Dealing with Objections to Purchasing LTC Insurance in a Volatile Economy

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We hear many reasons for delaying the purchase of LTC insurance. But those feelings may be even stronger when the economy and markets are unstable. Clients may see extended care planning as "nice to have, but now is not the time." One reason people delay planning and purchasing LTC coverage is the belief that by waiting for the market to recover, or for the economy to change, that they will be in a better position to purchase a policy. But will they? What does the person consider to be a "recovered" portfolio, and how long could that take? What constitutes a better economy in reference to buying insurance? And more importantly, what are the consequences of waiting that these individuals are not considering?

- While a client is waiting for a "better time," they may have another birthday (or two or three). Each year you age, the policy becomes more expensive than if purchased today.
- For those wanting to add inflation benefits to a policy, waiting to purchase lessens the impact with less years for the benefit value to grow.
- A big risk is a change in health. A person who feels great today may see their health change on a dime, resulting in a decline of the application.
- Worse yet, a long-term care event could occur while the individual is "waiting for a better time" to purchase coverage.
- The biggest impact may be how self-funding LTC expenses during a down market can financially upset a retirement plan. Generally, it is less disruptive to pay smaller insurance premiums during a down market, than to pay for larger LTC expenses during a down market.

THE RISK OF SELF-FUNDING, PARTICULARLY IN A DOWN MARKET OR A HIGH INFLATION ECONOMY

Individuals and couples have been known to declare that they can afford to self-fund an extended care event. They may even tout that they can grow their account higher than any benefit pool offered by an insurance company. How sound is their plan?

Self-funding (often incorrectly called "self-insuring") presents flaws that do not exist with LTC insurance.

- How long will you have to save and invest for an extended care event before it happens?
- What rate of return will be earned over the long term?
- Will an economic period of high inflation impede your ability to contribute into your self-funded plan or cut deeper into the retirement income being used to pay for extended care?

- Even if all goes well, can you be certain there won't be a crash in the market at the time funds are needed to pay for an extended care event?

It's all unknown.

When you look at the above considerations, you can't be sure that all of these fluctuating circumstances will be in a favorable position for self-funding, or for accessing funds when the time comes to use the savings to pay for long-term care expenses. That is why self-funding could be called "un-suring," because you are unsure of the timing before the need may occur, unsure of the long-term rate of return, and unsure whether the market will be (and continue to be) in a healthy place while you begin withdrawing funds to pay for care.

Keep in mind that when taking money out of a down market, the loss is permanently realized—you can't grow it back, let alone grow it going forward; therefore, one could equate this as a double loss.

When looking deeper into this challenge, we find that paying for a LTC insurance policy—even during volatile markets and economies —can be done more effectively than saving for extended care expenses, with an overall outcome that can have a higher chance of success. LTC coverage comes in many forms, and the purchase of traditional LTC insurance can be very valuable, particularly with inflation added. However, this article will concentrate primarily on using linked benefit LTC coverage to overcome market and economic timing objections.

LINKED BENEFIT (HYBRID) LTC COVERAGE

Linked benefit LTC policies continue to be a growing market. A single premium is no longer required to purchase this type of policy, which is good news. With the advent of multi-premiums, the purchase of a linked benefit policy could make sense at any time, whether markets are up, down, or sideways.

It may help to explain what is meant by a linked benefit policy. Also sometimes referred to as hybrid LTC insurance, the policy is comprised of two benefit pools. The first pool is a small life insurance death benefit with a LTC rider that is usually equal to or greater than premiums paid. It is not intended to provide life insurance protection, but rather, it protects against the premium being lost or never used if the benefit payout is small. When qualifying for a LTC claim, benefits will be paid first by accelerating the death benefit. Once exhausted, the second benefit pool—which is pure LTC protection—will begin paying LTC benefits. Even if the policy is totally exhausted, there is usually a guaranteed minimum death benefit which varies by carrier from a few thousand dollars to as much as 20% of the death benefit amount.

WHY LINKED BENEFIT LTC POLICIES MAKE SENSE REGARDLESS OF THE MARKET ENVIRONMENT

We normally think of dollar cost averaging as a concept where money is placed *into* the market on a monthly basis to help manage the risk of market volatility. However, because some insurance companies offer linked benefit policies with no modal factor—where the cost of the policy is the same whether paying annually or monthly—the policy can be paid for using "reverse dollar cost averaging."The policy will be paid over time using monthly premiums to allow more money to remain in the portfolio to capture recovery and future growth.

