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Where's the Beef in Long-Term Care Insurance Protection?

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Life insurance policies with living benefits, also known as hybrid or combo products, have emerged in popularity with a plethora of variations now available from insurance carriers. These products complement traditional long-term care insurance (LTCI), filling out the continuum of much needed retirement planning solutions. In this article, I will analyze the main long-term care product categories to show:

- Where's the Beef? Which insurance products provide most of the long-term care protection in the market today as a percentage of premium.[1]
- What the latest features and tax incentives available on traditional long-term care products are, including the Reverse Combo.
- How traditional LTCI and life combo products fit in your tool kit of customer solutions.

THE SPECTRUM OF LTCI PROTECTION

There is a spectrum of insurance products that address long-term care protection ranging from pure LTCI to nearly pure life insurance. We can measure the amount of long-term care protection that they provide by estimating what portion of the premium price tag is expected to be paid for long-term care relative to acceleration of the life insurance customer's death benefits.

Insurance premiums are also paid over different schedules ranging from one large single premium to smaller annual premiums over the policyholder's lifetime. Equivalent recurring annual premium for single pay products can be estimated by dividing the single pay amount by twelve.[2]

The 2015 industry LIMRA surveys for traditional LTCI and combo long-term care provide total sales figures for each segment. Figure 1 summarizes the data from the LIMRA study after adjusting single pay premium as described above.

Traditional LTCI: As the purest form of long-term care coverage, virtually 100 percent of premiums are dedicated to paying long-term care benefits. Traditional LTCI allows consumers to leverage the most long-term care protection per premium dollar.

The newest traditional product on the market provides two people residing in the same household LTCI coverage under a joint policy. As an example of leverage provided by traditional LTCI purchased today, both individuals would be covered for up to a total of $438,000 of tax-free benefits for a single premium of $29,000 if both are age 50 or $38,000 if both are age 60. $438,000 is equal to the total benefit pool available using the sample benefits selected: 3 year benefit period x $200/day x 365 days x 2 people.

Lifetime benefits on this product cost exactly double what three year benefits cost. Most traditional LTCI products are purchased with a 90 day waiting period "deductible." Inflation protection is also very common and desirable in the higher-end market to keep up with the cost of care over time. Some carriers have gravitated toward more limited benefits or providing short term care, so that individuals can get at least some coverage at a lower target premium. However, a new carrier has emerged with popular high-end features such as lifetime benefits, 10-pay and single pay options.

Many people are surprised by the amount of leverage still available on traditional LTCI. It's all a matter of perception. Ten years ago, prices were half of what you see today for the same benefits, with rate increases slowly bringing them back to today's rate adequacy.

Insurance carriers have learned the hard way from legacy products that traditional LTCI can only be offered to healthy individuals who plan well in advance of the need. Policyholders have confirmed that the coverage has tremendous value based on customer retention at higher renewal rates than any other insurance product. In addition, customers' claim satisfaction rates are likewise favorable. Couples get the best deal because they subsidize the cost by taking care of each other before tapping into their benefits. The good news is that new products sold today have a record low likelihood of requiring future rate increases based on a recent Society of Actuaries study.[3]

The Beef: There were a total of 104,332 traditional LTCI policies sold in 2015, accounting for $261 million of lifetime recurring premiums. The first single pay alternative in many years recently became available late in 2016.

The ideal client is using traditional LTCI as a leveraged way to protect assets in retirement. While the hope is that the benefits will never be needed, the coverage provides a safety net for a catastrophic event. This concept is reminiscent of term life or disability income insurance and can be thought of as the next phase for retirement planning.

It is estimated that the total target market is over 10 million for those in the right age range who are currently healthy with assets to protect, and do not already have a long-term care plan in place.[4]

Traditional LTCI has many built-in advantages provided by the government to incentivize long-term care planning. Among the most popular are:

- Traditional LTCI benefits are generally received tax-free.
- LTCI premiums may be fully tax deductible for business owners with a full or partial tax deduction for the employee, and without discrimination requirements.
- Traditional LTCI premiums can be paid directly using non-qualified annuity or non-qualified life insurance cash values through a tax-free 1035 exchange.
- Pre-tax HSA funds can be used for LTCI premiums.
- Public-Private LTCI partnership programs are available protecting assets in Medicaid situations.

TRADITIONAL LTCI—REVERSE COMBO

A new concept released in 2016 that has reinvigorated interest in the traditional LTCI product is offering a rider to provide a return of premiums (ROP) paid back to the policyholder upon death and an option to surrender the policy for a return of 80 percent of the premium. I call this feature the reverse combo because it offers a life insurance-type benefit on an LTCI-based product instead of a long-term care rider on a life insurance based product.

