Your Money

Pros and Cons of Buying Hybrid Long-Term Care Insurance

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By Scott Olson

Hybrids are the insurance industry's latest attempt at solving one of the biggest concerns facing boomers: long-term care. Due to fears about rate increases, sales of traditional long-term care insurance have stalled. Sellers of life insurance see this as an opportunity to make permanent life insurance products (e.g. whole life and universal life) sexy again.

The many variations of hybrid policies, however, can be overwhelming and confusing. There are few standardized terms and many of the labels are used interchangeably: "combo policy," "linked-benefit," "asset-based," "accelerated death benefit," "extension of benefits," "continuation of benefits," and the list goes on.

The insurance jargon is meant to be unintelligible to the consumer.

Regardless of the labels, all hybrids have one thing in common: they combine long-term care insurance with some other type of insurance. Just like "hybrid cars" combine two energy sources (gasoline and electricity), "hybrid policies" combine two types of insurance: long-term care insurance plus a life insurance policy or a deferred annuity.

The long-term care insurance is attached as a "rider" to either a life insurance policy or a deferred annuity.

In this article I will give you some tools to help you understand the key differences between each type of hybrid so that you can make a wise decision.

Single-Premium vs. Annual Premium

The simplest way to differentiate between hybrids is how often the premium is paid. Some hybrids require a large, one-time premium payment. Other hybrids have annual (or monthly) premium payments, like most types of insurance.

A single-premium life insurance policy with a "long-term care rider" can do three things:

- If you need long-term care, a portion of the death benefit (usually 2% to 4%) is paid for your care each month.
- If you die without needing care, the death benefit is paid to your heirs.
- You can cancel the policy, at any time, and receive the cash surrender value.

The industry describes this as: "Live, die or quit." If you live, it will help pay for your long-term care. If you die, it pays a death benefit to your heirs. If you decide you don't want the policy anymore, you can cancel it and receive the cash surrender value.

A single-premium annuity with a "long-term care rider" is similar:

- If you never need care, the annuity's accumulated value is paid to your beneficiary.
- If you do need care a portion of the annuity's accumulated value (usually 3% to 4%) is paid for your care each month.
- If you decide you don't want the annuity anymore, you can cancel it and receive the annuity's cash surrender value.

Drawbacks to Single-Premium Products

The main drawback to the single-premium products is the opportunity cost. Even though the materials explaining the product may state the "minimum guaranteed interest rate is 4%," after subtracting for "other charges" and "cost of insurance" the actual growth of your cash value is usually less than one-half of one percent. After subtracting surrender charges, your return is often negative, especially in the first 10 years of owning the policy. Although there are no "ongoing premium payments" the opportunity cost may be greater than what you'd pay annually for a traditional long-term care insurance policy.

The second drawback to the single-premium products is the insurer uses your single-premium to pay for your care. If you need care, your single-premium becomes something like a deductible. It is used to pay most of your long-term care expenses for the first 24 to 50 months (depending upon the policy).

One Big Advantage to the Single-Premium Products

The big advantage to the single-premium products is lenient underwriting. These products are very easy to qualify for even if you have serious health problems.

The insurer is willing to accept higher risks for these products because they are earning money on your single-premium until you need care, and once you need care, the first 24 months (or so) of long-term care expenses are primarily paid with your single-premium. If you're comfortable using your money to pay for the first 24 months (or so) of your care, a product like this may be very suitable for you.

Annual Premium Hybrid Products

An annual premium life insurance policy with a "long-term care rider" is very similar to a single-premium policy:

- If you need long-term care, a portion of the death benefit (usually 2% to 4%) is paid for your care each month.
- If you die without needing care, a death benefit is paid to your heirs.
- You can cancel the policy, at any time, and receive the cash surrender value.

Note, however, that the cash surrender value of an annual premium hybrid starts off at zero and grows a little every year as you continue to pay your annual premium.

There are 48 variations of this type of product. Rather than try to explain the nuances of all 48 types, there's one question you can ask the insurance agent (or investment adviser) that will keep you from making a huge mistake.

When investigating this type of hybrid ask: "What is the premium I must pay each year to guarantee this policy will stay in force until my 100th birthday?"

Here's a little secret in the life insurance industry: Most "permanent" life insurance policies are not guaranteed to stay in force until age 100. Most "permanent" life insurance policies are designed to lapse when you're in your 70s or 80s. If the life insurance policy lapses before you need long-term care, you will receive nothing from the policy: no cash value, no long-term care benefits, no death benefit. That is why you must be certain that the hybrid policy you purchase is guaranteed to stay in force until age 100 (or longer).

Look for LTC Benefits Greater than the Death Benefit

Most hybrids have long-term care benefits that are equal to or less than the death benefit. If you're considering a hybrid to help you with future long-term care expenses, you'll get a lot more value if you buy a hybrid with long-term care benefits that are greater than the death benefit.

Some hybrids offer long-term care benefits that are three times the death benefit. Other hybrids have long-term care benefits with no lifetime cap (i.e. the policy can never run out of long-term care benefits regardless of how long you may need long-term care.)

Biggest Myth About Hybrids

The narrative you'll often hear about hybrids goes like this: "If you don't want to pay for expensive long-term care insurance, consider one of the newer hybrid policies that combines life insurance with long-term care insurance." The implication is that a hybrid is less expensive than a traditional long-term care policy. That's generally not true.

Most people purchase long-term care insurance in their late 50s. A healthy couple in their late 50s will typically pay 45% to 150% more premium for a hybrid policy than they would for a comparable long-term care insurance policy.

Choosing the Best Policy for You

If you're comparing different hybrids and/or traditional long-term care insurance, here's a simple way to cut through the insurance jargon and focus on the most important benefits. Ask each insurance agent and/or investment adviser you're working with these three questions:

1. "If I need to use this policy for long-term care, what is the maximum amount it will pay each month, if I need care five 5 years from now? 15 years from now? 25 years from now?" I call this the "monthly maximum."
2. "If I need to use this policy for long-term care, what is the maximum amount it can pay over my lifetime if I need care 5 years from now? 15 years from now? 25 years from now?" I call this the "lifetime maximum."
3. "If I don't need to use this policy for long-term care, what will my heirs receive?"

Compare these values with each policy's premium and it'll be a lot easier for you to pick the policy that is right for you.

About the author: Scott Olson is the co-founder of LTCShop.com and author of Simple LTC Solution: How to Protect Your Life's Savings with a Long-Term Care Partnership Program, a book that teaches complex concepts using real-life examples and everyday language that anyone can understand. With 23 years of experience in the long-term care insurance industry, Olson is a sought-after expert on the subject. He has been quoted in The New York Times, AARP Bulletin, U.S. News & World Report, Business Week, Kiplinger's, and other leading publications. Olson was one of the first insurance professionals to earn the certification for Long-Term Care designation (CLTC). He is a member of the CLTC Board of Advisors.

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