Understanding the Importance of LONG-TERM CARE PLANNING

Straight Talk about Common Misperceptions
Volume III - Options for Transferring Risk

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Certification for Long-Term Care

A long-term care plan can help provide FREEDOM and PEACE OF MIND

Welcome to the final (of three) educational eBooks designed to help you gain the knowledge you need to effectively plan for extended care. We feel strongly at CLTC that planning is not optional. That extended care is not a place or a condition. It is a life-changing event that needs a plan.

In our first eBook, "LTC Basics," we discussed,

- The Definition of Extended Care
- The Impact of Needing Extended Care
- The Odds of Needing Extended Care

This was followed in eBook 2, "**Money Matters**," with a discussion about,

- Facing the Cost of Extended Care
- The Feasibility of Using Personal Assets to Pay for Care
- The Reality of Relying on Public Programs

We also provided a high-level overview of the types of private insurance available in the market.

In "**Options for Transferring Risk**", we turn our attention to a much more in-depth discussion of long-term care insurance. Specifically,

- The Regulation of Long-Term Care Insurance
- The Types of Insurance Products Available Today
- State Partnership Plans
- The Tax Advantages for Long-Term Care Insurance

When Self-Funding and Federal Funding Aren't an Option

When self-funding or relying on the federal government for funding extended care aren't an option (the case for many), then the best way to pay for care is with long-term care insurance. It can provide an income stream that is separate from the income needed to meet other financial commitments.

Regulatory Oversight of Long-Term Care Insurance

Each state, through its insurance department or division, regulates that state's insurance carriers in accordance with laws known collectively as the state insurance code. Although each state has the authority to regulate its insurance business in any manner it chooses, state insurance laws and regulations are remarkably consistent, due primarily to the influence of the National Association of Insurance Commissioners (NAIC), which sets model regulations governing all insurance, including long-term care insurance.

The NAIC has model long-term care regulations on such matters as the standard definition of long-term care insurance, what benefits must be available and in what settings, renewability, pre-existing conditions, 30-day look back periods, Alzheimer's care, and so on.

These model acts and regulations are updated regularly to reflect changes in regulatory needs and priorities and to keep up with changes and innovations from insurance companies.

Designing An Extended Care Solution

The field of LTC insurance has been evolving. There are many types of insurance products available today that are based on innovative designs. All of them have the same purpose - to fund a plan to pay for care, thereby protecting the insured and those they care about.

Defining the Terminology

Generally, extended care insurance solutions come in two primary designs:

- **“Traditional” or “stand alone” LTC insurance (TLTCI)**
- **Combination (Combo) policies** – these are solutions that “combine” some form of extended care insurance benefits with another financial product.

Examples of “combo” products include:

- Linked Benefit with LTC Extension of Benefits (EOB)
  - Life insurance based, or
  - Annuity based
- Life Insurance with an Accelerated Death Benefit Rider for LTC
- Life Insurance with an Accelerated Death Benefit Rider for Chronic Illness
  - With a separate up-front chronic illness rider premium; or
  - No up-front charge with charges assessed at the time of claim

Please note: There is no clear regulatory or universal definition of the terms combo, linked-benefit, hybrid, or asset-based and are often used interchangeably in the marketplace.

“If you ever need care one day, it’s your loved ones - not you – who will feel the brunt of the personal and financial consequences of extended care.”

Traditional Individual Long-Term Care Insurance

Traditional Individual LTCI (TLTCI) pays benefits for a qualifying long-term care event only. The pool of funds is purchased based on a benefit period and daily or monthly amount of eligible benefits. Benefits can be paid on a reimbursement basis while others may have indemnity provisions (meaning they pay the full daily or monthly benefit when compensable services are received, rather than reimbursing actual costs).

TLTCI is typically the least expensive (of all the options) because benefits are only paid for extended care claims.

As the name suggests, an individual TLTCI policy covers only one person, though many offer a sharing provision for couples. In addition, couples – legally married or living together sharing household expenses - may also be entitled to a “couples discount”.

Traditional LTCI policies have the most options for customization. This includes choice of benefit period, elimination period, inflation options and other riders. Premiums are designed to remain level but are not guaranteed and can be increased.

