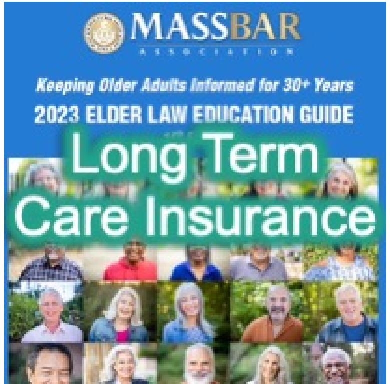

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CHAPTER 6

LONG-TERM CARE INSURANCE

Although most adults expect to remain healthy and independent throughout their lives, some develop chronic illnesses or conditions that require care over a prolonged period of time. Such care can range from assistance at home to more extensive care in assisted living facilities or nursing homes. Long-term care in any setting can be expensive. For example, the published average cost in Boston, Massachusetts, for a licensed home health aide is $31 per hour, for an assisted living facility is $81,816 per year, and for a semi-private room in a nursing facility is a staggering $172,824 per year, according to AARP's cost of care calculator.

Unfortunately, Original Medicare, Medicare Supplements, Medicare Advantage Plans and ordinary health insurance generally do not cover long-term care expenses. As a result of this gap in coverage, the cost of long-term care is often borne by the individual, who is forced to either privately pay or apply for MassHealth (Massachusetts Medicaid) coverage when the individual can no longer pay through their own financial resources. Due to the costs associated with long-term care and the strict asset requirements of MassHealth eligibility, many adults are seeking private long-term care insurance (LTCI) to help pay for these costs. LTCI helps pay for the cost of care in both private homes and private facilities to preserve the retirement nest egg, protect income streams and promote greater choices in care.

Unfortunately, many major insurers have stopped offering traditional LTCI to consumers due to many factors, including low return on investment in the current economy and miscalculated underwriting with more and longer claims than originally anticipated. In addition, some companies have increased premium rates substantially on existing policies, and companies still offering new policies have increased rates and tightened underwriting guidelines. The premium increases on existing polices, while bad news for older adults on fixed incomes, often come offered with what are known in the industry as "landing spots." These are options allowing the policyholder to pay the same premium but reduce policy benefits, such as the daily amount paid or the length of time the policy will pay. Several bills have been filed in the Massachusetts Legislature in the last few years seeking to impose limits on premium increases. As of December 2022, none have been passed into law. Unfortunately, the rate increases on Massachusetts LTCI policies have resulted in consumers seeking out-of-state group policies in an effort to obtain the protection, but at a lower cost. The problem there is that the Massachusetts Division of Insurance, which regulates Massachusetts LTCI policies, has no basis to regulate out-of-state policies. There is increasing pressure on policymakers to find a way to regulate policies for Massachusetts consumers buying LTCI products out of state, and to also find a way to limit premium increases on existing LTCI policies. In these difficult times, it is important to discuss options with trusted advisers (attorneys and financial planners) to review the situation. Also, please consider bringing family members into the conversation, as the children may be able to step up and pay the premiums to protect the parents' life savings and legacy. Be sure that a trusted person is named on the application as a person to be notified in the event of a failure to make a premium payment. Together, the older adults, children and advisers may well be able to find a creative and sustainable way to preserve the policy after an in-depth review of the family finances and available capital.

That said, as the industry has changed and policies have become more expensive, it may be advisable to give greater consideration to hybrid life/LTCI contracts and fixed annuities with LTCI provisions *(see Section E of this chapter)*. These can provide an alternative to traditional LTCI. This chapter will discuss both options in detail.

NOTE: In a MassHealth Fair Hearing decision from 2020, a hearing officer concluded that MassHealth's position that LTCI benefits constituted countable income in determining eligibility for community benefits under the Frail Elder Waiver was incorrect. The decision was not appealed by MassHealth and stands for the proposition that benefits paid from an LTCI policy that constitute repayment for incurred medical expenses are not countable income for Frail Elder Waiver eligibility purposes.

A. What Are the Benefits of Long-Term Care Insurance?

Modern long-term care policies can offer coverage for long-term care expenses not otherwise covered by medical insurance. Policies may provide a cash benefit or offer reimbursement for the cost of care up to the policy limits. Many policies today will cover care in the home and in facilities, providing flexibility for the insured older adult. As custodial care can be quite expensive, the insurance policy can provide the funds necessary to pay for care without exhausting assets or liquidating retirement plans. Oftentimes, liquidating retirement plans can create income tax issues, further accelerating the degradation of the older adult's nest egg. Furthermore, if care expenses exceed interest earned on the retirement assets, the older adult can rapidly reduce principal, leaving fewer assets available to generate future income or leave to loved ones.

A significant benefit to a traditional LTCI policy (in contrast to hybrid policies, described in Section E) is that Massachusetts law and MassHealth regulations allow for an exemption against a post-death claim by MassHealth for recovery of MassHealth benefits paid during the life of the policyholder. This exemption protects the primary residence (the "home") provided that the policy meets certain minimum requirements. The minimum policy benefits must be in place at the time the policy is purchased (the policy could certainly exceed these and still qualify), and must, under current regulations:

- Include coverage for nursing home care for at least 730 days;
- Pay at least $125 per day for nursing home care; and
- Begin paying benefits within one year, or have a substantial deductible.