The reverse combo provides greater long-term care coverage and less life insurance than life combos with the wide flexibility of traditional LTCI designs. There is also a version of the policy that provides both ROP and all long-term care claims without offset. The product provides about 60 percent of premiums dedicated to long-term care protection. Often advisors lead with the reverse combo design and then find customers choosing lifetime benefits in lieu of ROP for roughly the same cost.

LIFE INSURANCE WITH LTC EXTENSION OF BENEFITS (EOB) RIDERS

The next product in the spectrum of providing long-term care coverage is life insurance with an acceleration of the death benefit upon meeting the long-term care trigger. Once the cash value is exhausted, the policy provides an extension of benefits (EOB) to continue to pay long-term care benefits up to a specified benefit period. Another way to think of this is that, for example, the first two years is the long-term care deductible where the customer is spending down the life insurance death benefits before the extended long-term care coverage kicks in.

This funding mechanism results in an estimated average of 27 percent of premiums dedicated to long-term care protection with a range of about 10 percent to 40 percent depending on how much EOB and inflation protection is purchased.

Life insurance with EOB inhabits an important part of the long-term care spectrum because it offers a variety of niches where traditional LTCI products have receded:

- Alleviates concerns about rate increases on traditional LTCI products that do not have single premium or 10-pay options;
- Allows life insurance asset accumulation with account value growth and the ability to take out loans;
- Offers effectively a longer deductible than can be provided on traditional LTCI; and,
- Allows individuals with some health conditions no longer acceptable for traditional LTCI to obtain coverage.

The Beef: There were a total of 25,471 life with EOB rider policies sold in 2015, accounting for $193 million of lifetime recurring premiums. Applying 27 percent of those premiums as covering long-term care protection results in $52 million of long-term care protection sold in 2015.

LIFE INSURANCE WITH LTC ACCELERATION OF BENEFITS (AOB) RIDERS

Life insurance with acceleration of benefits (AOB) is a more limited version of the EOB rider, because only the life insurance death benefit can be accelerated for long term care. Once that death benefit is exhausted, no more long-term care coverage is provided. A multitude of carriers offer versions of this feature on a variety of life insurance products because the cost of the AOB rider is on average only about seven percent of the premium[1]. The popularity of this product is part of the trend to expand the availability of benefits for asset based life insurance and can be done at relatively low cost for the carriers. The products with these features in most cases utilize life insurance underwriting, which then provides access to this coverage for individuals with health conditions who might not have otherwise qualified for traditional LTCI or life insurance with EOB riders.

The Beef: There were a total of 109,615 life with AOB rider policies sold in 2015, accounting for $388 million of lifetime recurring premiums. Applying seven percent of those premiums as covering long-term care protection results in $27 million of long-term care protection sold in 2015.

LIFE INSURANCE WITH CHRONIC ILLNESS RIDERS

This product is a cousin to the life with long-term care rider concept in that it provides a lump sum percentage of the life insurance death benefit for an individual with a permanent end of life need. The rider can be added for an average of three percent additional premium because the acceleration period is shorter. The acceleration period is shorter because policies using chronic illness benefits are likely to die sooner, so the life benefit would otherwise have been paid a little sooner for these claimants than for non-chronic illness claimants. Underwriting is simplified and agents need not be specially trained in long term care. However, the product cannot be advertised as long-term care coverage nor does it have the regulatory protections of long-term care products.

The Beef: There were a total of 94,154 life with chronic illness rider policies sold in 2015, accounting for $533 million of lifetime recurring premiums. Applying three percent of those premiums (which in some cases is presented as a 3% reduction in coverage) as covering "long-term care" protection results in $16 million of long-term care protection sold in 2015.

WHERE'S THE BEEF?

Life insurance with AOB and chronic illness riders represent the fastest growing segment of the long-term care continuum with more carriers offering these features every year. Similarly, the number of traditional LTCI carriers has been decreasing although a new carrier entered the LTCI market during the summer of 2016 for the first time in nearly a decade. Surprisingly, despite these trends, nearly 75 percent of long-term care protection still originates from traditional LTCI and for good reason. Traditional LTCI is still a highly desirable product from a leverage and tax advantaged standpoint and fulfills a clear purpose. Healthy customers leading with the need for long-term care protection will get the most value from traditional LTCI and life with EOB riders. Similarly, customers primarily needing life insurance now have a multitude of options available to them and can find policies that fill a variety of needs especially if there are health concerns. ■

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ENDNOTES

1 Based on 2015 Year End LIMRA Surveys on LTCi Standalone and Combo LTC

2 Calculated as follows, using slide 4 of *https://www.soa.org/Files/Pd/2016/las/pd-2016-05-las-session-65.pdf: Single Pay /* (Equiv Recur Premium – Recurring Pay)

3 *https://www.soa.org/Files/Sections/ltc-pricing-project.pdf*

4 Estimated using census data to determine the affluent population in the target age range, less the population that already has LTC coverage.