of people turning age 65 can expect to use some form of long-term care during their lives.”

And this care may not come inexpensively.

Long-term care may include some medical care, however most is found in services that are provided to an individual that help with basic factors of daily life.

Examples of what is known as “Activities of Daily Living” (ADL) would be getting dressed, eating, transferring from a bed to a chair, caring for incontinence, bathing, and using the bathroom.

Other activities that don’t quite fall into the ADL category are called “Instrumental Activities of Daily Living” (IADL). These would cover tasks such as taking medication, cooking, cleaning, and managing money. It should also be noted that these tasks are sometimes underestimated when the discussion of caring for someone arises.

“70% of people turning age 65 can expect to use some form of long-term care during their lives.”

Source: US Department of Health and Human Services

For example, after a hospital stay due to a fall, family members will certainly be around to help the individual get dressed, move around their house, and be there for dinner.

The question becomes will anyone remember that the electric and cable bills are due and the recycling needs to be put out every other week? Simply overlooking a few simple tasks can add time and stress to a situation, and one that can be solved with the proper planning.

There are a few ways long-term care can be paid for, and each comes with benefits and drawbacks. While paying out of pocket or relying on Medicare or Medicaid might be right for some, it's not the best solution for all.

Another alternative is insurance for long-term care, and based on a number of factors can be tailored to fit individual needs and goals.

How does long-term care insurance work?[1]

Essentially, a long-term care policy acts as insurance against paying for large healthcare expenses out of pocket and helps allow your savings and other assets to remain in tact.

Long-term care insurance can cover

- Home care
- Assisted living
- Adult day care
- Nursing homes

Long-term care insurance can cover home care, assisted living centers, adult day care centers, and nursing homes. One major benefit is that no matter what your income level, having a long-term care plan lets you choose where you receive care.

This is especially important if you should require nursing home care, since nursing home facilities many times give preference to those who can pay for their own care as opposed to those who are paying via Medicaid. This means you'll have a wider array of facilities to choose from and be able to make a selection that best suits the needs of you and your family.

1 Any guarantees are based upon the claims paying ability of the underlying insurance company.

Lastly, a sometimes overlooked benefit is the fact that outsourcing care can be a huge stress relief, even for just a few hours a day. This can free up family members to run errands, catch up on work, and even take some much needed time for themselves.

While it won't solve every problem, having greater peace of mind with your finances and time can help a difficult situation become a little less challenging.

So what types of long-term care plans are there?

What is traditional long-term care insurance?

These are benefits you would receive in the event you have a qualifying life event (which we'll cover shortly) and need care. Once you start receiving these benefits, they last until you no longer need care or the policy reaches its limit.

First, you should be in reasonably good health to qualify for this type of coverage. If you should develop problems that would require long-term care before you have a policy in place, it becomes much more challenging to qualify for this type of plan.

Next, the premium, or cost of the plan is determined by your age[2] when you purchase it, along with the plan's features and benefits you've selected.

To qualify to begin receiving these benefits you typically need to be chronically ill or cognitively impaired, and need help with two out of six activities of daily living (as outlined in part one).

Another point to consider is that this type of plan usually has a kind of deductible. The difference is you don't pay a predetermined amount, however you are responsible for paying out of pocket costs for about the first 90 days or so after you qualify for benefits. This time period is called an "elimination" period.

2 Other factors such as health and current medications also help determine the premium

Five key features of traditional long-term care insurance

Here are some considerations to discuss with your financial professional when selecting a long-term care policy…

1. Benefit – This is the amount your plan will pay each day, and coverage typically will range from $50 to $350 per day.

2. Benefit period – This is the length of time your policy will pay benefits once you need care. While some plans will offer a lifetime benefit, most plans typically fall within the one to six year coverage range.

3. Elimination period – Think of this as how high you'd want your deductible to be. Most plans typically allow a 20 to 100 day window where you'll be responsible for your own care until benefit payments begin. Obviously the longer the window the more out of pocket costs you would incur.

4. Location of care – While some lower cost plans will cover only nursing home costs, you can purchase some more expensive plans which cover care in assisted living facilities, adult day care centers, and even your own home.

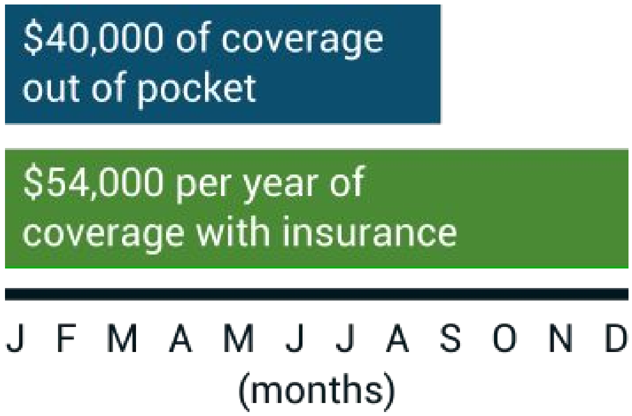
5. Inflation protection – This can be an add-on to your plan and while it will cause the premium to increase, having inflation protection can help insulate you from some of the rising costs of healthcare by allowing the benefit to increase by a certain percentage each year. A daily benefit of $100 may seem like enough today, but may only get you so far 10 or 15 years from now.