The variety of linked benefit policy premium schedules vary by carrier, but let's take a look at paying for a policy over a 10 year period of time, and how it can make sense whether the market is down or up. Remember, upon that first premium paid, even if a monthly premium, the policy is immediately leveraged.

GRAPH 1	10-YEAR PREMIUM SCHEDULE ON A 55 YEAR-OLD MALE WITH 3% COMPOUND INFLATION					
Age	Policy Year	Monthly Premium	Annual Premium	Total Premium Paid to Date	Death Benefit	Total LTC Benefit
55	1	$833.33	$10,000	$ 10,000	$104,253	$337,174
60	6	$833.33	$10,000	$ 60,000	$104,253	$390,878
64	10	$833.33	$10,000	$100,000	$104,253	$439,936
70	16	$0	$0	$100,000	$104,253	$525,307
75	21	$0	$0	$100,000	$104,253	$608,974
80	26	$0	$0	$100,000	$104,253	$705,968
85	31	$0	$0	$100,000	$104,253	$818,411
90	36	$0	$0	$100,000	$104,253	$948,762

A 10-year premium schedule (or other extended schedules such as pay to age 65) can make sense for many reasons including:

- Individuals with excess salary may find it affordable, easier, or more palatable than accessing an asset.
- Withdrawing funds from a portfolio over ten years could be looked at as "reverse dollar cost averaging."
    - In a down market, pulling money out slowly could make for a better portfolio recovery. And in the case of an early death, there is still some death benefit leverage which could help compensate for a down portfolio and increase what is left to beneficiaries.
    - In an up market, strong returns could allow the policy premium to be paid from earnings, a policy itself that will have an immediate leveraged amount of LTC benefits.
    - In a sideways market, whether lasting months or even years (such as the period between 1966-1982), purchasing a linked benefit policy is one way to get guaranteed leverage for the purpose of extended care planning.

Take a look at a hypothetical example in **graph 1** above using a 10-year premium schedule on a 55 year old male with 3% compound inflation.

As you can see in the above chart, paying just $10,000 annually for 10 years with 3% compound inflation can leverage into a sizable LTC benefit pool, guaranteed. The initial first year leverage happens the moment the first monthly premium of $833.33 is paid. In addition, there is no market volatility risk—the benefit is not tied to market performance, so it is an asset an individual can own that has a known result.

DEALING WITH ECONOMIC UNCERTAINTY: **HOW A REDUCED PAID UP (RPU) POLICY OPTION CAN HELP**

Financial worries can turn into objections as individuals face economic uncertainty. Questions may include:

- "What if I have to cut back work hours, or I lose my job before the policy is paid off and I can no longer afford the premium?"
- "What if inflation continues to erode what my income can cover, making it harder to afford paying premium?"
- We've been helping family members financially. That obligation could eventually make it tough to afford the premium.

The good news is that some carriers of linked benefit LTC policies also offer a Reduced Paid Up (RPU) policy feature during the premium payment phase. Essentially, an individual will receive a paid up policy of LTC benefits, based on a pro-rata percentage of premiums already paid. For example, if you paid premiums for six full years of a 10-year premium schedule, and you

GRAPH 2	RPU POLICY WITH 3% COMPOUND INFLATION AND 10-YEAR PREMIUM SCHEDULE				
Age	**End of Year**	**Annual Premium**	**Total Premium Paid to Date**	**Death Benefit**	**Total LTC Benefit**
55	1	$10,000	$10,000	$104,253	$337,174
60	6	$10,000	$60,000	$104,253	$390,878
	PREMIUM STOPS				
60	6	RPU 60%	$60,000	$ 62,552	$234,527
75	21	$0	$60,000	$ 62,552	$365,384
85	31	$0	$60,000	$ 62,552	$491,047

would like to stop paying premium and take an RPU policy, the new guaranteed paid up benefit pool would be 60% of the total LTC benefits at end of policy year six. If the policy has inflation, it will continue to inflate starting at the new RPU amount.

