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INSURANCE

Long-Term-Care Mistakes

by Kimberly Lankford

Avoid these five blunders people commonly make when trying to cut premium costs.

In an attempt to hold down your long-term-care insurance premiums, you might cut some corners that could cost you a lot of money in the long run. Avoid these five common mistakes:

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1. Relying on average benefit amounts. The first decision you need to make when buying long-term-care insurance is how big a daily benefit you need. "Everything else centers around that," says Mike Ashley, a long-term-care insurance broker near Kansas City. But if you rely solely on the national average, you could fall short of the cost of care in your city -- or you could end up buying too large a benefit and skimping on other parts of your coverage.

For example, the average daily cost of a private room in a nursing home is \$203 across the country, according to the MetLife Mature Market Institute. But the average daily cost is \$135 in Birmingham, Ala., and \$330 in San Francisco. The average hourly rate for a home health aide varies just as much: It's \$13 in Birmingham and \$21 in San Francisco. To figure out how much coverage you need, check out prices for facilities in your area you wouldn't mind using. Then figure out how much of the bill you could shoulder yourself.

Ashley surveyed nursing-home costs in his area and found an average price tag of \$3,900 per month (about \$130 per day)--much lower than the national average. The price of care in Kansas City has been going up by about 4.25% per year, which would bring the monthly cost to more than \$13,500 in 30 years

-- by the time a 55-year-old is 85 and most likely to need care. "When I show clients that number, they go, 'Oh, my God!' " he says. But Ashley is quick to point out that a nursing home is probably the worst-case scenario and that many people receive care at home or in an assisted-living facility, which may be less expensive.

Then Ashley asks clients how much they can afford to pay out of their retirement savings (the key is to think in terms of future dollars, just like the rest of retirement expenses). If they can afford, say, \$3,000 per month in nursing-home costs in 30 years without dipping into savings, then they should buy enough long-term-care coverage to provide up to \$10,000 a month by then.

Assuming local nursing-home costs continue to rise by 4.25% per year, they'd need to buy about \$2,400 in monthly benefits now to provide that much coverage in 30 years -- which translates into about an \$80 daily benefit, assuming they buy a policy with 5% compound inflation protection (see below for more on inflation-protection options). "Don't buy more than you need," says Ashley.

2. Skimping on the waiting period. You can lower your premiums by choosing a longer waiting period before benefits kick in (called the "elimination period" in insurance jargon). But too long a waiting period can cost you.

For a John Hancock policy with a \$200 daily benefit, a three-year benefit period and a 30-day waiting period, a 55-year-old would pay \$2,430 per year. Extending the waiting period to 60 days lowers the price to \$2,227. A 90-day waiting period drops it to \$2,025; 180 days to \$1,822, and 365 days to \$1,620. But a longer waiting period means you'll need to pay the bills yourself before benefits kick in. At an average daily rate of \$200, that translates into a \$36,000 bill with a 180-day waiting period, and \$73,000 for a 365-day waiting period.

And that's just in today's dollars. Your expenses will be much higher when you consider the future cost of care. If costs continue to rise by about 5% per year, that daily bill could rise to \$677 in 25 years -- which means you'd pay \$122,000 with a 180-day waiting period and nearly \$250,000 with a 365-day waiting period. Those bills make saving \$200 -- or even \$400 -- per year in premiums seem like small change.

Bottom line: Most people should consider a 60-day or 90-day waiting period, which keeps premiums manageable but limits out-of-pocket costs.

3. Picking the wrong type of inflation protection. It's essential to have some kind of inflation adjustment. A policy with a \$200 daily benefit will barely make a dent in the bills if care costs \$677 per day when you finally need it, leaving you with \$73,000 to cover an annual bill of nearly \$250,000.

The best inflation-protection coverage automatically increases your benefit amount by 5% compounded annually, keeping pace with the rising cost of care. Such policies are pricey, often doubling the cost of

coverage, but your premiums will remain the same even as the benefit amount increases.

