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LONG-TERM-CARE INSURANCE JUST GOT CHEAPER

But Beware of the Gaps

Insurance that covers bills for home care, assisted living and nursing homes sounds like a great idea—the problem is that it tends to be costly.

Annual premiums for long-term-care insurance typically are several thousand dollars a year, more than most people are willing or able to pay. Insurance companies now offer a solution—policies that cost 15% to 25% less.

Downside: These relatively inexpensive long-term-care policies have limitations that can greatly curtail their usefulness. Insurance agents sometimes fail to fully explain these limitations to customers, many of whom will not discover that there are serious problems with their policies until they make claims.

Bottom line: A reduced-cost long-term-care insurance policy could prevent financial ruin should you require an extended stay in a nursing home, but be wary of policies that eliminate too much. *What to watch for in stripped-down long-term-care insurance...*

■ **Insufficient inflation protection.** The cost of long-term care has been rising steadily. Traditional long-term-care insurance policies offer a 5% compound inflation rider to protect policyholders from these increases. Stripped-down policies might provide price-increase protection linked to the economy's overall rate of inflation, but price increases for long-term care have historically risen at a much faster pace. Some policies offer no inflation protection at all. Insufficient inflation protection can balloon into a major problem over time.

Some might argue that limited coverage is better than none at all, but this is not necessarily true. Most retirees would very quickly run through their savings paying the remaining out-of-pocket costs. These policyholders will wind up depending on Medicaid to pay their nursing home bills, the same as if they had had no coverage. It's better to skip such a policy.

Warning: Insurance companies sometimes include 5% *simple* annual inflation protection in their policies rather than the standard 5% annual *compound* protection. You might not notice the difference until it's too late. With 5% simple interest inflation protection, coverage increases by 5% of the *original* coverage amount each year—$200 this year increases by $10 a year, reaching $400 in 20 years. For true 5% inflation protection, previous inflation adjustments must be factored in when additional adjustments are made, a system known as compound interest. With compound interest, $200 this year rises to $531 by year 20.

Verdict: Purchasing a policy with less than 5% compound annual inflation protection is a false economy. Insist that the insurance agent show you exactly where in the policy the inflation protection is described, and make sure the phrase "compound inflation" is used.

■ **Longer elimination periods.** Long-term-care insurance traditionally kicks in after 30 days of care is financed out of pocket. With a stripped-down policy, this "elimination period" might be 90 days, 100 days or longer.

Example: John Hancock Leading Edge policies have 100-day elimination periods.

Verdict: Long elimination periods are a reasonable way to reduce the cost of long-term-care insurance by 10% to 25%—*if* you can afford to pay the required number of days of care out of pocket.

■ **Lower daily benefits.** Low-end policies might offer a maximum daily benefit far below what nursing homes charge—perhaps $100 per day, while the average nursing home actually costs more than $200.

Warning: Nursing home costs vary greatly by region. Even $200 per day in coverage is not enough if you retire in, say, Manhattan or San Francisco.

Verdict: Policies with low daily benefits may be a reasonable option for those who do not have sufficient income to finance a more comprehensive policy *and* who expect to have between $300,000 and $1 million in retirement savings, not including equity in the home. Such people have significant assets to protect, but

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not so much that they could easily pay for an extended nursing home stay out of pocket.

■ **Fewer years of coverage.** Most long-term-care policies will pay for at least five years of care. Some pay for care for as long as the policyholder needs it. Low-cost policies might set the limit at just two or three years.

Verdict: The typical stay in a nursing home lasts less than three years, but we don't buy expensive insurance to protect us from the typical—we buy it to protect us from potentially ruinous financial risks. Evaluate your financial situation carefully before considering a policy that offers less than five years' protection.

■ **High copayments.** Some stripped-down long-term-care policies require policyholders to pay a significant percentage of the cost of their care on an ongoing basis.

Example: Genworth Cornerstone Advantage policyholders must pay 20% of their cost of care. The policies can cost much less than other policies.

Verdict: High-copay policies, like low-daily-benefit policies, are appropriate only for those who cannot afford more comprehensive policies and who will have between $300,000 and $1 million in retirement savings.

■ **Shared policies.** Insurance companies offer discounts of perhaps 20% or more when married couples "share" a policy, essentially purchasing a certain number of years of long-term-care coverage that can be divided up between the spouses.

Verdict: Shared policies are a smart idea for married people. They offer lower rates and the flexibility to apply coverage to either spouse. These policies provide coverage if one spouse requires an extended nursing home stay…or if both spouses require short or moderate-length nursing home stays. *Trap:* They cannot provide complete coverage if *both* partners require extended nursing home stays, but the odds against this are steep. If it does occur, Medicaid is a viable way to pay additional nursing home bills—with both partners already in nursing homes, preserving the couple's assets is less of a priority. ■■