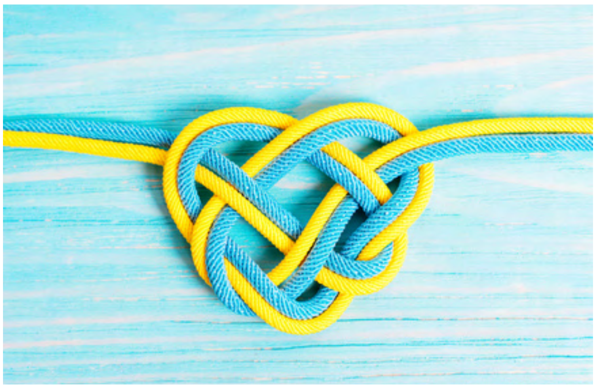
Why Someone Might Prefer a TLTCI Policy:

- On a budget
- No need for life insurance or an annuity product
- Only want to plan for extended care expenses (without a death benefit)
- Couples looking for a shared pool of benefits
- Individuals who want or need Partnership Medicaid asset protection

Why Someone Might Not Prefer an Individual TLTCI Policy:

- Premiums are not guaranteed
- Strictest underwriting
- No return of premium if benefits are not used

Combination Products



Combination products earned their name because they join solutions from two product categories. Life insurance or an annuity with Long-Term Care insurance. Their common thread is they pay a benefit whether extended care benefits are needed or not.

Hybrid or Linked Benefit with LTC Extension of Benefits (EOB) – Life or Annuity Based

Hybrid/Linked-EOBs fall under the umbrella of combination products because they join solutions from life insurance (or annuities) with long-term care. Extension of benefits (EOB) denotes having extra.Specifically, an extended benefit pool.The first pool of monies is associated with the life insurance death benefit (annuity cash value) which can be accelerated to cover care expenses.

Regardless of the type of product, the underlying benefit (e.g., the life insurance death benefit or annuity cash value) is depleted first to pay the extended care benefits. Once those base policy benefits are exhausted, the extension of benefits (EOB) (or "continuation of benefits" (COB)) portion of the policy begins to pay.

It is important to remember that these products are intended primarily for extended care planning, not for life insurance needs.Also, linked benefit LTC products enjoy the same LTC consumer protections required by the federal tax code and NAIC.

Why Someone Might Prefer a Linked Benefit with LTC Extension of Benefits Policy:

- LTC-purposed coverage
- Guaranteed premiums
- Simplified underwriting available
- Death benefit available without LTC use
- Return of premium is built-in

Why Some Might Not Prefer a Linked Benefit with LTC Extension of Benefits Policy:

- Highest premium - single or limited pay may be required
- Limited death benefit
- Cash value/death benefit used first to pay LTC claims
- Not Partnership qualified

Life Insurance with an Accelerated Death Benefit Rider for LTC

In this instance, there is one pool of leveraged benefits on a life insurance policy, with the ability to pay benefits based on the first need – extended care or death. As a result, the death benefit is available either as extended care benefits, a death benefit, or a combination of the two.

Most companies will allow up to 100% of the death benefit to be accelerated for an extended care claim. Or the insured may be able to choose (at time of application) what percentage of the death benefit to accelerate.The benefit is paid as a percentage of the total amount available for acceleration – typically the options are 2%, 3% or 4% per month.

For example, if a client purchases a $500,000 death benefit with 100% acceleration at 2% per month, the LTC monthly benefit would be $10,000 for 50 months or just over four years.

If LTC benefits are not needed, or only partially used, the remaining death benefit is paid tax-free to beneficiaries (assuming no loans or withdrawals were taken from the cash value, which reduces both the death and extended care benefits.)

Why Someone Might Prefer Life Insurance with an Accelerated Death Benefit Rider for LTC:

- Life insurance focused with an extended care option
- Flexible premium payments
- Reduced LTC underwriting
- Cost effective, particularly < age 50
- Cash indemnity LTC benefits available

Why Someone Might Not Prefer Life Insurance with an Accelerated Death Benefit Rider for LTC:

- Premiums may not be guaranteed
- LTC inflation rider not available
- LTC benefits reduce the death benefit
- Not Partnership qualified

Life Insurance with an Accelerated Death Benefit Rider for Chronic Illness

(with a separate up-front chronic illness rider premium)

Chronic Illness riders with up front charges are optional riders found on permanent life insurance. When they were first marketed, they had one notable restriction which was, in order to be eligible to accelerate the death benefit for care, the insured's condition had to be permanent and expected to last for the rest of their life. This is no longer the case, though is also not a requirement – it's important to check the contract language.

These types of product benefits may be initiated in a similar fashion as LTC policies – i.e., the chronic illness trigger is loss of two ADLs or a cognitive impairment. The rider is underwritten separately and typically has a separate, up-front cost. The monthly benefits and cumulative total benefits are determined when the policy is issued (assuming no withdrawals or loans from the policy) so the insured knows from day one what their benefits will be. Each dollar paid in chronic illness benefits reduces the death benefit by one dollar – resulting in 100% of policy benefits being paid - either as chronic illness benefits and/or a death benefit.

