Facing up to the costs of long-term care

CNN Money

NEW YORK Money Magazine) — Some insurance decisions are easy. Take life insurance. You know you need it to replace the income your spouse and kids would lose if you died. Insurers don't have much leeway to dispute claims for death benefits because "deceased" is a pretty definite condition.

After you decide how much to buy, you can compare various term policies, see which are the cheapest and most practical, and buy the least expensive one that fits your needs.

Long-term-care insurance seems just as simple – at first. Its purpose is to protect you from a very real, very scary possibility – that one day you might be unable to take care of yourself. If you wind up in a nursing home or need extensive assistance at home, you will face catastrophic costs that could eat up every dollar you ever earned.

The average daily rate now for a stay in a nursing home is $183, or nearly $67,000 annually, an expense that after a few years would sink all but the very well-off. And prices will go up. If they rise a bit faster than inflation, by 2026 the daily rate could hit $486 a day, or $177,000 a year.

Insurance looks like the solution – the customary mechanism for sharing a potentially devastating financial risk with thousands of other policyholders. And it can work.

Teetering on the edge of insurance

Take the case of David and Kristi Schubbe of suburban Minneapolis. Starting in 2002, when she was only 61, Kristi became forgetful and had difficulty performing routine tasks such as following familiar recipes. After three years David became unable to care for her, even with a home aide. He found a nearby nursing facility that specializes in Alzheimer's patients.

"I knew when I saw it, this is where I want my Kristi," he says. The bill is $5,400 a month, but their long-term-care policy, which the Schubbes bought in 2001, covers the entire expense. Insurance helped make the tragedy manageable.

Says David: "It took the financial element out of when to go [into a home], where to go and how to do it."

What if the Schubbes had not purchased insurance? Medicare would not have helped because it doesn't pay for long nursing-home stays. Medicaid might have paid – about 43 percent of nursing home residents eventually qualify – but only after David had exhausted much of the couple's assets. Transferring assets

to relatives is almost impossible because the government penalizes you for having given money to others within the previous five years.)
States set strict limits on how much money the spouse not in care can retain. In Minnesota, for example, the spouse can keep half of the couple's assets up to about $100,000, plus their home with as much as $500,000 in equity).
Finally, some nursing homes will not accept Medicaid, so relying on it would have diminished the Schubbes' options. Long-term-care insurance, however, has plenty of catches.
First, you may pay thousands of dollars in annual premiums, possibly for decades, even after retirement when you have a smaller income; if you stop paying, you can lose your coverage and everything you put in.
Second, you have to look far into the future and guess what kind of care you will need and how much it will cost. Most disturbing, perhaps, some insurers' business practices have recently cast doubt on how much you can trust them to hold up their end of the deal.
In the past few years many policyholders have faced exorbitant rate increases – sometimes 40 percent or more. And a rash of lawsuits complain that insurers are delaying or unfairly denying the claims of some of their most vulnerable policyholders.
A Chinese menu of benefits
Decent health insurance will pay for anything from a flu shot to triple-bypass surgery. Long-term-care insurance offers no such blank check.
"You have to define long-term care the way your contract defines it, not by the way you might actually need it," says Robert Friedland of the Georgetown University Long-Term Care Financing Project.
A policy pays a set daily rate for a nursing home stay or other care, say $100 or $150. The higher the rate you select, the higher your premium. And if the day rate increases to $250 by the time you need care and your policy specifies $100, you're on the hook for the rest.
Some policies will raise the benefit with inflation, some won't, and the formula differs from policy to policy. How long will the policy pay? For your lifetime, if you can afford such coverage, or for the number of years you select.
To qualify for coverage, you must typically be cognitively impaired or unable to perform a certain number of activities of daily living ADLs), usually two. Some policies offer coverage only for home care; others cover nursing home stays plus adult day care or assisted living. Some policies waive premiums while you're in care; others keep charging you.
To choose a policy, buyers must sort through enough permutations and combinations – each with its own price tag – to do a Chinese restaurant proud.