Look above at **graph 2** for an example of an RPU policy that has 3% compound inflation with a premium schedule of 10 years. You will see that when taking an RPU policy at the end of year six, the policy is converted to a paid up policy at 60% of the original value[1]. From there, the 3% compound inflation continues to work and builds the LTC benefit back up and then forward.

WHAT VALUE DOES THE DEATH BENEFIT OFFER ON A LINKED BENEFIT POLCY?

Linked benefit LTC policies are not for people with typical life insurance needs, as the purpose of these policies is long-term care protection with a death benefit whose primary purpose is to protect unused premium against loss. However, the first several years of a linked benefit policy will see a nice death benefit leverage and internal rate of return (IRR). This could be an attractive side benefit for those who may value some death benefit leverage in early years of the premium payment schedule. For example, there may still be a small death benefit need for just a few more years. If death were to occur during the early years of the policy, the capture of death benefit leverage on an early death benefit could be useful because:

- The house is not quite paid off
- The kids are still in college
- There is still some debts to pay off
- The early death benefit leverage could help recover portfolio losses

As you can see in **graph 3** on the next page, the IRR on the death benefit might be considered attractive and could fill the need for additional life insurance needed for just a few more years.

LIFE INSURANCE WITH A LTC RIDER: FILLING TWO NEEDS WITH ONE POLICY

For those who have a life insurance need and can afford permanent life insurance, adding a LTC Rider to the policy can provide cost efficient LTC coverage for a small amount added to the life insurance premium. It is important to note that the LTC rider will reduce the death benefit dollar for dollar if used, but as long as life insurance needs will decline over time, this can be a cost effective solution to provide the life insurance needed now with a policy that can transition focus to LTC coverage later.

When considering long-term care coverage, guaranteed premiums and benefits are important features, and there are life insurance policies with LTC riders that can guarantee both the policy premium and benefits.

The leverage, whether for death benefit, LTC benefits, or a combination of both, will be well leveraged for the entire life of the policy. For people whose first need is life insurance, this may be a better solution. The LTC rider added to the life insurance policy can

GRAPH 3

Age	End of Year	Annual Premium	Total Premium Paid to Date	Death Benefit	Total LTC Benefit
55	1	$10,000	$10,000	$104,253	942.53%
56	2	$10,000	$20,000	$104,253	176.73%
57	3	$10,000	$30,000	$104,253	76.84%
58	4	$10,000	$40,000	$104,253	42.28%
59	5	$10,000	$50,000	$104,253	25.59%
60	6	$10,000	$60,000	$104,253	16.03%
61	7	$10,000	$70,000	$104,253	9.97%

provide first steps in extended care planning with an affordable solution that meets the immediate needs of life insurance.

SUMMARIZING THE STRATEGY

Volatile markets can be a difficult time for individuals to make financial decisions. But waiting to purchase LTC coverage until a "better time" may not be the wisest decision.

- It is generally less disruptive to pay for the smaller expense of LTC insurance during a down market, than to pay for a large LTC expenses during a down market.
- Buying now saves age and cost over waiting
- When inflation is added to a policy, buying now provides more time for benefits to grow
- Good health today does not mean good health in a few months or years from now
- Linked benefit LTC policies have guaranteed premiums. When purchased with a multi-pay premium schedule, such as a 10-year schedule, it can be positioned as "reverse dollar cost averaging" that buys a fully leveraged LTC benefit pool of protection as well as life insurance leverage for a short period of time.
- Reduced Paid Up provision (RPU) provides an "out" should you hit on hard financial times, allowing you to keep the proportional coverage you already paid.[1]
- If life insurance is currently the primary need, the combo life/LTC products provide immediate leverage for life insurance and starts extended care planning with a rider that transitions to LTC benefits if needed.

Volatility in the markets or economy should not be the lone reason to delay extended care planning and the purchase of LTC coverage. Properly positioned, purchasing it can be appropriate no matter where the markets and economy sit.

[1] Keep in mind that linked benefit policies that offer RPU (reduced paid up) policies must still meet regulatory requirements, and as such will generally have a minimum death benefit that must be maintained – for example $6,000 (varies by carrier). On 10 year or less premium schedules this usually can be met even if RPU is requested after just one full year of premium payments. However, premium schedules longer than 10 years (such as pay to age 65 or pay to age 100) could be affected by this requirement and require more than one year of premium payments to achieve the minimum death benefit requirement before RPU can be elected.

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