It is important to note this type of product is prohibited from being described or marketed as Long-Term Care insurance. Advisors representing these products do not need a Health license to sell it nor submit to ongoing continuing education. Finally, Chronic Illness riders are not required to include consumer protections that are required of a tax-qualified LTC insurance policy.

Life Insurance with an Accelerated Death Benefit Rider for Chronic Illness

(with charges assessed at the time of claim)

Chronic Illness riders with no charge until acceleration have grown significantly in popularity. They can be found on all types of Life insurance, including Term insurance.

In this instance, the chronic illness rider is a feature included in the policy at no additional up-front charge. But “no charge” does not equate to “free.”Instead of charging for the rider up front (as described above), a discount is applied to the death benefit that is accelerated when the rider is actually needed. The amount deducted is permanently forfeited as a back-end charge for the rider. Because of this, the amount of the chronic illness benefit cannot be determined until the time of claim.

The discounting of the benefit is based on several variables including age, gender, policy rate class, degree of impairment, as well as discount interest rates and policy cash values at time of claim.

Furthermore, there are two formats for determining the charge for the CI rider and how benefits will be determined.

The Discount Method: Both the charge and the benefit are determined at claim.

Lien Method: The benefit is known when the policy is issued, but the remainder death benefit is unknown.The cost (compounding lien) is deducted from the remainder death benefit paid to the beneficiary.

Why Someone Might Prefer Life Insurance with an Accelerated Death Benefit Rider for Chronic Illness:

- Life insurance focused with an LTC option
- Premium flexibility
- Reduced LTC underwriting
- Cost effective, particularly < age 50
- Availability of cash indemnity LTC benefits

Why Someone Might Not Prefer Life Insurance with an Accelerated Death Benefit Rider for Chronic Illness:

- Premiums may not be guaranteed
- LTC inflation rider not available
- LTC benefits reduce death benefit
- Not Partnership qualified

Beware: Chronic Illness Riders and Critical Illness Riders are Not the Same!

It is common to hear the terms "chronic illness" and "critical illness" used interchangeably and they are often combined under the term "living benefits". However, they cover different types of conditions, and each rider serves its own specific purpose:

- A **chronic illness rider** is associated with conditions of morbidity or an extended care impairment. The rider pays benefits when the insured has a rider-defined chronic illness event such as cognitive impairment or impaired activities of daily living.

- A **critical illness rider** is associated with very serious acute health conditions.This rider pays benefits for qualifying diagnosed conditions such a heart attack, stroke, cancer, the need for a major organ transplant, etc. Critical illness riders are generally NOT used for funding extended care.

LTC Partnership Programs

LTC Partnership programs, which are managed by individual states, make LTCI more valuable by offering guaranteed asset protection to those who purchase an approved policy. If after exhausting the policy's benefits, a policyholder applies for Medicaid, they can protect, depending on the plan, all or some of their assets which otherwise would have had to be spent down.

Partnership LTCI policies must:

- Include in inflation protection provision, and
- Be sold only by Partnership-certified insurance advisors who undergo special training

Keep in mind the policyholder's income is not protected from Medicaid.

Long-Term Care Insurance Policies and Tax Benefits

Tax qualified LTCI policies offer their holders certain tax benefits, including tax-free benefits, and depending on the type of policy, deductibility of premiums and preferential tax treatment in many states.

For example,

- All benefits from a policy that reimburses actual expenses are tax-free
- All benefits from a policy that pays a set dollar amount when the patient is terminally ill are tax-free
- All benefits from a policy that pays a set dollar amount when the patient is chronically ill are tax- free up to a set dollar amount per day (adjusted annually)

Benefits paid for covered care services from any type of LTCI policy are tax-free according to the guidelines above.

But only "traditional" individual types of LTCI coverage are eligible for a deduction of the premiums because premiums paid for an annuity or life insurance are never deductible.

Be the Architect of an Extended Care Plan

Review

When self-funding or relying on the federal government for funding extended care aren't an option (the case for many), then **the best way to pay for care is with long-term care insurance.**

Long-term Care insurance policies come in three designs:

Traditional LTC insurance that can allow two separate policies to share LTC benefits; **combination policies**, which link LTC benefits to another product like an annuity or life insurance and **life insurance that accelerates the death benefit to pay for extended care.**

Long-Term Care insurance policies offer tax-benefits such as tax-free benefits, deductibility of premiums, and preferential treatment by many states.

Only "traditional" LTC insurance policies can qualify for Partnership status; no form of hybrid or linked benefit LTCI can provide Partnership asset protection.

> ***You may never need care over a period of years, but if you did, what do you think providing care would do to your family emotionally, financially, and physically?***