Long Term Care Insurance (LTCI)

Marketed by over 160 companies, LTCI is the fastest growing segment of the insurance industry.

As the Baby Boomers now age toward their 60's, 70's and 80's, the growth in LTCI makes sense. We live longer than our parents; the things that used to kill us now just disable us. But this phenomenon creates a risk because as we live longer, we use up all our funds for medical care. And where there is risk, there is insurance. That specific kind of insurance is LTCI.

LTCI is essentially an agreement between you and an insurance company for a pool of money they will pay out in the event you need long term medical care. In insurance terms, there is a very specific definition of when LTCI is triggered. There are six recognized "activities of daily living (ADL)" that we take for granted:

- Bathing
- Continence
- Dressing
- Feeding ourselves
- Using the bathroom
- Transferring (from a bed to a chair, for example)

An LTCI contract usually begins paying the benefit when the insured has lost any two of the six ADLs mentioned above. No matter where you are when it happens – at home, in assisted living, nursing home, etc. – when you lose two of the six ADLs, the policy is triggered.

By "triggered", I mean that the policy comes into active use. Typically, however, the policy does not start actual payments until you satisfy the "elimination period" (EP). The EP is basically identical to the deductible on your auto insurance. You pay the initial cost of a claim up to the deductible amount on your car. Then, if the claim is above and beyond that amount, the insurance company starts kicking in its share. The same applies with LTCI.

When you satisfy the deductible or "elimination period," you begin to collect actual cash benefits. This can mean two things: either you have to set aside enough money to pay for your care during the elimination period, or you have to hope that the initial cost of your medical care is covered by your health insurance or Medicare. For example, Medicare covers the first 100 days of nursing home care that results from any Medicare covered illness or injury. Therefore, most people choose a policy with an EP of 90 or 100 days. This approach allows the LTCI benefits to begin roughly when the Medicare or insurance coverage ends. But, it never hurts to have a good cushion of savings set aside in case Medicare does not cover your initial expenses.

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LTCI normally pays in monthly checks based on the amount of coverage you contracted for – e. g., $4,500 per month for three years or $3,000 per month for lifetime.

The benefit is a monthly amount, payable over a particular number of years, and may or may not have inflation protected increases built in. Obviously, the cost of the insurance is predicated on the benefits you may receive; the higher the benefit (and thus the higher the risk to the insurance company), the higher the premium cost to buy it.

Now, notice that I said "benefits you may receive." Like any insurance, you may pay the premium while all the while hoping you never need to use the coverage. Although most senior clients know one or more of their peers who required long term care, many of them don't fully appreciate the risk of needing long term care themselves.

Statistics indicate that 39% of individuals age 65 or older will require long term care at some time in their lives. If we only consider individuals age 75 or older, the likelihood of needing long term care jumps to 60 percent. (Source: Reged.com, CA Annuity study, 2004). More specifically, current statistics suggest that out of every 100 seniors, 61 will never need any kind of nursing care. Of the 39 who do, 19 of the original 100 will need less than one year's care and can thus self-insure. Of the remaining 20 who need more than one year of care, eight will need more than five years of care. Thus, only 8% of those eligible for LTCI are likely to get their money's worth in terms of collecting benefits.

It is therefore very unlikely that you will need to use LTCI if you are a purchaser. The principal question is: can you afford to be one of the 8% who need chronic long term care if it costs $70,000-$90,000 per year? Can you weather that storm? Can your spouse continue to live well if you are the one in the nursing home? Do you want to plan for that contingency or not?

Before you answer, realize that the single biggest risk to your financial well-being in your 70's, 80's, and 90's will be health care costs. These costs will also be the single biggest risk to your being able to leave an inheritance. To go about answering the question of how to plan for LTCI expenses, think about your financial situation and ponder these larger questions. Once you have a strong sense of what's really important to you, the smaller question of whether to buy insurance should be easier to answer.

Here's where to start: if either you or your spouse ever needed long term medical care, could your current income handle the cost? Funny as it may sound, I have a number of clients who actually would be saving money if one of them went into a nursing home since they spend more money as a healthy couple than they would if one of them were in a nursing home. If you are not one of those lucky couples, then think about this.

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If one of you needed to enter a nursing home or receive home health care, which assets would you liquidate first?

How long could you afford to continue to liquidate those assets? As a general rule of thumb, folks who have few, if any, assets at retirement – say $100,000 or less – are not really candidates for LTCI. Ostensibly, people who need to liquidate assets in large quantity do so because their guaranteed income of Social Security and pension are small. When coupled with few assets, these folks quickly "spend down" to the Medicaid limit and therefore qualify for state welfare benefits.

In the end, LTCI is really for the people in the middle range of wealth. While the folks who have sufficient assets and income can self-insure, the folks at the bottom of the rung have Medicaid to fall back on. Where will you end up? It's always the people in the middle who have assets to protect and who fear being driven into poverty that really need to consider buying the insurance. Does this apply to you?

How much will it cost? The cost of LTCI premiums ranges anywhere from $200 to $500 per month based on your age, health, and the type of benefit you wish to purchase. Regardless of the monthly cost, you are better served to think of the cost in terms of how much principal you are preserving, rather than how much premium is going out the door each month.

While the cost may appear to be, say, $2,400 per year, that premium might be buying $4,000 per month of benefit. If you owned the policy for ten years, the total out of pocket expenses to you is $24,000. While this may temporarily make you sick to your stomach, realize that if you are one of 39-out-of-100 seniors who need some level of nursing care, you will recoup your $24,000 in just six months of receiving the $4,000 per month benefit. Think about that: ten years of premiums recouped in just six months. Should you be in the category of the 19-out-of-100 who receive benefits longer than one year, you will collect far more than you put in.

Another way to look at it is to consider the $2,400 premium as equivalent to $40,000 of your principal earning 6% per year. The interest can pay the premium each year since LTCI costs generally do not change year to year. In this case, even if all the premiums you paid out never come back to you, you have likely at least maintained your principal to pass on as a legacy. The nursing home gets none of it. If, however, you went without the coverage and did end up in a nursing home, the $40,000 would be gone in ten months.....if you are lucky!