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LTC Insurance As A Protection Tool

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Long-Term Care Insurance (LTCI) as a Protection Planning Tool

What is it?

Long-term care insurance (LTCI)

In return for your payment of premiums, a long-term care insurance (LTCI) policy will pay a selected dollar amount per day (for a selected period of time) for your skilled, intermediate, or custodial care in nursing homes and, sometimes, in alternative care settings, such as home health care. Because Medicare and other forms of health insurance do not pay for custodial care, many nursing home residents have only three alternatives for paying their nursing home bills: their own assets (cash, investments), Medicaid, and LTCI. For information about Medicare, Medicaid, and other programs that provide financial assistance with long-term care costs, see Coordination with Government Benefits.

In general, long-term care refers to a broad range of medical and personal services designed to provide ongoing care for people with chronic disabilities who have lost the ability to function independently. The need for this care often arises when physical or mental impairments prevent one from performing certain basic activities, such as feeding oneself, bathing, dressing, transferring, and toileting.

Long-term care may be divided into three levels:

- Skilled care--Continuous "around-the-clock" care designed to treat a medical condition. This care is ordered by a physician and performed by skilled medical personnel, such as registered nurses or professional therapists. A treatment plan is drawn up.
- Intermediate care--Intermittent nursing and rehabilitative care provided by registered nurses, licensed practical nurses, and nurse's aides under the supervision of a physician.
- Custodial care--Care designed to assist one perform the activities of daily living (such as bathing, eating, and dressing). It can be provided by someone without professional medical skills, but is supervised by a physician.

Tip: Note that the preceding terms may be defined differently by Medicare. For more information, see Medicare. For more information about LTCI in general (and for specifics on what to look for in a good LTCI policy), see Long-Term Care Insurance (LTCI).

How is LTCI useful as a protection planning tool?

The risk of contracting a chronic debilitating illness (and the resulting catastrophic medical bills incurred) is considered by many to be one type of risk best transferred to an insurance company through the purchase of LTCI.

A number of factors can increase your risk of requiring long-term care in the future. Naturally, your health status affects your likelihood of incurring a long stay in a nursing home. Indeed, people with chronic or degenerative medical conditions (such as rheumatoid arthritis, Alzheimer's disease, or Parkinson's disease) are more likely than the average person to require long-term nursing care. And because women usually outlive the men in their lives (if any), females stand a greater chance of requiring long-term nursing care. However, if you already have a primary caregiver (like a spouse or child), your likelihood of needing a long stay in a nursing home will be less--particularly if you're a man. Because the cost of long-term care can be astronomical and may exhaust your life savings, purchasing LTCI should be considered as part of your overall asset protection strategy.

Example(s): Irene is a 75-year-old widow with two children, Donald and Maria. Irene owns her condominium apartment and has $200,000 in liquid assets. After enjoying independence much of her life, Irene suffers a stroke and now needs help with such things as bathing, dressing, and eating. Donald and Maria look into home health care and discover that it will cost $1,500 per week (or $78,000 per year). The money that Irene had hoped to pass on to her children will instead be spent on expenses that may otherwise have been covered by an LTCI policy.

Tip: Bear in mind, also, that purchasing an LTCI policy while you are still healthy helps you to maintain control over your assets until such time as you actually require care. This stands in contrast to most Medicaid planning tools. Medicaid planning can also enable your nursing home bills to be subsidized by a third party (the state); however, it often involves transferring your assets promptly to avoid Medicaid penalties. With LTCI, there is no need for you to divest yourself of assets years ahead of time.

If you transfer some of your assets to your children while your LTCI is paying your nursing home bills, will you be subject to any penalties?

This depends on a number of factors, including the duration of benefits you selected in your LTCI policy. As mentioned, LTCI can be employed as part of your overall Medicaid planning strategy if your goal is to qualify for Medicaid at some point. If you are very wealthy and have no intention of ever applying for Medicaid, transferring your assets will make no difference. If you do envision receiving Medicaid assistance with your nursing home bills at some point, however, then transferring your assets within a few years of the time you apply for Medicaid could pose a real problem.

In general, if you transfer certain assets for less than fair market value within what's known as the look-back period, the state presumes that the transfer was made solely to qualify you for Medicaid. Therefore, the state will impose a waiting period or period of ineligibility upon you before you can start to collect Medicaid benefits. For more information about look-back periods, see Look-Back Period for Medicaid. Also, see Medicaid Penalties and Hardship Exceptions for additional information about ineligibility periods. Purchasing an LTCI policy allows you to transfer your assets to your loved ones after you enter a nursing home. If you select the proper duration of benefits provisions in your policy, your LTCI policy should cover your nursing home bills during the ineligibility period caused by the transfer. Thus, you can give your assets away, enjoy paid nursing home bills during the ineligibility period, and qualify for Medicaid when the insurance policy runs out.

Example(s): Marge is a 75-year-old widow who purchased a five-year LTCI policy a few years ago. Marge enters a nursing home, which charges $5,000 per month. At the same time, she transfers all of her assets (worth $250,000) to an irrevocable trust to qualify for Medicaid when the insurance benefits run out.