Policies with future-purchase options, which allow you to buy additional coverage over time without medical screening, can start out costing half as much as policies that automatically increase your benefit amount. But such policies soon wind up being much more expensive. That's because the increased benefits are generally priced at your age when you buy the extra coverage -- and not how old you were when you first bought the policy.

A study by Legacy Services, an independent insurance agency specializing in long-term-care insurance for large employers, illustrates the problem. If a 47-year-old man buys long-term-care coverage with a \$150 daily benefit, three-year benefit period and 90-day waiting period, he can expect to pay \$827 per year for a policy with automatic 5% compound inflation protection and just \$347 per year for a policy with future-purchase options.

But if he increases the benefit amount by 5% per year, the policy with the future-purchase options will cost \$1,158 per year by the time he is 65 years old, versus a stable \$827 for the automatic 5% policy-- although both would provide the same \$364 in daily benefits.

The difference is even larger as he gets older. By age 80, when he's more likely to need care, the FPO policy will cost \$7,811 per year, and the inflation-protection policy still will cost \$827, with both policies providing \$756 in daily benefits. You could choose not to exercise some of your future-purchase options, but then you might fall far short of your needs and have to make up the difference from savings.

Some companies offer variations on these two inflation-protection models, which can be a better deal. For example, New York Life offers a policy that automatically increases your benefit amount along with the urban consumer price index and boosts the annual cost based on your age when you bought the policy.

So, a 55-year old-who starts with a \$150 daily benefit, three-year benefit period and 90-day waiting period would pay \$2,377 per year for a policy with automatic 5% increases, \$1,189 for a policy that increases with the CPI-U, and \$845 for a policy with standard future-purchase options. If the CPI-U increases by 5% per year (it could be higher or lower), the benefit amount would be \$508 by the time the person reaches age 80. If you bought the policy with the automatic increases, you'd still be paying \$2,377 per year for that amount of coverage. For the policy with the CPI-U adjustments, you'd be paying \$4,027 per year, and for a policy with future-purchase options based on your increasing age, a whopping \$9,412 per year.

4. Assuming group coverage is the best deal. You might think that if you work for a big employer that you're getting a special deal when you buy a long-term-care policy. But you could find a much better deal on your own. In fact, group policies tend to cost healthy, married people 20% to 40% more than if they'd bought individual policies with the same coverage, says Brad Winnekins, of Legacy Services.

One reason is that many group policies offer coverage to all employees regardless of health (called "guaranteed issue"). This can be a great deal if you have medical problems. But it also means that healthy people end up subsidizing less healthy people, which boosts the cost for everyone.

Individual policies usually offer big discounts to people in good health. Plus, many group policies don't offer spousal discounts (which can run as high as 40% with some individual policies) and special benefits, such as shared-care coverage, which allows spouses to pool their benefit periods. And some groups offer only policies with future-purchase options, and not 5% compound inflation protection. Your best bet: Before buying coverage at work, compare the group policy with individual policies available from the major players (see below).

5. Working with the wrong company. A lot of people are afraid to buy long-term-care insurance because they've heard horror stories about people whose premiums jumped by double digits at exactly the worst time -- after they'd retired and could ill afford the price hike.

Although there's no guarantee that your long-term-care rates won't rise, state insurance commissioners have made it tougher for insurers to lowball rates to get customers and later raise rates when policyholders are too old to go elsewhere. And some insurers with pricing problems have left the long-term-care business.

Still, many big companies have never increased premiums for current policyholders. It's a good idea to stick with such companies, which know the business and have been stable in the past-especially because it may be decades before you need the policy and it's tough to switch companies when you're older and have developed medical problems.

It's best to work with a broker who deals with several companies and knows the policy nuances. Winnekins prefers John Hancock, MetLife, Genworth, Prudential, MassMutual and New York Life. Ashley says he generally works with the big three -- John Hancock, MetLife and Genworth -- which, he says, are among the companies that have not raised rates for their own policyholders. He recommends Genworth to people who are interested in a variety of caregiving situations; their policy allows more flexibility to use nonlicensed caregivers and has no waiting period for home care.

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