Kiplinger.com

Know the limitations when choosing among long-term-care insurance plans

By Kimberly Lankford
Sunday, March 21, 2010

If you're thinking about buying long-term-care insurance, here's one more reason to do it: Long-term-care costs continue to escalate. In 2009, the average annual cost of a private nursing-home room rose 3 percent, to nearly $80,000.

Insurers are rolling out policies that hold down premiums by shifting some of the cost of future care to policyholders. "There is tremendous interest in looking at more economical ways to insure for long-term events," says Beth Ludden of Genworth. Some companies have introduced new forms of inflation protection that can help slash premiums. Others are offering strategies to hedge your bets when it comes to choosing the appropriate length of coverage.

Although many of these policies will save you money, they may also squeeze your benefits. So know the limitations before you decide whether one of them is right for you.

Cheaper inflation protection. Because you may wait 20 years or more to tap your long-term-care policy, it's essential that the amount of your daily benefit keeps up with rising costs. Insurers have been experimenting with more affordable ways to provide inflation protection. John Hancock's Leading Edge policy -- the type that Marzolf bought -- adjusts the daily benefit each year based on changes in the consumer price index. That's why his policy costs up to 40 percent less than the company's standard policy, which uses a 5 percent compound-inflation factor.

A CPI-linked policy can be risky, though. In years of high inflation, you may come out ahead. In low-inflation years, however, such as 2009, the cost of care may escalate, but your benefit may not (although it cannot shrink).

Insurers have also been slashing costs by offering **Guaranteed Purchase Option coverage (GPO).** These policies do not automatically adjust for inflation, but you may boost your coverage every few years, regardless of your health. **You will pay higher premiums for the extra benefits based on how old you are when you buy them.**

The cost to buy such a policy can start out substantially lower. A traditional policy with a 5 percent annual inflation adjustment may cost more than twice as much in the first year as one with a guaranteed option to bump up inflation protection in the future. **But the savings may be a false economy: Buying additional coverage with a guaranteed option could end up costing more for less coverage in the long run.**

If you can afford it, stick with a policy that offers inflation protection based on a 5 percent annually compounded rate. But if you are looking to hold down costs -- and are willing to shoulder some of the potential future expenses -- consider a CPI-adjusted policy. It's cheaper than the compounded version and may be a safer bet than one with a guaranteed purchase option. However, you may want to buy a higher daily benefit initially to stay ahead of future caregiving cost increases.

Shared benefits. One of the most difficult decisions to make when buying a long-term-care policy involves the length of your benefit period. A typical 65-year-old is likely to need some form of long-term care for three years, according to the National Clearinghouse for Long-Term Care Information. A few people, such as those with Alzheimer's disease, may need care for a much longer time. But policies that provide lifetime benefits are expensive, often costing more than $4,000 a year for people in their 50s.

Patrick and Jeanne O'Neill, owners of the Big Sky Bread, in Wilmington, Del., discovered an affordable way to hedge their long-term-care bets without spending a lot of dough. After his father died of prostate cancer following three years of care, Patrick didn't want to worry about what would happen if he needed care himself someday. And he was concerned that he or Jeanne would need care for a longer period than the typical three or four years. But the five-year policies they found were unaffordable.

Then their insurance agent, Andre Hoeschel, told them about a **shared-benefit** policy. The O'Neills bought a three-year shared-benefit policy that gives them a pool of six years of coverage between them. So if Patrick needs care for four years, for example, Jeanne would still have two years' worth of benefits. "You hate to pay for something and not use it," Patrick says. "But the odds are that one of us will need it."

Buying a shared-benefit policy costs about 15 percent more than buying two policies with three-year benefit periods. But it was less expensive than the policies with a five-year benefit period that the O'Neills were considering.

More cost sharing. Another money-saving strategy is to insure against only a portion of potential long-term-care costs. "A lot of customers are saying that instead of getting a policy that covers the full risk, let's look at something that will cover most of the costs," Hoeschel says. "They are willing to cover 10 to 40 percent of the costs themselves."

Essential planning. When it comes to buying long-term-care insurance, 50 is the new 60. Consumers are buying coverage at younger ages to take advantage of lower premiums (although they are paying those premiums longer).

-- Kiplinger's Personal Finance (shortened to fit 2 pages)