Costs and coverage of traditional long-term care insurance

Here's an example of how this may work. Let's say that you spend $2,000 per year on a plan which will yield $54,000 per year in coverage (which allows for about $150 per day).

Some may say that $2,000 per year is a lot to spend over the course of 20 years when the likelihood of needing coverage is unknown, especially if we feel relatively healthy.

Wouldn't it be better to simply pay out of pocket with the money you save in the event you do need coverage?



Well, if you did pay $2,000 per year over 20 years, it would only take you about nine months to break even on coverage.

That's not that much time, considering some of these healthcare needs could be over years, not months.

Pros and cons of traditional long-term care insurance

On the plus side, the premiums are generally predictable and this traditional insurance may allow you to stay in your own home longer.

It also helps protect your assets and allows your family members greater peace of mind in the event they're needed to help extensively with medical and daily activity needs.

Additionally, the benefits may grow with inflation (if that plan is selected), and policies may even have some tax benefits (although it's always recommended to consult your tax professional with your individual situation and needs).

As far as the drawbacks are concerned, these premiums can be expensive, generally you'll need to pay them for your entire life, and you'll have to initially be in decent health to qualify.

The greatest point against this type of coverage though is the fact that there is a chance you may never actually need it.

Traditional long-term care insurance

Pros

- ★ Predictable premiums
- ★ Protects assets, such as your home
- ★ Allows greater peace of mind
- ★ Possible tax and inflation benefits

Cons

- ★ Can be expensive
- ★ Will probably need to pay entire life
- ★ Have to be in decent health to qualify
- ★ Chance you may never need it

There is a way around this problem though, which we'll explain next.

Universal life insurance with long-term care benefit

These policies, also known as hybrid policies, allow you to set money aside and use some for long-term care only if needed.

Here's an example. Let's say your retirement income is based on four sources: Investments and/or qualified plans (your 401k or IRA), a pension and/or Social Security, life insurance, and then cash reserves.

How this plan works is that it uses part of your cash reserves and sets them aside in a Universal Life policy.

The main upside here is that this earmarked money often times can result in up to five times[3] your premium dollars to reimburse long-term care costs.

Now, back to the problem with traditional long-term care plans. If you didn't need the care in those plans, you paid for something you didn't use.

However, with this hybrid plan, whatever funds you didn't use for long-term care would be passed on to your heirs on the event of your death in the form of a tax free death benefit.

So, while you may not get the amount of coverage of a traditional plan, the money is still being used for *something*.

3 Source: Lincoln Money Guard Reservce LCN0805-2016784

We've also seen in some cases where an adult child will pay for long-term care insurance for their parent. The reasoning is the adult child or children will not be limited by a fixed income as many retired parents are.

Additionally, if the child is going to be receiving the tax free death benefit anyway, it is almost an insurance policy as much for them as it is for their parent.

If it's not used, they will get the funds back. If it is used, it's spent in such a way that it offers care and greater peace of mind for the family, saving high expenses and lots of time for others as well.

Next steps

So you're thinking more seriously now about long-term care insurance. So what are your next steps and what are some other areas to consider?

1. Talk to professionals - Lots of different policies are available, so work out scenarios with your financial professional. It also may be a good idea to consult your physician who can help you gauge your health risk factors.

2. Assess your finances - How much coverage do you feel comfortable purchasing? How much would you have remaining for living expenses or to pass on to your heirs?

3. Explore services and costs in your area - What are the facilities like? Could your needs be met at a less expensive facility, or would you have more extensive needs?

4. Talk to your family about your plans - There may be scenarios you haven't thought of where family members would be willing to help out more than you had expected. Or maybe it's the opposite. Make sure you have these conversations before an urgent decision needs to be made.

5. Act on your decision - Age in underwriting the policy can be key. In other words, if you want to purchase a policy, don't wait too long. The simple reason here is it costs less to buy a policy when you are younger.

Conclusion

As we've seen, this is not a one-size-fits-all type of plan, as everyone's financial situation and health outlook is going to be different. But there are several options that can be used to alleviate some of the pressures of this stage of life.

So while aging can't be prevented, focusing on long-term care planning can provide some peace of mind so you can spend less time worrying about care, and more time asleep in that hammock.

About Scarborough Capital Management

For over two decades, Scarborough Capital Management has provided comprehensive wealth management services to busy individuals and families who don't have the time to develop and manage a portfolio. What sets our company apart is our inherent interest in helping everyone from the mid-level employee to the top-tier executive preparing for retirement. Our services include a comprehensive array of financial planning support for people in all stages of life, including 401(k) and 403(b) Management, Thrift Savings Plan (TSP) Management, Wealth Management, Personal Pension Analysis, Social Security Analysis and Financial Planning.

If you have questions about how current events affect your portfolio strategies, please contact our office.

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