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Alternatives to Long-Term Care Insurance

The costs of long-term care can be overwhelming, potentially exhausting retirement income and savings. You may be thinking about buying long-term care insurance (LTCI) to help cover some of the potential costs of long-term care, but LTCI can be expensive, and if you do buy the coverage, you probably hope you never have to use it. A complete statement of coverage, including exclusions, exceptions, and limitations, is found only in the LTC policy. It should be noted that carriers have the discretion to raise their rates and remove their products from the marketplace.

The prospect of paying costly premiums for LTCI that you may never use might not appeal to you. But there are alternatives worth considering.

Self-insure

You could use your personal savings and retirement income to pay for long-term care expenses (self-insurance). While this option may be appealing, there may be some drawbacks. Depending on the type of long-term care, where that care is provided, and for how long, it's possible that you could run out of savings while still needing care. Also, using your own savings and income for long-term care costs may affect the financial well-being of a spouse or other dependents. And you may not have anything left to pass on to your heirs when you die.

Life insurance to pay for long-term care

One of the risks of buying LTCI is that you may spend thousands of dollars in premiums and never use the insurance. As an alternative, you may be able to use life insurance to help pay for long-term care expenses. For instance, some insurers offer policies that combine long-term care insurance with permanent life insurance. While these "combination" policies may differ, they generally offer a pool of money that can be used to pay monthly expenses associated with long-term care. If you don't use the policy for long-term care, then it will pay a death benefit to your designated beneficiaries if the policy is in force at your death.

Alternatively, you might be able to add an acceleration rider to your life insurance policy that will allow you to tap into (accelerate) your death benefit for long-term care expenses. Again, if you don't use the death benefit for long-term care costs, the policy will pay the death benefit to the beneficiaries you name in the policy. In any case, before buying a policy, you should have a need for life insurance and you should evaluate the policy on its merits as life insurance. Optional benefit riders are available for an additional fee and are subject to contractual terms, conditions, and limitations as outlined in the policy and may not benefit all investors. Any payments used for covered long-term care expenses would reduce (and are limited to) the death benefit and can be much less than those of a typical long-term care policy. Any guarantees are contingent on the financial strength and claims-paying ability of the issuing insurance company.

Medicaid

Medicaid is a joint federal and state government program that helps people with low income and assets pay for some or all of their health-care bills, including some costs associated with long-term care. Qualifying for Medicaid and covered services is based on federal requirements and eligibility rules, which vary from state to state. Generally, to be eligible for Medicaid, you must meet certain preconditions, which include income and asset levels that meet your state's eligibility requirements. You may need to exhaust your savings to qualify for Medicaid. Once the state determines that you're eligible for Medicaid, the state will make an additional determination of whether you qualify for long-term care services, based on whether you need assistance with personal care and other service needs, such as eating, bathing, dressing, toileting, and transferring (to or from a bed or chair).

Test Your Investing IQ

How much do you know about market basics? Put your investing IQ to the test with this quiz on stocks, bonds, and mutual funds.

Questions

1. What does it mean to buy stock in a company?

a. The investor loans money to the company

b. The investor becomes a part owner of the company

c. The investor is liable for the company's debts

2. Which of the following statements about stock indexes is correct?

a. A stock index is an indicator of stock price movements

b. There are many different types of stock indexes

c. They can be used as benchmarks to compare the performance of an individual investment to a group of its peers

d. All of the above

3. What is a bond?

a. An equity security

b. A nonnegotiable note

c. A debt investment in which an investor loans money to an entity

4. What kind of bond pays no periodic interest?

a. Zero-coupon

b. Floating-rate

c. Tax-exempt

5. What is a mutual fund?

a. A portfolio of securities assembled by an investment company

b. An investment technique of buying a fixed dollar amount of a particular investment regularly

c. A legal document that provides details about an investment

6. What is the difference between mutual fund share classes?

a. The investment advisers responsible for managing each class

b. The investments each class makes

c. The fees and expenses charged by each fund class

Answers

1. b. The investor becomes a part owner of the company. Stocks are often referred to as equities because they represent an ownership position. As part owners, shareholders assume both the potential financial risks and benefits of this position, but without the responsibility of running the company.

2. d. All of the above. A stock index measures and reports value changes in representative stock groupings. A broad-based stock index represents a diverse cross-section of stocks and reflects movements in the market as a whole. The Dow Jones Industrial Average, NASDAQ Composite Index, and S&P 500 are three of the most widely used U.S. stock indexes. There are also more narrowly focused indexes that track stocks in a particular industry or market segment.

3. c. A debt investment in which an investor loans money to an entity. Unlike shareholders, bondholders do not have ownership rights in a company. Instead, investors who buy bonds are lending their money to the issuer (such as a municipality or a corporation) and thus become the issuer's creditors.