The risk of rate hikes
The Schubbes were in good health when they bought, so they were able to get coverage for themselves for a $3,000 annual premium. Those who have health problems like diabetes, cancer or arthritis will pay higher premiums. Or in the worst case, they might not qualify at all.
Insurance sales people point out that you can lessen that risk by purchasing a policy when you're young. The premiums would likely be low, and most insurers promise that they will not hike your rates because of age or health problems. But insurers can still raise rates for other reasons and often do. They may have to pay more claims than they expected, for example.
Lester Watts, 72, and his wife Judy, 61, of Clive, Iowa bought a long-term-care policy from Equitable Life & Casualty two years ago. Their premium was $280 a month. Within the year, however, the insurer won the right from the state to raise its rates. The couple's premium would rise to about $360 a month. "It all smacks to me of a bait and switch," says an angry Lester Watts.
The insurer says that new policyholders like the Wattses were notified at least a year before the rate increase went into effect, giving them time to cancel. Rather than do that, however, the Wattses have decided to reduce their benefits to keep their premium level.
Prices that keep heading skyward could eventually force you to drop the policy. At that point you may lose your coverage and all the money you paid. You'll be hard put to find a cheaper policy elsewhere, since you are older now than when you first bought, and a worse insurance risk.
"You are more or less married to an insurer and you can't really change," says John Rother, director of policy and strategy for AARP, the retirees' lobby. AARP also markets a long term-care policy from MetLife.)
Rate hikes may slow. Regulation is improving, and Jesse Slome of the American Association for Long-Term Care Insurance argues that insurers have learned from experience how to price policies more accurately from the start. That's plausible. But you may not know for decades whether they're right.
Will you get paid?
If you buy long-term-care insurance, you are trusting that your benefits will be paid at some point long into the future. But this year news began to surface, both in the New York Times and the Des Moines Register, that seniors around the country were having difficulty collecting claims.
Consumer advocates and plaintiffs attorneys argue that long-term-care insurers have an even stronger financial incentive to take a hard line with their customers than, say, auto or life carriers.
"Old people don't last long; sick people don't fight hard," says Frank Darras, a California lawyer who has sued insurers over unpaid long-term-care claims. A claim, of course, is a judgment call, but it's almost everybody's judgment but yours.

In September, Louis Heldenbrand turned out for a public meeting of insurance regulators in Des Moines to tell of his unsuccessful efforts to help longtime neighbor Dorothy Parker, 88. Five years ago she bought $100-a-day coverage from Bankers Life & Casualty. After breaking her pelvis in December 2006, Parker, who weighed just 88 pounds at the time, checked into a nursing home.

Despite her condition, Bankers Life denied payment in June, saying she did not meet the policy's definition of "chronically ill." According to a claim document from Parker's nursing home, signed by her doctor, Roger Hansen, she was incapable of performing only one ADL. Her policy requires her to be deficient in two.

With help from a lawyer, Parker has appealed. Hansen, who says he has since looked more closely at her medical records, states that he believes she is in fact limited in three ADLs. Parker can amble down the hallway with her walker but often gets dizzy. "I feel I need to be here," she says.

In early August, Hansen wrote to the insurer itemizing Parker's three ADLs in specific detail. "She's a fall waiting to happen," he says. Bankers asked for more documents, and while Parker awaits a decision, she's paying $3,700 a month for nursing-home care, as well as premiums, which the insurer hiked by $100 to $390 a month in May.

John Wells, who runs the long-term care business for Conseco, Bankers' parent company, told MONEY that for privacy reasons he couldn't discuss Parker's case. He said that Conseco pays 98 percent of claims and that if the company didn't scrutinize them, other policyholders could have to pay higher rates.

To buy or not

With so many risks to weigh, how do you decide whether you need long-term-care insurance – and if you do, what to buy? To start, you think of the big picture.

Remember: This is ultimately a question about your financial security. Imagining yourself so frail and vulnerable that you need to live in an institution or rely on a stranger's help is deeply unsettling. If you let an insurance agent frame the decision in those terms, you'll buy a policy in five seconds.

Instead of freaking out, you should focus on the potential financial need. Georgetown's Friedland says that even people only in their forties and fifties should recognize that they may have to pay for at least some long-term care.

So when calculating how much you'll need to save for retirement, you may want to add in enough to pay for several months of long-term care. That way you'll have some assets standing between yourself and Medicaid – and therefore more options. And the more you save, the easier it will be to pay for insurance if you want it when you are older.

If you are already in retirement or close to it, you have to ask yourself whether you have enough assets to bother protecting – and enough to live on in retirement. If you are scraping by, you may be so pinched

