When Hybrid Long-Term Care Insurance Makes Sense

The prospect of debilitating illness late in life is not a pleasant one, but it's wise to protect yourself and your family from the financial hardships that could result from it. A common way to prepare yourself is by purchasing some form of long-term care insurance.

Long-term care insurance works like this: You pay an annual premium, and if you need long-term care due to age or illness, the policy pays out a daily or monthly benefit. Some people are hesitant to consider these policies because, if they die without needing long-term care, they feel they've "wasted" the premiums.

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As a way to counter that, so-called hybrid policies have become popular. These policies combine long-term care insurance with permanent life insurance policies such as universal life insurance (which, like whole life insurance, includes a savings-investment component that builds up over time).

In the hybrid scenario, a policyholder would withdraw funds from the policy when they are needed for long-term care, and the insurance company pays for care when those funds run out. And if the policyholder dies without having needed expensive long-term care, the heirs receive a death benefit — therefore the premiums paid into the policy are not "wasted."

What are the main advantages of a hybrid policy vs traditional LTC plan?

I find that some clients can't get past the "use it or lose it" nature of traditional long-term care insurance. It is emotionally difficult to buy an insurance policy that may cost $4,000 to $8,000 per year and will pay out nothing if you pass away in your sleep. I had a client pass away last year in his mid-80s. He paid about $3,250 per year in premiums for 19 years. That is more than $60,000 that he and his family didn't get to use for something else.

That is the nature of insurance, however — you pay money to protect yourself from a risk that you hope never happens. If you pay for 20 years on a term life insurance policy and walk away with nothing, you don't wish you had died during that period. Likewise, I never think that I wasted money on car insurance if I didn't get in a car accident that year. For some reason, though, many

people think differently about long-term care insurance.

Hybrid policies reduce people's fear of wasting premiums by offering two exit strategies. The first exit strategy is that after the surrender charge period (usually 10 years), you can get most of your premiums back if you decide to cancel the policy. The illustration you receive from the insurance company shows that you will not make a return on your cash if you cancel it, but it is comforting to know that you can at least get a do-over if you change your mind down the road and want to cancel the policy.

Secondly, there is a death benefit that is paid to your heirs when you die. Leaving an inheritance is really important to a lot of people. They like knowing that some of the money they paid in premiums to the hybrid policy will be given to their kids.

The last major advantage is that the benefits are guaranteed. If you pay your premiums, you will have a contractually guaranteed death benefit, guaranteed cash value and a guaranteed amount of long-term care coverage.

Traditional long-term care insurance policies, on the other hand, do not have these guarantees. In fact, insurers can petition the state departments of insurance to raise your premiums, sometimes as much as 50% per year. Some retirees with limited assets can't afford these increases.

What are the main disadvantages?

Because hybrid policies do so many different things, they aren't the best at any one thing. I recently ran an illustration where a client would pay $150,000 in premiums and after Year 10 could only walk away with $120,000 if she decided to cancel the policy. That is better than nothing, but walking away costs you $30,000 plus the opportunity costs on what you could have made investing that $150,000. The death benefit for most of the years of this policy was also only a little more than the $150,000 of premiums she would pay in. Because the insurance company is offering so much long-term care insurance, it can't offer great growth on the cash value or a great death benefit.

Another disadvantage of hybrid policies is that the premiums are paid over shorter periods of time than traditional long-term care, which can make them unaffordable for some people. While many factors can influence the price, hybrid care for a 62-year-old woman might be about $8,000 per year for 10 years, as opposed to roughly half that for a traditional LTC premium that is payable for life (or until care is needed). Conservative investors may like the idea of taking $100,000 that is currently in a CD and leveraging that money to provide some

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life insurance and some long-term care coverage.

Lastly, the premiums you pay for hybrid policies are not potentially tax-deductible, because hybrid policies are not considered tax-qualified policies.

How should consumers choose the right plan?

I recommend you get quotes on several different types of policies and get comfortable with the costs, benefits and disadvantages. It is hard to make a decision without seeing real numbers and comparing the different types of insurance. Some people don't have the assets to be able to fund a hybrid policy within 10 years, and that alone could push them toward traditional long-term care.
Your health could also play a role in your decision — the underwriting for hybrid policies is usually a little easier, so your health may push you toward a hybrid policy.

Finally, many people cannot stand the thought of paying $30,000 or more in premiums and never receiving a dime back from the insurance company. If that sounds like you, you might be drawn toward a hybrid policy.

For a more detailed explanation or a quote, call us anytime.

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