If the policy did not have the minimum benefits in place when purchased, but due to inflation riders, the policy did have the minimum benefits in place when the person was institutionalized, an amendment to the exemption law passed with the state budget for 2020 allows the exemption to apply if, at any time after purchase, the policy has the minimum benefits in place (provided that the actions noted below are taken).

Note that having the exemption in place will not prevent a lien being placed on the home while the MassHealth applicant is alive and on benefits. This lien is intended to keep the home from being sold during the applicant's lifetime. If the home is sold during the applicant's lifetime, MassHealth will be entitled to recover any benefits paid for the applicant from the proceeds of the sale. However, upon the applicant's death, the exemption will prevent MassHealth from recovering those benefits when the home is then inherited by the applicant's heirs or other beneficiaries.

In addition to these basic provisions in the policy, the following actions must be taken to take advantage of the exemption:

1. **An application for MassHealth long-term care must provide that the applicant does NOT intend to return home.**
2. **The policy must still be in place at the time of institutionalization, and some minimum policy benefits must still be in place.** Be mindful that exhausting the benefits of a policy too soon could jeopardize the protection of the primary residence. The exemption only covers long-term care costs, such as nursing home or hospice costs. MassHealth payments for medical bills, such as hospitalization during life, are not protected. The exemption only applies to the person(s) who is, or are, the named insured(s) under the LTCI policy. For instance, if only one spouse has an LTCI policy, unless the policy covers both spouses, the exemption will not protect the house against the MassHealth costs of the spouse who does not have the policy.
3. **The home must not be sold during the time the applicant is alive. The home can be rented or otherwise occupied or not occupied, but if it is sold while the applicant is alive, MassHealth can recover benefits paid for the applicant from the sale proceeds.**

Because current hybrid LTCI policies allow for a return of premium paid by the policyholder during the term of the policy (you can get your cash paid for the policy back), they do not qualify for the exemption.

B. Potential Tax Advantages

For individuals who do not itemize deductions, no income tax deduction is available for LTCI.

Under IRC Section 7702B (a)(1), LTCI is treated as an accident and health insurance benefit. For those who itemize deductions, premiums may be deductible up to the eligible LTCI premium limit. For example, the individual who turns 71 before the beginning of 2021 can claim a deduction for up to $5,640 in long-term care premiums on their 2022 return, but the deduction, combined with other deductible medical expenses, may be deducted only to the extent it exceeds 7.5% of adjusted gross income.

Please note, policyholders who own a business may well have the ability to deduct a greater portion of the premium depending upon how the business is structured. Consult your tax adviser for more information.

When benefits are received, the reimbursement for care under a policy bought by an individual is not included in income (IRC Section 104(a)(3), 7702B(a)(2)), but if the contract provides for a per diem reimbursement, the exclusion is limited to $370 per diem in 2023. Different provisions apply to LTCI provided through an individual's employer. If the premiums paid are not includable in the employee's income currently, benefits will be taxed when received. If LTCI is provided through an individual's employer, and the premiums are includable in the employee's income when paid, benefits will not be taxed when received.

C. When to Purchase Long-Term Care Insurance

As with any other type of insurance, it is necessary for consumers to purchase LTCI before they need it. The main advantage of purchasing LTCI earlier in life is the reduced cost of premiums. For example, the premiums for a typical policy purchased for a female, non-smoker, age 55, would be approximately $5,466 per year. The same policy for the same person at age 75 would be approximately $14,928. Purchasing LTCI earlier in life, however, carries its own risks. First, LTCI is generally an unwise investment for those who cannot afford to pay the policy premiums for the remainder of their lives because policyholders often pay premiums for many years before receiving services. When retired and on a fixed income, managing premium payments may become difficult.

In addition, LTCI premiums can and do increase over time. Significantly, a prominent insurance company raised rates an average of 83% for federal employees on the plan. Most policies are guaranteed renewable, not non-cancelable, allowing the insurance company flexibility to raise premiums on a class basis. In fact, over the last decade, many carriers have had rate increases and, in many cases, increased rates by more than 40%. Such increases can make keeping the policy in place for older adults on fixed incomes very difficult. As was common throughout the last decade, states continue to approve rate increases. Companies are looking at ways to provide so-called "landing spots," amending policies so that benefits are reduced but premiums remain affordable.

D. What to Consider When Comparing Policies

- **Limits on Benefits**

LTCI policies generally feature both daily (expressed in dollars) and lifetime maximum benefits (expressed in days). Daily maximum benefits vary in terms of the amount of money the insurance company pays for each day or month a policyholder is covered by an LTCI policy. If the cost of care is more than the policyholder's daily or monthly benefit, the policyholder will need to pay the balance out of their own pocket. Please note, some insurance companies offer monthly benefit options rather than daily.

