

# BDMP WEALTH MANAGEMENT



FINANCIAL, RETIREMENT & ESTATE PLANNING  
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## A PRIMER ON LONG TERM CARE INSURANCE

by

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As the Baby Boomer population continues to age, we receive an increasing number of questions about long term care insurance. The motivation to learn more comes from two main sources: clients who want to protect an inheritance for their children or other beneficiaries, and clients who want some control over where they spend their final years.

Long term care insurance is a very complicated insurance product with many “moving parts,” each of which impacts the premium cost. We typically begin with a design we can recommend without hesitation. Then, if necessary, we revise the design to accommodate the client’s budget (how much the client can afford/is willing to spend) on long term care insurance.<sup>1</sup> Although there are differences among the policies offered by the various insurance companies, here are the **major** design elements which are consistent across the top tier policies.

**Eligibility for Benefits.** Benefits under long term care insurance policies are triggered by impairment of cognitive function or the loss (*or inability to perform without assistance*) two “activities of daily living” (ADL’s). The number of ADL’s is usually six, and they are: bathing, dressing, toileting, continence, eating, and transferring.

**Monthly or Daily Benefit.** Most often expressed as a monthly benefit for services in a facility *or for in home health care*, the monthly amount can be adjusted in \$100 increments. Occasionally, the benefit is stated as a daily amount, which can be adjusted in \$10

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<sup>1</sup> Our commitment as independent insurance professionals is to search the marketplace for the best policies for each client. This involves consideration of the top-tier companies, and the company ultimately recommended will depend on a number of variables (some companies prefer married couples, others are more favorable for single individuals; some like clients in one age group, others prefer a different age group, etc.).

Unless medical underwriting issues—or other factors—require us to look beyond the top tier companies, we limit our search to companies we believe are committed to remaining in the long term care insurance business and which have a history of rate stability and high level of client service at the time a claim is made.

increments. At this time (2008), we are typically recommending as a full benefit \$180 per day or \$5,400 per month.

**Benefit Duration.** This design element determines for how many years the benefits will be paid. With reimbursement policies [see below], the benefit duration is more accurately described as how large is the pool of money available to meet long term care costs. Policies are typically offered for 2, 3, 4, 5, 6, 8, 10 years or unlimited.

We generally recommend that three (3) years is the minimum benefit duration that should be considered, and six (6) years is typically the maximum we recommend. However, especially for younger clients, where the incremental cost for a longer benefit duration—or even an *unlimited* one—is small, we occasionally recommend a longer period.

**Reimbursement, Indemnity, or Cash Benefit.** A **reimbursement** policy will, as its name suggests, reimburse the insured for qualified expenses up to the daily or monthly benefit amount. Receipts are required. If the daily or monthly benefit limit is not reached, the “remaining balance” rolls forward, in effect, extending the duration of the coverage.

An **indemnity** policy will pay the entire daily or monthly benefit to the insured if qualified care is being received. However, receipts must still be submitted to the insurance company.

The premium costs are comparable for a reimbursement and indemnity designs. To understand the difference in benefits, however, consider this example. Assume a policy with a daily benefit of \$200. If the loss of ADL’s triggers benefits, under an **indemnity** policy the insured will receive a check for \$200, *regardless of the costs actually incurred that day*. With a reimbursement policy, if the cost incurred for a particular day were only \$180, then only that amount would be paid. The \$20 “surplus” would be carried forward to be used another day.<sup>2</sup>

In contrast to reimbursement and indemnity policies, a **cash benefit** policy will pay the benefit amount to the client upon a showing that the insured has lost the requisite number of ADL’s. The full amount will be paid *whether or not any actual expenses have been incurred*. No receipts need to be submitted to the insurance company. Cash benefit policies are generally more expensive than reimbursement or indemnity policies, and not all companies offer a cash benefit design.

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<sup>2</sup> Some reimbursement policies offer monthly reimbursement. Under a monthly reimbursement provision, the insured could receive *more* than the daily benefit. That is, if benefits are triggered, it is the *monthly* total that acts as the cap, not the daily amount. For example, if the policy design is \$200 per day, and the actual costs incurred for home care are \$300 but they are received only every other day, the insured will receive a check for that month for \$4,500 (\$300/day x 15), since the total (\$4,500) is lower than the monthly maximum of \$5,400 (\$200/day x 30 days). [An indemnity policy can never pay more than the daily benefit.]

