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Investments | Wealth Management

The Long-Term Problem With Long-Term Care

Another Insurance Company Folds Up Shop

Individuals have one less company to buy long-term care insurance through with Prudential Financial Inc.'s recent announcement that it is pulling the plug on selling new individual long-term care insurance policies. With MetLife and Guardian Life, this marks the third retreat from this market in under two years. The fact that these large firms are shying away from insuring the risk of long-term care expenses is a prime example of why this elephant-in-the-room problem will continue to wreak havoc on the finances of American families.

In a nutshell, these companies have decided that their money and efforts are better spent creating products that 1) have an easier-to-forecast future risk and 2) are affordable to more people.

It's Not Just About Mom and Dad

These days, when thinking of long-term care (LTC) expenses, most individuals wholeheartedly agree that buying coverage is a good idea. However, the intensity of the agreement doesn't reach its peak until an individual has direct experience with a family member in need of assistance. Most realize that they should buy the coverage for themselves and their spouse, and/or hope that their parents have gotten coverage on themselves. Although it isn't fun to have these conversations up, down, and across the family tree, it is a good idea to think of all family members and the potential financial, emotional, and physical fallout from having to become an unexpected caregiver. With this in mind, grown children in their 50s and 60s, siblings, in-laws, and uncles and aunts should be included in the thoughts of how care-giving activities for these individuals would impact your household financially, emotionally, and physically. An uncle and aunt in your hometown might have kids of their own, but if all the kids live in other areas of the country, who do you think is going to be called to action?

Rules of Thumb

As with most financial-planning related areas, there is not a precise answer to figuring out what kind of LTC insurance to buy. The primary problem is the cost. Since the odds of incurring long-term expenses are so great, combined with the high cost of healthcare and high healthcare inflation, the cost of LTC insurance is substantial. However, a few rules of thumb can apply. First off, if someone needs every last cent of income their retirement portfolio can provide, then there probably won't be a way to work the cost of LTC insurance into the budget. That being said, if someone has wiggle room in their budget, then these rules of thumb could apply to the following categories:

Retirement assets over $2 million: This is a level where one might effectively be able to "self-insure". However, if these assets are truly needed to provide maximum income, then the financial risk of LTC is still very real. The good news is that the cost of coverage, albeit expensive, should easily work into a revised budget.

Retirement assets ranging from a few hundred thousand to $2 million: This is the group that has the most to lose. A lifetime of prudent decisions that has led to a comfortable retirement could be easily destroyed by the cost of LTC. Individuals in this group should place the highest priority on trying to solve the LTC problem.

Retirement assets below a couple hundred thousand dollars: This group would likely have their retirement assets depleted if average long-term care expenses were incurred. If very little income is needed from a retirement portfolio, then funding LTC coverage might be possible, but otherwise it will likely be too much of a burden.

The Hybrid Solution

One exciting development within the LTC insurance market the past several years has been the creation of "hybrid" insurance policies. Although no one ever wants to collect on any of their insurance policies, Hybrid LTC policies address the concern of paying premiums for years and never receiving any benefit if LTC expenses are not incurred. These policies take many forms, but two common variations take the form of life insurance and a fixed annuity. With the life insurance version, a lump-sum payment buys a paid-up life insurance policy. If LTC coverage is needed, a monthly benefit is received that essentially converts the life insurance death benefit into a larger LTC benefit. The result is that as long as the policy remains in force, an owner will either receive the LTC benefit while living or their beneficiaries will receive the life insurance benefit.

The fixed annuity version of hybrid policies is similar to the above life insurance example except that the lump-sum payment buys a deferred annuity. If LTC coverage is needed, a monthly benefit is received that over time will cumulatively be much more than the initial lump-sum investment. However, if the insured has a change of heart in the future, the annuity can be cashed in to receive its value with interest, less any penalties. Upon death, if the use of the LTC benefit hasn't depleted the annuity's value, beneficiaries would receive the remaining amount.

What To Do Now

With the nation's median assisted living cost running over $39,000 per year, and over $77,000 for skilled nursing care with a private room, what steps should individuals be taking to address this issue? The first is to have family discussions regarding the risks. Second would be to get quotes on the estimated cost of coverage before more insurance companies exit the market.

If you, a family member, or friend would like to discuss this and obtain quotes, please feel free to contact us.