PROTECTING YOUR CLIENT FROM LONG TERM CARE COSTS AND THEIR SOLUTIONS

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So how do you as your client's most trusted adviser protect your client from making a mistake and not understanding their real exposure and financial threat to the high costs of long term care? You basically have 2 initial choices assuming your client is under age 75, relatively healthy and understands that an unexpected, unreimbursed long term care expense is a real threat that can unravel their as well as their spouses retirement plans and lifestyle. You can either address the "800 lb. gorilla in the room" and talk about the "What if" scenario including the purchase of an LTCI policy. Or you can avoid the fact that costs for care at home or in an assisted living community are in the $60,000-$75,000 range, and that costs in a skilled nursing facility are in the $125,000-$175,000 range and are both increasing by 3% annually. The initial choice becomes should I or shouldn't I have this unpleasant and difficult conversation with my client. Since the odds of this problem affecting a client over age 80 is approximately 70%, it may make a great deal of sense to get your clients thinking about a solution to a problem he/she may one day likely face.

The first question becomes where will the necessary funds come from to pay for these costs? Is there a readily accessible source of sufficient funds that will not trigger a large unnecessary taxable event when liquidated? Should I self -insure against this threat or would it make more economic sense for me to purchase a long term care Insurance contract from one of the major insurers? Having a long-term care insurance contract will not only provide your client with the dollars necessary to pay for some or all of the expenses associated with their care, but will provide them with the independence and peace of mind knowing that they'll never be a burden to their kids or spouse. But will the costs be justified if they *never* need the coverage?

Depending on your client's particular corporate structure and age they may be able to deduct the entire premium or a part of it. However at a minimum most states have a 20% state tax credit for any individual. This is also one of the few times that an Insurance benefit can be paid for on a totally discriminatory basis, i.e. all officers and spouses, and then be taken as a 100% deduction in various corporate settings.

The second question becomes should I consider keeping all or a part of the exposure to a long term care expense? Should I self-insure or share the risk with an Insurer?
Is it less costly to self-Insure? Is this the best use of my assets? What type of an investment of my

asset's is this? *Keep in mind,* the premiums paid for this coverage isn't an investment at all, Instead it's a cost of protecting assets against a likely loss.

A long term Insurance contract can be purchased to provide a set dollar amount $100 -$500 on a daily basis. The coverage can pay a benefit for a minimum of 2 years to a maximum of 6 years after a 90-100 day waiting period. Most contracts are of a comprehensive nature meaning that they will pay for care in an Insured's home, an assisted living facility, or in a skilled nursing facility. They will pay for all 3 levels of care, custodial care, as well as skilled care and anything in between.

The prime reason many individuals are reluctant to purchase such a contract is because they're concerned about the waste of annual premium dollars if they pay a premium and then never need to collect the benefits? Many others are under the impression that they'll be better off if they merely self-Insure. So In an effort to encourage private individuals to purchase a long term care contract, and overcome the preceding two concerns, the Insurance Industry in conjunction with the federal government recently enacted legislation effective Jan, 2011, as part of the 2006 Pension Protection Act. This act now allows an individual to access up to $120,000 in 2015, annually adjusted for inflation, on a tax free basis from the death benefit of a life Insurance contract, if used to pay for a qualifying long term care expense.

If your client is healthy enough to purchase a long term care Insurance contract, he/ she now has 3 choices.

1. They can purchase a stand- alone traditional long term care contract ideally suited for the younger client 45-60.
2. They can chose one of the newer hybrid/combo policies that combines a life Insurance contract with a *long term care rider* or a *chronic care rider*.
   Although each option allows for a tax free distribution of death benefit for a qualified long term care expense, there are significant differences between the 2 options. The long term care rider has an upfront charge but no additional cost when the benefit is used. As opposed to the Chronic Care rider which has no upfront charge, but an interest charge is imposed if and when the benefit is actually used. Be aware not to allow your client to inadvertently confuse these two cost structures as it would be like comparing apples and oranges. Ideally suited for clients aged 60+ that have an existing need for

Permanent Insurance and secondarily a desire to have access to a tax free withdrawal to pay for long term care expenses if needed

3. Also available as of Jan 1 2011 is the ability to avoid tax on the gains of an annuity contract if it is used to purchase a long term care contract.
   For example if an individual started with a $50,000 single premium deferred annuity and it grew to $100,000 previously an individual would first have to pay the tax on the $50,000 gain. If however that same individual placed the same single premium annuity into a linked/combo annuity they would have the full $100,000 available as there would be no tax due. Plus they would have the leverage of a long term care Insurance policy which for a 65 year old would bring the net amount available to pay for long term care expenses up to approximately $350,000-$400,000.

Lastly the adviser should be aware that as a result of many Insurers having priced their long term care contracts incorrectly over the last 20+ years, primarily due to erroneous assumptions regarding earnings, drop rates and utilization rates, many of these companies are now attempting to raise rates. One such company is in the process of obtaining a historic 50-60% rate hike. My concern is that they will use that significant increase as a bargaining chip to encourage older existing policyholders to give up and scale back various benefits they previously purchased i.e., a larger daily dollar benefit, a longer benefit period, a 5% annual compound inflation rate. In any event it will cast a further negative and worrisome message to those currently considering purchasing a long term care Insurance policy.

If at all possible a client should *not* give up these valuable benefits on a wholesale basis and should carefully consider which if any benefits to drop, and pay the higher cost. Reason being, once they give these higher benefits up, they will never again be able to replace them, which is exactly what the Insurers are hoping to accomplish with these significant rate hikes. In my opinion a client should consider purchasing a LTCI contract in their mid –late 50's when their youth and good health will allow them to purchase this valuable protection at a lesser cost. One way to offset the fear of increasing future rate hikes is to purchase an individual or second to die combo/hybrid policy, or a traditional policy that pays a future dividend to offset future increases.

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BIO

Henry Montag is an Independent Certified Financial Planner in practice since 1976. He is a principle of The TOLI Center East, which provides independent fee-based performance evaluation for trust owned life insurance for private trustees & their advisers. He has had articles published in the NYSBA, NYSSCPA's Tax Stringer, &Tax Facts. He has lectured extensively on the proper utilization of financial products to protect and preserve assets to the NYSBA, the NYSSCPAs, the AICPA, Accounting Today & NcCPAp. He has been a source for The Wall Street Journal, Investor's Business daily, Investment News, Newsday, and has recently co-authored a book for the American Bar Association, entitled:
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