Using Life Insurance to Pay for Long Term Care

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There is no doubt the cost of Long Term Care today and especially in the future represents a significant risk to most families' savings and retirement, since we are living longer, and since this type of care is not covered by regular health insurance, Medicare or Medicare Supplement insurance.

Long Term Care is also called *custodial care*, and is defined by IRS Code 7702B as it relates to tax-qualified Long Term Care insurance. Almost all Long Term Care Insurance policies written after 1996 are tax-qualified, meaning the benefits are not subject to tax, and some or all of the premiums may be tax deductible.

Specifically, Code 7702B spells out the qualifications or "triggers" under which benefits can be claimed under a Long Term Care Insurance policy. These qualifications are either…

- *Your doctor's expectation that you will need assistance with at least 2 of the 6 Activities of Daily Living (dressing, bathing, eating transferring, toileting, continence) for at least 90 days - or –*
- *Your doctor's expectation that you will need substantial supervision due to a severe cognitive impairment (Alzheimer's, etc.)*

Roughly half the claims with LTC insurance today are for cognitive issues, i.e. Alzheimer's and other forms of dementia. One exclusion, however, would be mental or nervous disorders caused by *intentional, self-inflicted* alcohol or substance abuse.

Traditional, stand-alone Long Term Care Insurance is the most common due to its relatively low cost (especially for couples, married or not), but life insurance can also be an option.

Here are a few ways life insurance can help…

Hybrid Life Insurance

Life insurance in the U.S. has been around since the founding of this country, but only recently in the last 15 years or so have hybrid or combination policies been available.

Hybrid policies are built on a "chassis" such as Universal Life insurance, Whole Life insurance or sometimes an annuity and come with a "rider" (option) for Long Term Care. Almost all hybrid policies today are combined with permanent life insurance, and as such have a *tax-free death benefit*.

The LTC rider is an option that is usually only available when applying for the life insurance policy or annuity, not afterward.

The rider allows the insured to draw down the death benefit for qualified Long Term Care expenses, but it can also include an additional pool of Long Term Care benefits (for an additional premium), if the death benefit has been fully exhausted and care is still needed.

If the hybrid policy is paying for Long Term Care, and the insured dies before the all the death benefit has been exhausted, whatever balance remains is paid to the insured's beneficiary(ies) or estate. If Long Term Care is *never* needed, then upon the insured's death, his or her beneficiaries receive the full death benefit.

Originally, this product was a single (lump sum) premium only, but today companies also offer custom payment terms such as 5 years, 10 years and even annual lifetime payments.

The biggest advantages of the hybrid policy for the insured are that it a) avoids rate increases (typically seen with traditional LTC insurance) and b) provides a "certainty" that the insured and/or his or her family will recover the premiums, one way or the other, and tax-free, too.

Additionally, the single-premium hybrids have a Return of Premium rider that allows the insured to cancel his or her policy (usually after a couple years) for a full refund of the initial premium (less any claims paid).

Expense Recovery

Without traditional or hybrid Long Term Care Insurance, chronically-ill individuals or their family members often tap into income or savings to pay for Long Term Care, and this can represent a serious blow to families. However, if the chronically-ill person has a life insurance policy, upon his or her death, the beneficiaries can use the death benefit proceeds to "recover" some or all of the expenses incurred while their loved one was alive.

Life Settlement

Another option is to sell your life insurance policy in the Life Settlement market and use the cash proceeds to pay for Long Term Care.

The cash received from the sale and the way it is received are determined by the insured's age, gender and health, in other words, his or her life expectancy. *The shorter the life expectancy, the bigger the payout. The longer the life expectancy, the smaller the payout.* However, the total cash payout is often just a fraction of the death benefit.

This can be a useful option when the insured has a life expectancy of 2-3 years, but only after all other possibilities have been exhausted, including stand-alone Long Term Care Insurance, Life Insurance with a Long Term Care rider, Veteran's benefits and Medicaid.

One common mistake I see among people in their late 50s and 60s is they will drop their term life insurance before picking up their Long Term Care Insurance. As they approach retirement and their kids are grown, they rush to cut "unnecessary" premiums. Who wouldn't? But around this time, health issues tend to crop up, and often these health issues make it difficult, expensive or even impossible to get Long Term Care Insurance OR even Life Insurance.

So, a word of caution… it's best to look into and decide (yes or no) on Long Term Care Insurance BEFORE giving up your life insurance policy. If Long Term Care Insurance is not attainable for health reasons, then keeping that life insurance policy might be the only thing that saves you from spending tens or hundreds of thousands of dollars of your own hard-earned money down the road on something you never expected… two or three or more years of Long Term Care.

If your life insurance policy is a term policy and about to "expire" in a year or even a few years from now, almost all term policies allow conversion to a *permanent* life insurance policy (albeit at a higher premium) with NO UNDERWRITING, but only up to a certain date or age. The younger you convert your term policy, the lower the premium will be on the new permanent policy. This is called a "Term Conversion", and any experienced life insurance agent can help you get a quote and assist in the conversion process.

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