- **Length of Benefit Period**

LTCI policies cover different periods that measure the length of time policyholders can receive benefits from their policy. In Massachusetts, LTCI benefit periods may last as little as two years or as long as a lifetime. While lifetime policies offer the greatest security, many consumers cannot afford the premiums. For most individuals, four years of coverage is more than sufficient, as the average nursing home stay is approximately 2.5 years.

- **Length of Elimination Period**

LTCI elimination periods are waiting periods before benefits begin. Just as health insurance beneficiaries usually pay for a portion of their treatment out of pocket before they are eligible for benefits, LTCI beneficiaries must pay their long-term care expenses out of pocket during the elimination period. Policies may have no elimination period at all, or may have an elimination policy lasting a full year; typically, the longer the elimination period, the lower the premium.

- **Eligibility to Begin Receiving Benefits**

Insurers determine whether a policyholder is eligible to begin receiving policy benefits in different ways. The more common methods center on the policyholder's ability to perform various activities of daily living (ADLs). Insurers typically consider a policyholder's ability to eat, walk, move from a bed to a chair, dress themselves, bathe and use the bathroom. Ordinarily, a physician or licensed health care practitioner chosen by the insurer evaluates these skills, and a policyholder becomes eligible to begin receiving benefits when they cannot perform two or more ADLs. When comparing LTCI policies, the consumer should evaluate which ADLs a prospective insurer will consider. Consumers are prudent to consider only those policies that mention bathing specifically, since most older adults with long-term care needs require assistance with this task.

E. LTCI/Life Insurance Policy (Hybrids) Contrasted with Traditional LTCI

In recent years, many of the major insurers have exited the individual LTCI industry. With fewer providers and less competition, pricing has become less favorable. Because many older adults have concerns about long-term care issues, planners in the industry are developing alternatives. One such alternative is hybrid life insurance/LTCI combination policies. With life insurance/LTCI hybrids, insureds can accelerate access to the death benefit if they need long-term care. The named life insurance beneficiaries receive either the full death benefit if the long-term care benefits are not used, or what remains of the death benefit if the policy has been tapped for long-term care (less any service fee assessed per the insurance contract). These types of policies often offer guaranteed level premiums for life (providing stable costs), while traditional LTCI premiums are subject to change. Also, certain older adults with morbidity issues may be able to qualify for coverage in cases in which they are declined for LTCI, as many of the hybrid products are underwritten on life insurance (mortality standards), not long-term care (morbidity criteria).

Some contracts offer amounts greater than the death benefit to pay for long-term care, and even if the death benefit is exhausted by long-term care expenses, some policies offer a residual death benefit payable to beneficiaries. In most cases, however, with an accelerated death benefit, one cannot expect substantial insurance payouts for both an expensive long-term care episode and death. The consumer must continue to pay the life insurance premiums while receiving the accelerated benefit.

These policies do not offer joint benefits for spouses (as some so-called joint and survivor traditional LTCI contracts do), since each spouse would have their own individual policy.

Hybrid policy premiums generally are not tax-deductible, though benefits are usually received tax-free. Generally, standalone LTCI policies provide a wider range of benefit options than a combination policy. Also, hybrid policies may not have inflation protection, which would significantly erode the purchasing power of the benefits in the future. Consumers are encouraged to purchase a benefit that is sufficient to cover needs after accounting for potential increased costs of care later.

Insurance companies are also offering fixed annuities with embedded LTCI-like protections and whole life policies, which are funded by a one-time lump sum and provide LTCI benefits. Please note that these annuity-based options often come with less stringent underwriting requirements. With the recent, rapid increase in interest rates, these annuity-based policies are currently offering competitive rates and terms. These new contracts allow for policies with inflation options that may prove beneficial, as well as reports from the insurer outlining for the client the portion of the premium that may be

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tax-deductible. The policies are customarily funded with non-IRA assets. As these options evolve, and to determine which option to use, please be sure to discuss their applicability to your situation with your experienced and trusted adviser. Remember, as noted in Section A, that if a hybrid LTCI policy allows for a return of premium paid by the policyholder during the term of the policy (you can get your cash paid for the policy back), it would not qualify for the "home" exemption to MassHealth estate recovery.

CONCLUSION

Currently, LTCI plays only a small part in the overall long-term care financing system, covering only about 10% of all long-term care costs. However, as individuals live longer, the applicability of insurance options as an estate planning tool is likely to grow. Remember that it may not be affordable to purchase a policy large enough to cover the entire cost of care. In such cases, one may do well to employ a co-insurance principle in which the consumer purchases a policy that covers some of the risk, and commits to cover the difference (if care is needed) from assets or income. This way, the premium is more manageable, but the risk is still addressed.

As LTCI is a complex insurance product, consumers should gather information and begin discussing these options for payment of their long-term care costs with family members and experienced advisers well in advance of when they might need long-term care. One resource for general information that is very useful is "A Shopper's Guide to Long-Term Care Insurance," 2021 edition, put out by the National Association of Insurance Commissioners. This publication can be found at https://content.naic.org/publications?name=guide+to+long-term&field_publication_category_target_id=All.