Example(s): Transferring certain assets into an irrevocable trust within 60 months of applying for Medicaid creates a waiting period or period of ineligibility for Medicaid, based on a formula. In Marge's case, the applicable waiting period would be 50 months (the amount she transferred divided by the cost of care in her area). Marge has no funds left to pay for her care, and Medicaid won't kick in until the 50 months have elapsed. Fortunately, Marge's LTCI policy will cover her nursing home bills during the ineligibility period. And, when her insurance benefits run out five years from now, she will qualify for Medicaid.

Tip: The Deficit Reduction Act of 2005 gave all states the option of enacting long-term care partnership programs that combine private LTCI with Medicaid coverage. Partnership programs enable individuals to pay for long-term care and preserve some of their wealth. Although state programs vary, individuals who purchase partnership-approved LTCI policies, then exhaust policy benefits on long-term care services, will generally qualify for Medicaid without having to first spend down all or part of their assets (assuming they meet income and other eligibility requirements). Although partnership programs are currently available in just a few states, it's likely that many more states will offer them in the future.

When can it be used?

You anticipate the need for long-term care, you wish to protect your assets for your loved ones, and you can afford to pay the premiums.

When buying an LTCI policy, you must consider not only whether you can afford to pay the premiums now, but also whether you'll be able to continue paying premiums in the future, when your income may be substantially decreased. Overall, however, purchasing LTCI is a wise move for older Americans who are financially comfortable (or who are at least able to afford the premiums), who wish to maintain control over assets for as long as possible, and who'd rather give away houses and other assets to loved ones.

Strengths

Subsidizes nursing home bills

Aging is inevitable, and the gradual inability to function independently is a great concern for many people. Although the prospect of entering a nursing home is a daunting one, equally frightening is the expense of nursing home care.

Purchasing an LTCI policy can give you some peace of mind; it's comforting to know that at least some of the cost of the first few years of nursing home care will be paid for. Moreover, because nursing homes may limit the number of beds available to Medicaid patients, you may have a wider choice of facilities if you're covered by LTCI than if you had to rely on Medicaid to pay for your care.

Allows you to protect your assets

Purchasing an LTCI policy allows you to transfer your assets to your loved ones after you enter a nursing home. The policy should cover your nursing home bills during the Medicaid ineligibility period caused by the transfer. Without such a policy, you'd either have to transfer your assets years before entering a nursing home or else deplete some of your assets by private-paying the nursing home during the period of Medicaid ineligibility caused by your late transfer of assets. The LTCI policy allows you to preserve your assets for your loved ones instead of spending them on nursing home bills.

Premiums may be tax deductible

If you purchase a tax-qualified LTCI contract, some or all of your LTCI premium may be deducted on your federal income tax return. Simply add the applicable portion of your premium to your other deductible medical expenses. To claim a deduction, the total of your medical expenses must exceed 7.5 percent of your adjusted gross income.

Tradeoffs

May be expensive

The cost of LTCI varies depending on your age, the benefits you choose, the insurer, and other factors. When buying an LTCI policy, you must consider not only whether you can afford to pay the premium now, but also whether you'll be able to continue paying premiums in the future (when your income may be substantially decreased).

Risk is involved

Paying insurance premiums each year in the expectation that you might (at some future time) require nursing home care is a risky move. There is always the possibility that you will remain healthy and able to function independently as you grow older. The money you pay out in premiums is money that you cannot give to your children or other loved ones, so be aware of the tradeoff.

May not be necessary if you'll qualify for Medicaid

If you have modest resources, very likely, you can qualify for Medicaid by spending down some assets and/or engaging in a little Medicaid planning a few years ahead of time. That way, you'll be able to avoid paying the high cost of premiums over a number of years.

How to do it

If you are interested in purchasing LTCI, there are a couple of steps you should follow:

Compare policies and check the financial security of the companies you're reviewing

You can determine the financial security of a company by reviewing its A. M. Best's rating along with the ratings of other services, such as Moody's or Standard & Poor's, at your local library. You should select a company that has received a rating of A or A+ from A. M. Best.

Review the policy's provisions carefully to ensure that it offers the features you require

There are a number of factors you should be concerned about, such as inflation protection, a full range of care (including home health care), and exclusions for pre-existing conditions.

Tax considerations

Income tax

Benefits you receive from a "qualified" LTCI policy are not taxable to you as income and are treated as excludable benefits received for personal injury and sickness to the extent that such benefits do not exceed a per diem limitation. However, benefits received from a policy that is not a tax-qualified one might be taxable as income.

Deductibility

Federal law allows you to deduct all or part of the premium paid for a tax-qualified (LTCI) contract. A portion of your LTCI premium should be added to your other deductible medical expenses. To claim a tax deduction, the total of your medical expenses must exceed 7.5 percent of your adjusted gross income.

> **Caution:** Not all long-term care contracts are tax-qualified--your policy must meet certain federal standards.
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> **Caution:** Starting in 2013, the 7.5 percent floor on itemized deductions for medical expenses increases to 10 percent. However, taxpayers age 65 and over are exempt until 2017.

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