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White paper

LTC combo policies

Sensible solutions for long-term care

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A while back, I was challenged by a financial professional who asked me why anyone would sell long-term care (LTC) coverage such as life insurance combined with a long-term care component. He was of the opinion that selling a single product with combined purposes creates confusion - that life insurance should be used for the purpose it was originally designed for - and long-term care needs should only be handled with dedicated LTC products. In a perfect world of clientele, he might be right. However, I routinely speak to financial professionals who have clients with objections and obstacles pertaining to long-term care coverage, and they're looking for solutions their clients are willing to purchase.

Traditional long-term care insurance (LTCi) policies may be the best choice for some people. They offer the most customizable choices for coverage, and may be less expensive — at least initially. However, there are common obstacles to these sales.

- *"Use it or Lose It" (loss of premium)* is one of the most common objections. A return of premium feature is expensive, seldom elected, and paid to the beneficiary. It is not for "buyer's remorse".
- *Potential price hikes.* While today's newer products reflect pricing based on gender and the current low interest environment, high policy retention and the unknown effect of better mortality increasing claims may still force LTCi companies to continue filing for rate increases, which can be unlimited in number.
- *Psychological block.* Many people find it difficult to purchase a product they hope never to use.
- *Clients under age are rarely open to purchasing traditional LTC policies.* Less than 12% of traditional LTCi policies are sold to people under age 50.[1]
- *Never ending annual premiums.* Most companies only offer annual life pay options. Single and short pay schedules, which reduce the risk of multiple price hikes, are more limited in availability.

Today, there are products that can address these client objections. The marketplace is growing with alternative LTC solutions attached to financial products; and these solutions can help meet client concerns as well as enhance the use of some life insurance scenarios.

Alternative LTC solutions linked to life insurance

LTC coverage combined with financial products (sometimes referred to as LTC combos) vary in type and design; and with proper choice of product, can enhance a client's financial strategy. This article will address LTC coverage attached to life insurance and the value it may provide. For example:

- People who are buying life insurance at an age where family protection is the primary need can use the addition of a LTC Rider to transition the use of the life insurance policy later in life to LTC coverage — a time when the need for family protection has been greatly reduced but protecting retirement income and assets from long-term care expenses may be more important.
- Combo solutions provide a way to avoid the "use it or lose it" (loss of premium) objection since the premium paid, and often more, will be recovered either through use of the policy for LTC benefits, and/or the payment of a death benefit.

- Premiums, death benefits and LTC benefits can be guaranteed with certain products. As long as premiums are paid as scheduled and no withdrawals or loans are taken, premiums cannot be increased and LTC benefits cannot be reduced.
- Premium schedules available vary from single pay and life pay to anything in between, so the client can choose a product and premium schedule that fits their financial circumstances and objectives.

While long-term care solutions linked to life insurance require underwriting, the requirements vary by product line from full LTC underwriting to simplified LTC underwriting. Some companies will also allow their LTC rider to be table rated, something that is not available with traditional LTC policies. Combo LTC solutions have similarities to traditional LTCi policies in the fact that they pay tax free long-term care benefits; and pay either full monthly benefits by some form of indemnity or benefits though monthly expense reimbursement. Otherwise, the features are generally not as customizable as a traditional LTCi policy. The trade off to lack of customization is knowing that if the policy is little or never used, a death benefit is paid as a form of cost recovery.

Linked Benefit LTC (also known as hybrid or asset based LTC)
With this type policy, choice of benefit periods vary from two to eight years (depending on the carrier), but one common choice is a 6 year benefit period sold as a “two plus four” option, which we will describe here. The first benefit pool is an amount that is available for monthly LTC benefits, but any amount not used for LTC is paid as a life insurance death benefit. This benefit pool lasts for two years when collecting the full LTC benefit amount. This benefit pool is reduced dollar for dollar and must be exhausted first when going on LTC claim.

Once the first benefit pool is exhausted, monthly LTC benefits are paid from the second benefit pool, which is available only for LTC benefits and lasts 4 years when collecting full monthly benefits. Any uncollected LTC benefits from the second pool are lost at death; however, when the insured passes away, a guaranteed minimum death benefit is paid to the beneficiary, even if the first pool of benefits have been totally exhausted.