**Individual Policy or Shared Care.** A shared care policy allows a couple<sup>2</sup> to allocate between themselves the total benefit years available *as need dictates*. For example, if a couple took a 6 year shared care policy, either partner could use 4, 5, or 6 years, leaving the remainder (if any) for the other partner.

Because insurance companies have learned that they are more likely to pay out the entire benefit under a shared care design, a policy with a 6 year shared benefit is more expensive for the couple than if each spouse had purchased an individual 3 year policy. Shared care is a good option for couples not buying a longer benefit period.

**Home Care Benefit.** This is the percentage of the facility benefit paid for in home care, if benefits are triggered. Since most clients prefer to stay at home as long as medically feasible, we recommend 100%. Many policies today automatically provide for 100% home care, but it is still possible to find policies that offer a choice of 100%, 75%, or 50% of the facility benefit. *In our view, under no circumstances should a client consider a home care only policy.*<sup>3</sup>

**Inflation Rider.** We see this rider as essential for most of our clients, since the need for long term care is (hopefully) in the distant future. To keep pace with inflation, we typically recommend the 5% compound inflation rider, with no cap. Alternative choices include: no inflation rider, 5% simple interest capped at twice the beginning benefit amount, 5% simple interest with no cap, 5% compound interest capped at twice the beginning benefit amount, and 5% compound interest with no cap. Additionally, some companies offer a 3% inflation rider.

**Elimination Period.** This is the waiting period during which the insured must self-pay for long term care services. Stated differently, it is the length of time that must pass *after* benefits are triggered *before* the insurance company will begin to pay benefits to the insured. Medicare *may* pay for the first 100 days, but this is not always the case. Nonetheless, our analysis is that the most cost-effective solution is usually a 90 or 100 day elimination period. First day, first dollar coverage is available, as are elimination periods of 30, 60, 90, 180 and 360 days.

**Return of Premium/Non-Forfeiture.** This provision, which adds about 40% to the cost of a policy, provides that if the insured stops paying premiums, there is a return of some portion of the premiums paid or some period for which benefits would be deemed paid-

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<sup>2</sup> The term “couple” does not mean only legally married spouses. Whether heterosexual or same sex couples—as long as they have been together three years or more—are eligible for a shared policy . . . and for the premium discount offered to couples.

<sup>3</sup> One of the most troublesome “scams” in the long term care insurance field is the marketing of home care only policies. These are inexpensive policies, usually sold with the line “You don’t want to go into a nursing home anyway, so why pay for the facility care?” The sad truth is that just when the client really needs the benefits most (that is, when they are unable to manage at home even with assistance), the policy shuts down and leaves the policyholder with no benefits to meet the costs of long term care.

up (i.e., a limited paid up policy). Our recommendation is to **decline** these provisions. Most policies automatically include a *contingent non-forfeiture* provision, which allows the insured to reduce coverage or convert the policy to a limited paid-up benefit in the event of a substantial premium increase.<sup>4</sup>

**Other Considerations Which Affect Premium Cost.** Finally, the cost of long term care insurance will depend on how the insurance company evaluates the health of the applicant (standard or preferred), whether the applicant is married (or in a stable relationship), and if so, whether both spouses or partners are applying for the insurance or whether only one is doing so. Preferred health status usually results in a premium reduction of 10%. Premium discounts are also offered for applicants who are married (or in a stable relationship). The range of these discounts is generally *another* 30 to 40% if both apply and are accepted, and typically 15% if only one applies or one member of the couple is declined for health reasons.

The best way to find out what the cost of a long term care insurance policy for you will be is to begin the application process with the design of your choice. As with any insurance from a reputable agent, you are under no obligation to complete the purchase until the medical underwriting has been completed and you know:

- What health classification is offered, and
- What the final cost (with all discounts) will be.

We hope you find this summary helpful. Please remember, however, this is just a summary of the *main* policy design elements. There are numerous other provisions contained in the different policies offered by the various insurance companies. As you think through the long term care insurance process, we welcome your specific questions.

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<sup>4</sup> Long term care policies are sold with a premium designed to remain level for the life of the policy. However every company reserves the right to seek to have the state insurance commissioner approve an increase in premiums for existing policies as well as on new policies to be issued. These rate increases are rare, and as insurance companies gain more experience in the long term care market, we expect them to be even less common. However, they can and do occur. It is to address such cases that the contingent non-forfeiture benefit applies.