

Limited Payment Options

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Most long term care policies require you to continue to pay premiums for the rest of your life. There are, however, a few policies that offer you the option of paying the premium for a shorter period of time. The most common options are a ten-year payment plan, and a pay to age 65 option. A few policies offer a single premium option.

With any limited payment option, make certain the premium is guaranteed to be paid up at that point.

In my opinion, the biggest advantage of the single premium option is that you pay the premium once and you're done. This is a significant advantage because if there are no more premiums to pay, you don't have to worry about whether premiums will be increased in the future. Nearly all policies with ongoing premiums have the possibility of premiums increasing in the future. The biggest disadvantage of a single premium policy is if you die in a few years after purchase. You may have paid a lot more money for the single premium than you would have paid with a continuous pay policy. The single premium policy usually will not refund any of the difference. "You pays your money and you takes your chances".

It is not uncommon for a single premium policy to cost as much as 20 times the continuous pay premium for an otherwise comparable policy.

A reasonable compromise may be a ten pay, or pay to age 65 option. You still have the risk that the premiums could increase during the premium paying period, but at least you have a limit to that risk because in 10 years or at age 65 (depending on which option you choose) that risk ends along with your premiums. You also have the same risk of dying young and having paid a lot more premium than you would have for a continuous pay policy. A knowledgeable agent can help you evaluate whether this option makes sense for you.

One other advantage of a limited pay policy is that it may be possible to finish paying premiums while you are still working. In that case, it will probably be much easier to pay the premium than it will be during retirement.

One way to evaluate whether a ten pay policy (or pay to age 65) makes sense for you is to calculate at what age you will have paid the same cumulative premium for the ten pay policy as for the continuous pay policy. It is not uncommon for a ten pay policy to cost between two and three times as much as a continuous pay policy. If you bought a ten pay policy at age 55 and it cost twice as much as a continuous pay policy, your break-even point based on cumulative premiums paid would be age 75. Since there is a good chance you will still be alive and active (not needing care) at age 75, if you can afford it the ten pay policy could be an excellent choice.

The same choice at age 70 probably wouldn't be a very good one since then the break-even point is age 90 and many of us will no longer be around paying premiums at that point.

One criticism of using cumulative premiums to determine the break-even point is that it ignores the interest you could have earned on the difference in premium between the ten-pay and the continuous pay. While this is true, it also ignores the longer time you are exposed to the risk of a premium increase with the continuous pay policy. There is no way of knowing for certain in advance which is going to be the best choice.

Since the biggest objection to the single premium policy (other than the high up-front cost) is the risk you'll die young, having paid a lot more for the single premium, you might be asking whether a single premium life insurance policy that also pays for long-term care would be a good solution to this concern. It is, but I have other concerns about these combination single premium life insurance/long term care policies. My biggest concern is whether the benefit period they offer will be adequate. Most of them will exhaust your benefits in 50 months (essentially 4 years).

For couples, these policies are usually based on a second-to-die life insurance policy where the 50 months of benefits are shared by both spouses, essentially a 2-year benefit period for each spouse. While a 2 year benefit is better than nothing at all, it certainly wouldn't be my first choice.

My second concern is inflation. The cost of long-term care services is almost certain to increase in the future. Historically they have increased between 5% and 6% per year on average. Since the life insurance policy death benefit typically determines how much benefit you have available for long-term care, to keep up with the increasing cost of care, the death benefit would also have to increase at 5% annually. This is usually not the case. Often, the death benefit increases very little or not at all. What was an adequate benefit today is likely to pay for less than half the cost of care when it's actually needed.

Before you ask, yes, I have seen the policy where the death benefit doesn't increase much but the supplemental pool of money for LTC does increase at 5% compound annually. You still have to use up the death benefit first before you can access the additional LTC pool. So you still have inadequate benefits for the first two years of care. There are other varieties as well. What I am describing is the most common.

If these were the only objections, this type of policy might still make sense. Just buy a lot more coverage than you need today so the benefit will still be adequate when you need care.

My other concern is whether these policies make any financial sense at all. They are usually sold on the premise that if "you don't use it, you don't lost it." While this is true, in my opinion it tells well less than half the story.

In order to compare these policies to traditional long-term care policies, you have to account for all of the money, particularly the interest the large single premium would have earned. From the size of the premiums involved, this is not a trivial point. You also have to ask what happens if you do need care. If you could be certain you'd never use it, there would be no point in buying it in the first place.

Let's consider an actual comparison I ran a few months ago. The single premium policy was from one of the leading companies offering this type of plan

A single premium of \$100,000 was prepaid to purchase a \$149,061 death benefit which would produce a \$6000 per month LTC benefit for 25 months with no benefits remaining after 25 months. For comparison, I started with the same \$100,000, assumed it was invested at the same 4.8% rate assumed in the single premium policy and systemically withdrew the premium for an LTC policy with a \$200 per day (\$6000 per month) benefit and a 2 year benefit period.

Table 1 summarizes the total amount of money available at death if there is no need for LTC. It is the Death Benefit of the Single Premium Whole Life policy compared to the side fund for the traditional LTC policy.

The other side of the story is what happens if you need care?

Year	Single Premium Life Policy Death Benefit	Side Fund Value with traditional LTC policy	Difference	Number of months of benefits which would consume the entire difference
1	149,061	101,859	47,202	8
5	155,260	110,231	45,026	7.5
10	165,211	123,165	42,046	7
15	175,653	139,515	36,137	6
20	185,846	160,186	25,660	4

Since Long Term Care Benefits paid from the Single Premium Whole Life/Long Term Care combo policy reduce the death benefit, but Long Term Care benefits from the Traditional Long Term Care policy do not affect the side fund, it doesn't take long before you have more money in your side fund than the remaining death benefit. When you need care, whose money would you rather use, yours or the insurance company's?

One other limited payment option, which is only available to couples, is a survivorship benefit. I have often referred to this as "a poor man's ten pay".

The basic idea is that a couple each buy a policy which includes a survivorship benefit and after a certain period of time, if one of them dies, the premiums for the survivor are permanently waived. The typical time period is ten years. At the later of two events, ten years or premium payment and the death of the spouse, the premiums for the survivor are permanently waived.

Some policies further limit this benefit by requiring that there can not have been any claims paid on either policy during the first ten years. This type is significantly less expensive than policies that do not include this restriction. Some policies also require that both spouses survive the first ten years.

A survivorship benefit can be a very attractive benefit for couples, particularly when there is a significant difference in age. Those policies that require no claims in the first ten years and that both spouses survive the first ten years are very affordable, usually adding less than 10% to the premium. They would be much less attractive for couples where there is a significant risk one will die or need care within the next ten years.

Conclusion

Limited payment options can be a very attractive way to limit your exposure to the risk of a future rate increase. For people in their mid-50's and younger, they provide an excellent way to finish paying premiums prior to retirement while they are likely to be more affordable. I have serious reservations about combination single premium life/long term care policies. Survivorship benefits can be very attractive to many couples.

Not intended to provide legal or accounting advice. Long Term Care is a complicated subject. It takes time to consider the implications of many of the options available. In addition to any necessary legal or accounting advice from the appropriate professional you should discuss your financial situation and objectives regarding long term care with a knowledgeable agent.