you'll have to drop a long-term-care policy before you need to use it.
After all, you'll be facing medical expenses besides long-term care. Finally, you may have other assets to tap: You might be able to take out a reverse mortgage or sell your home.
Two guidelines to help you decide whether you can afford long-term-care insurance: The National Association of Insurance Commissioners NAIC) suggests that you spend no more than 7 percent of your income on premiums, and Bonnie Burns of California Health Advocates advises that you shouldn't buy a policy unless you can withstand a premium hike of 10 percent to 20 percent.
Before you meet with an agent, talk to your kids. Many people buy long term- care insurance at least partly to avoid being a burden to their children. But when you need help, they will be involved no matter what your arrangements. And talking to your kids can help you decide how much and what kind of coverage you need.
For example, you may learn that your children aren't counting on an inheritance, which means you don't need as much insurance to protect assets. If they want to preserve a bequest and you need a larger policy, then you can ask them to help pay premiums, says Richard Kaplan, a University of Illinois law professor and an expert on elder law.
If your kids expect you to leave your home in Indiana and move near them in Boston, you'll need a policy geared to costs there, not the Midwest. If your family lives nearby, you may be able to delay going into a nursing home. A few hours each day from a home health aide and help from your kids may be enough for a while.
You may have no children or close relatives. "If there's no one, you should face that up front," says Kaplan. In that case you'll want to choose a policy with a bigger nursing-home benefit. If, in the end, you opt for long-term-care insurance, follow these steps:
Pick a rock-solid insurer.
You'll have to live with the policy you buy for decades, so you must choose a financially strong company. Above we list the six strongest among the largest carriers of long-term-care insurance, based on their financial grades from TheStreet.com Ratings, formerly Weiss Ratings, which accepts no fees from companies it evaluates.
When comparing policies, you should find out how many customer complaints an insurer has received. To check, phone your state insurance department or visit the Web site of the NAIC at naic.org/cis.
Some state regulators can also tell you about an insurer's history of premium hikes. The fact that an insurer has imposed many price increases in the past, however, does not necessarily mean that it won't raise prices again. And one that hasn't raised rates still might.
Get specifics.

You should learn exactly what your policy will and will not buy. Little words can mean a lot. Say your policy requires you to pay for the first 90 days of care yourself. Are those calendar days? Or just “service days” those days on which you get care)?

Other questions to ask: If you buy coverage for home care, will you have to use a special agency or can you hire an independent caregiver? If the policy covers assisted living, does it cover the cost of housing or only the care you receive? Also, ask the agent which facilities in your area the policy would cover – and which it wouldn’t.

Amy Bach of United Policyholders, a consumer advocacy group, recommends that you keep detailed notes of your conversation with the agent and file them with your policy.

Insist on flexibility.

Right now you don’t know what your long-term-care needs will be, so you should buy the most flexible policy you can afford. The best provide a flat cash benefit you can use as needed once you qualify, says Alfred Clapp, an independent agent in New York City.

But such coverage can add 70 percent to 100 percent to the cost of your premium. You may decide to trade off the number of years to boost the daily benefit. Consider a policy with only three to five years’ coverage. Just 8 percent of nursing-home claims run more than four years, according to Milliman Consultants & Actuaries.

You can also ramp up your daily benefit by choosing a long elimination period. Patricia Hurley, 66, of San Francisco bought a policy which won’t start paying until 90 days after the insurer approves benefits. “I intend to use this as a supplement to my own savings,” she says. Her policy also covers her for four years or until she exhausts her maximum benefit of $248,200.

Another money-saving option offered in some states: a partnership policy. It allows you to go on Medicaid after benefits run out but lets you and your family keep more assets than Medicaid normally permits.

Hedge against inflation.

A $200-a-day policy will cover a lot if you need it today, but inflation in nursing-home costs could turn that benefit into a pittance in a decade. To protect yourself, buy a policy with a benefit that increases by 5 percent compounded a year, says Joshua Wiener, a long-term-care expert at RTI International, a nonprofit research group.

Don’t go for “simple” interest. Inflation grows at a compounded rate. In 20 years a $100 daily benefit would turn into $200 with 5 percent simple interest. Compounded, the benefit would be $265.

Don’t rush.

Insurers want you to buy when you’re young. The policy will cost much less then than when you’re older. But if you buy at age 40, you could be paying premiums for as long as 60 years. It’s hard to know whether your insurer will still be strong, whether the way people get long-term care will change or how prices will rise.

Unless you have a family history of a chronic medical condition or of Alzheimer's, you can probably wait until you are near 60 to buy. You should still have a good chance of qualifying for coverage, and you'll have a clearer picture of the overall landscape.

Designate an advocate.

One family member should know you have a policy, what its terms are and where you keep it. And you should require the insurer to inform this person if you stop paying the premium.

You don't want to lose the policy because you have become cognitively impaired. If disputes about payment arise, this person will be well equipped to speak on your behalf.

Keep it simple.

The insurance industry is splendid at inventing new ways to package long-term-care insurance with items such as annuities or life insurance. But at least for now, you should steer clear of such multipurpose products.

"I once bought an answering machine that was also a photocopier and a scanner, and it didn't do any of those things well," says Deena Katz, a financial planner who teaches at Texas Tech.

As a general rule, you should buy your long-term-care insurance straight up. It's complicated enough as it is.