4. a. Zero-coupon. Unlike many types of bonds, zero-coupon bonds pay no periodic interest. They are purchased at a discount, meaning the purchase price is lower than the face value. When the bond matures, the difference between the purchase price and that face value is the investment's return.

5. a. A portfolio of securities assembled by an investment company. A mutual fund is a pooled investment that may combine dozens to hundreds of stocks, bonds, and other securities into one portfolio shared by many investors.

6. c. The fees and expenses charged by each fund class. A mutual fund may offer various share classes to investors, most commonly A, B, and C. This gives an investor the opportunity to select a share class best suited to his or her investment goals.

Mutual funds are sold by prospectus. Please consider the investment objectives, risks, charges, and expenses carefully before investing. The prospectus, which contains this and other information about the investment company, can be obtained from your financial professional. Be sure to read the prospectus carefully before deciding whether to invest.

All investing involves risk, including the possible loss of principal, and there can be no assurance that any investment strategy will be successful. Generally, the more potential for growth offered by an investment, the more risk it carries.

The performance of an unmanaged index is not indicative of the performance of any specific security. Individuals cannot invest directly in such an index.

Because zero-coupon bonds do not pay interest until maturity, their prices tend to be more volatile than bonds that pay interest regularly. Interest income is subject to ordinary income tax each year, even though the investor does not receive any income payments.

The return and principal value of stocks, bonds, and mutual funds may fluctuate with market conditions. Shares, when sold, and bonds redeemed prior to maturity may be worth more or less than their original cost.

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Kickstart Your College Fund with a 529 Plan

If you're looking to save money for college, one option to consider is a 529 college savings plan. Created over 20 years ago and named after the section of the tax code that governs them, 529 plans offer a unique combination of features that have made them the 401(k)s of the college savings world.

How do 529 plans work?

529 college savings plans are individual investment-type accounts specifically made for college savings. People at all income levels are eligible. Plans are offered by individual states (you can join any state's plan) but managed by financial institutions designated by each state.

To open an account, you select a plan and fill out an application, where you will name an account owner and beneficiary (there can be only one of each), choose your investment options, and set up any automatic contributions. You are then ready to go. It's common to open an account with your own state's 529 plan, but there may be reasons to consider another state's plan; for example, the reputation of the financial institution managing the plan, the plan's investment options, historical investment performance, fees, customer service, website usability, and so on.

A plan's investment options typically consist of portfolios of various mutual funds that vary from conservative to aggressive in their level of risk. Depending on the market performance of the options you've chosen, your account will either gain or lose money, and there is the risk that the investments will not perform well enough to cover college costs as anticipated.

Benefits

So why bother going to the trouble of opening a 529 account when you could choose your own mutual funds (or other investments) in a non-529 account?

Federal tax benefits: Contributions to a 529 plan accumulate tax deferred, which means no income tax is due on any capital gains or dividends earned along the way. Later, earnings are completely tax-free when a withdrawal is used to pay the beneficiary's college expenses — a benefit that could be significant depending on how your investment options perform. States generally follow this federal tax treatment and may offer an income tax deduction for contributions. That's why it's important to know what 529 tax benefits your state offers and whether those benefits are contingent on joining the in-state 529 plan.

Contributions: You can contribute a lot to a 529 plan — lifetime contribution limits are typically $300,000 and up. Compare this to the small $2,000 annual limit allowed by Coverdell Education Savings Accounts. In addition, 529 plans offer a unique lump-sum gifting feature that some may find particularly compelling: Individuals can contribute a lump-sum amount of up to five years' worth of the $14,000 annual gift tax exclusion — a total of $70,000 in 2017 — and avoid gift tax if they make a special election on their tax return and avoid making any other gifts to that beneficiary during the five-year period. Married couples, such as grandparents who want to contribute to their grandchild's college fund, can make a joint lump-sum gift up to $140,000 that is tax-free.

College account on autopilot: For college savers who are too busy or inexperienced to choose their own investments or change their asset allocation over time, a 529 college savings plan offers professional money management. And by having a designated account for college savings, you segregate those funds and possibly lessen the temptation to dip into them for a non-college purpose — a scenario that may be more likely if you are using a general savings account to save for college. Finally, by setting up automatic monthly contributions to your 529 account, you can put your savings effort on autopilot.

Tradeoffs

Non-college use of funds: The federal tax benefits of 529 plans can be great if you use the funds for college. If you don't, then the earnings portion of any withdrawal is subject to federal income tax at your rate *and* a 10% federal penalty.