The linked benefit LTC solution avoids the “use it or lose it” objection by offering a death benefit that is generally equal to or higher than the premium paid into the policy. Though placed on a life insurance foundation, these products have a 30 day free look period. There are also a variety of refund of premium options that can be included; and these features vary greatly by insurance company from day one refund of premium to a limited vesting or surrender period. These policies offer some customization with the ability to purchase substantial LTC benefits with choice of coverage periods and inflation protection similar to traditional LTCi policies. The policy may be paid for with a single premium, or with payment schedules of multiple years including pay to age 100; and monthly modes are offered by some companies on the multi-year payment schedules. Clients looking to purchase a linked benefit policy will generally go though a simplified underwriting process, which includes a telephone interview with cognitive testing. Generally, no para-med, no blood, nor any fluids are required; though occasionally an attending physician’s statement (APS) may be requested.

This linked benefit LTC policy may be a better fit for the following:

- More affluent clients with assets to reposition and who find value in paying up the policy quickly
- Clients who want LTC coverage closer to what is offered by traditional policies, such as longer benefits periods and inflation protection without risking loss of premium for non-use
- Clients whose main priority is LTC coverage to preserve income and assets, and understand the death benefit is more of a cost recovery vehicle, not fully leveraged death benefit protection
- Clients who want a policy that guarantees the premium cost and benefits paid

Life insurance with LTC Rider (also known as Living Benefits)
With this solution, long-term care coverage is accomplished by adding a LTC rider (for an additional charge) to the life insurance policy a person is purchasing. The death benefit is one pool of money that can be used while the insured is alive to help pay for qualifying LTC expenses. If long term care benefits are never needed or only partially used, any remaining death benefit is paid to the beneficiary. The LTC benefit is normally paid monthly and is a percentage of the death benefit, typically 2% per month of the death benefit (or LTC specified amount) - though choices range anywhere from 1% to 5%.

Long-term care riders are generally offered on permanent life insurance policies and are fully underwritten for both life insurance and long-term care. Therefore, it is possible to qualify for the life insurance yet be declined for the LTC rider. However, cognitive testing is not part of the underwriting process for this type solution and some companies will even allow their LTC Rider to be table rated. LTC benefits received will reduce the death benefit dollar for dollar; however, many companies offer a residual death benefit — such as 10% of the original specified death benefit amount — even if LTC benefits exhaust the entire death benefit of the policy. Be sure to check the policy contract as to whether a company offers an excess residual death benefit and what the details and limitation are.

But most importantly, one must keep in mind the original death benefit need. For some clients the insurance need may be to protect income and assets from depletion from in the event of LTC expenses. Other clients may have a specific amount of death benefit they wish preserved to be paid at death, so some companies will allow the LTC specified amount (the amount that may be accessed for LTC benefits) to be dialed down from the specified death benefit amount, which results is preserving a set amount that can be paid at death even if LTC benefits are used.

People typically interested in adding a LTC Rider to their life insurance policy vary greatly. The following client profiles provide an idea of who this type policy might be a good solution for:

- Clients with LTC concerns who have excess assets they wish to use to create a tax efficient legacy. With this solution, there is always a leverage of premium into a death benefit.
- This solution also appeals to clients who voice the typical objections to stand alone long-term care policies and like the idea that the entire benefit pool will be paid to either the policy owner or beneficiary
- Clients looking for an acceptable rate of return may look at this solution as a non-correlated asset in their portfolio. When purchasing a policy with death benefit guarantees, the ROR can be projected based on age of death or LTC event.
- Other potential prospects come from younger clients not ready to discuss purchasing full-fledged LTC coverage. The cost to add a LTC rider at younger ages is minimal and provides added financial protection should an unexpected LTC event occur such as from a car or sporting accident. While the purpose of the policy now is to protect the family financially in the event of the insured's death, the LTC rider can later transition the policy into LTC coverage.

Summary

For those who believe product sales should remain dedicated to the product category — that would be great in an ideal world where all is black and white. But the world I work in sees a lot of grey, and I am grateful LTC combo solutions exist, so we can still accommodate objections and obstacles with LTC solutions that a people are willing and able to put in place.

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[1] American Association of Long-Term Care Insurance- January 2019