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Does Long-Term Care Mix With Life Insurance?

By KELLY GREENE

With long-term-care insurance premiums climbing by double digits and several insurers exiting the business in the past two years, many families are turning to an alternative: using life insurance with long-term-care benefits.

Eric Palma

But buyers of life-combo products are facing sharp premium increases—or trimmed benefits—in the coming months, thanks to a new accounting rule that affects the type of life insurance often used with long-term-care riders. People who already hold such policies might see their premiums rise as well.

Life insurance policies with long-term-care riders, known as "hybrid" products, have taken off in the past few years, as reported in last week's Weekend Investor. Sales jumped 56% last year, according to Limra, an industry-funded research group.

One reason is that they overcome one of the biggest stumbling blocks for buyers of long-term-care policies—writing a big check for a product you hope you will never use. By pairing life insurance with long-term-care benefits, you can lock in a payout for your spouse, children or other heirs, even if you don't use the long-term-care benefit.

As with traditional long-term-care insurance, hybrid policies typically kick in when the policyholder needs help with two "activities of daily living," such as eating or bathing. They either pay you a set amount each month or reimburse long-term-care expenses, but they might not cover care for cognitive loss and could have waiting periods.

"Be careful, because not all long-term-care benefits are created equal," says Katherine Lanious, president of Capital Insurance Insights, a life-insurance wholesaler in Naples, Fla.

The living benefits in these hybrid products are typically limited to the amount of the death benefit. That can be much less than those of a typical long-term-care policy, which generally covers all qualified expenses up to a maximum amount for two to five years. The long-term-care benefits can add as much as 20% to the basic premium of an insurance policy, insurers and planners say.

There is another big unknown: Many hybrid products have been around for only a few years, so the people selling them have less experience with clients who have tried to collect the benefits.

On Sept. 12, the National Association of Insurance Commissioners revised an actuarial guideline, effective in January, to ensure appropriate reserves for the type of life insurance often used with long-term-care riders—"universal life" policies with secondary guarantees. Such policies provide permanent coverage throughout your lifetime.

By contrast, "term life" insurance has level premiums for a set time period, after which premiums could rise if you want to continue the coverage. Agents selling such coverage generally are paid a commission by the insurer, and there are surrender charges for universal-life policyholders who cash in their coverage early.

Insurance companies haven't yet said how much premiums will go up, but wholesalers and brokers are coming up with their own predictions. Estimates range from 5% to 20%, according to several analysts and insurance executives.

"For any of the guaranteed policies, you're going to see the increase," Ms. Lanious says. "They haven't released the figures yet, but it's likely it will be 25% on average."

A few carriers have told Joseph Lucey, president of Secured Retirement Advisors in St. Louis Park, Minn., that they are expecting 5% to 10% increases "across the board" next year, he reports. "There are going to be people who wait till next January and wish they'd bought the insurance earlier," he says.

Irvin Schorsch III, president of Pennsylvania Capital Management, a wealth-management firm in Jenkintown, Pa., says he has been filling in clients on the fence about long-term-care coverage since learning about the new reserve requirements and advising them to consider buying coverage this year.

Steve Katz, owner of three restaurants outside Philadelphia and one of Mr. Schorsch's clients, is researching the hybrid policies now and, in light of possible premium increases, plans to buy one before Dec. 31, he says.

"I turned 55 this year, my wife turned 55 a couple weeks ago, and we just had our first grandchild," he says. "It's definitely in the forefront of our minds right now."

Even with prices going up, some advisers are finding strategic ways to use the life-combo policies, including the following:

Designating one pot for long-term care. Mr. Lucey says he often recommends the policies for clients who already have enough savings to cover long-term care because they can use the life insurance to create a tax-free bucket. That way, "your family's not out there trying to figure out which asset to liquidate first to pay it," he says.

"When families don't make any plans for long-term care, all of a sudden they're in a situation where they're liquidating IRAs and paying huge taxes, and the markets aren't always going to work on their side," Mr. Lucey says.

Avoiding future premium rises. Charles W. Bruton Jr., an investment adviser in Downingtown, Pa., says he quit recommending traditional long-term-care insurance policies to clients several years ago because the premium increases were becoming more common, and more significant. One client's long-term-care insurance bill climbed more than 45% last year, he says.

With the life-combo products, the rates are guaranteed to stay the same. "The beauty of it is you don't have to worry about the insurance company coming back and raising the premiums," Mr. Bruton says.

Estate planning. If the long-term-care rider is what is called an "indemnity" benefit, not an expense reimbursement, you generally are allowed to put the insurance policy in an irrevocable trust and still use the accelerated death benefit for long-term care.

Then, when you die, your heirs get whatever benefit is left tax-free, and it isn't counted as part of your estate.

You have to have the indemnity rider to do this, Ms. Lanious says. With an indemnity plan, the benefit is paid to the owner of the policy, which is the trust. If the benefit is paid directly to the insured person, the trust could be disqualified.

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