Changing investment options: With a 529 plan, you're limited to the investment options offered by the plan. Plans generally offer a range of static and age-based portfolios with different levels of risk, fees, and investment goals. (Age-based portfolios generally have a "glide path" where the underlying investments automatically become more conservative as the beneficiary approaches college age.) If you're unhappy with the performance of the options you've chosen, under federal law you can change the investment options for your *future* contributions at any time, but you can change the options for your *existing* contributions only twice per calendar year. This rule can make it difficult to respond to changing market conditions. However, also under federal law, once every 12 months you can roll over your existing 529 plan account to a new 529 plan without having to change the beneficiary, which gives you another option if you're unhappy with your current plan's investment options or returns.

Assets hit $266 billion mark

As of March 2017, assets in 529 college savings plans reached $266 billion, spread over 12.2 million accounts.

Source: Strategic Insight, 1Q 2017 529 Data Highlights

Before investing in a 529 plan, you should consider the investment objectives, risks, charges, and expenses, which are available in the issuer's official statement and should be read carefully. The official disclosure statements and applicable prospectuses — which contain this and other information about the investment options, underlying investments, and investment company — can be obtained by contacting your financial professional. Also consider whether your state offers a 529 plan that provides residents with favorable state tax benefits. As with other investments, there are generally fees and expenses associated with a 529 plan.

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How do the economic milestones of young adults today compare with prior generations?

If you're the parent of a young adult who is still living at home, you might be wondering whether this situation is commonplace. According to a recent U.S. Census Bureau study, it is: One in three young people (ages 18 to 34) lived in their parents' home in 2015.

The Census Bureau study examines how the economic and demographic characteristics of young adults have changed from 1975 to 2016. In 1975, for example, less than one-fourth of young adults (ages 25 to 34) had a college degree. Young adults in 2016 are better educated — more than one-third hold a college degree (or higher) — but student loan debt has made it more difficult for them to obtain financial stability, let alone establish homes of their own in their 20s.

More young adults in 2016 had full-time jobs than their counterparts did in 1975. In particular, young women ages 25 to 34 are experiencing economic gains, with more than two-thirds in the workforce compared with less than half in 1975. Young women today are also earning more money than they did in 1975 — their median incomes have grown from nearly $23,000 in 1975 to more than $29,000 in 2016 (in 2015 dollars).

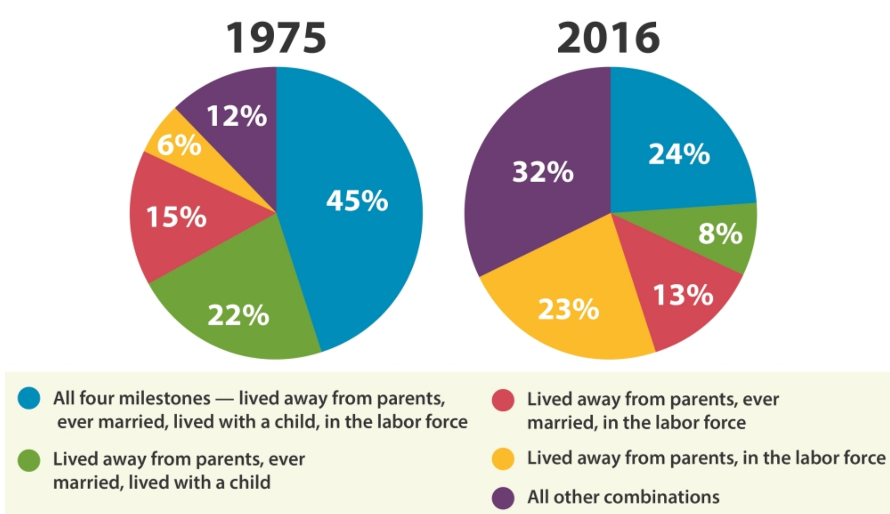
Despite the educational and economic advances that young adults have made over the last 40 years, many are postponing traditional adult milestones. In fact, a majority of young adults are not living independently of their parents. Of the 8.4 million 25- to 34-year-olds still living at home, one in four are not attending school or working. It's important to note, though, that this could be because they are caring for a family member or have health issues or a disability.

Compared to 40 years ago, the timing and accomplishment of milestones on the path to adulthood are much more diverse and complex today. To view the full report, visit census.gov.

Source: U.S. Census Bureau, "The Changing Economics and Demographics of Young Adulthood: 1975-2016," April 2017

Chart: Young Adult Milestones, 1975 vs. 2016

The following pie charts compare four common milestones of adulthood — getting married, having children, working, and living independently — achieved by young adults ages 25 to 34 in 1975 and 2016. The data indicates that the experiences of young people today are more diverse, with fewer accomplishing all four milestones in young adulthood. Instead, many young adults are delaying or forgoing some experiences (marrying and having children) in favor of others (living independently and gaining work experience).



Source: U.S. Census Bureau, "The Changing Economics and Demographics of Young Adulthood: 1975-2016," April 2017