

PRIVATE LONG-TERM CARE INSURANCE: NOT THE SOLUTION TO THE HIGH COST OF LONG-TERM CARE FOR THE ELDERLY

Lawrence A. Frolik

Long-term care can be extremely expensive. As older Americans plan for financing care for their golden years, one option is to purchase a Long-Term Care Insurance (LTCI) policy. However, despite the potentially steep costs of long-term care, few elderly individuals actually purchase LTCI. This decision is rational for most elderly people. First, LTCI insures a risk that may never occur, as the majority of elderly Americans only need a year or less of long-term care. Second, Medicaid provides a publicly subsidized alternative to LTCI. An elderly person can rely on his or her savings to pay for care and then qualify for Medicaid if necessary. Third, the likely benefits payout is difficult for insurers to estimate, resulting in higher premiums for policyholders. Additionally, the growth of assisted living facilities, a far more attractive living situation than nursing homes, may incentivize elderly policyholders to begin claiming benefits sooner, which also results in increased insurance rates. The elimination period of LTCI policies, coupled with the unpredictability of the need for LTCI and a daily benefit amount that is unlikely to cover the full cost of a nursing home, further renders purchasing such a policy unappealing. One possible solution is redefining long-term care costs as a social, as opposed to an individual, problem and requiring all older Americans to purchase LTCI, a measure that could reduce the burden on Medicaid while ensuring that all elderly Americans are able to afford long-term care.

Distinguished Faculty Scholar and Professor of Law, University of Pittsburgh School of Law.

I. Introduction

Long-term care for the elderly is expensive, very expensive.¹ A nursing home can cost \$50,000 to \$280,000 per year.² The annual cost of care in an assisted living facility is \$30,000 to \$94,000 per year.³ Paid, in-home care for twenty-four hours a day, seven days a week can cost over \$150,000 per year.⁴

Although the potential cost of long-term care is predictable, those who will need long-term care is uncertain; yet, those in their sixties face the risk of costly long-term care.⁵ When faced with a potentially very costly risk, a rational person must consider the purchase of insurance, in this case, long-term care insurance. Although long-term care insurance is available, few purchase it.⁶ While it may appear counterintuitive, not purchasing long-term care insurance is a sensible decision for most older persons, which explains why long-term care insurance is not a solution to paying for the cost of long-term care for the elderly.

II. The High Cost of Long-Term Care

Health care includes the subset long-term care (LTC) that is fundamentally different from other medical expenses.⁷ Although the need for LTC can occur at any age, it is required disproportionately by the elderly—those age sixty-five and older—with dementia, chronic

1. HOWARD GLECKMAN, *LONG-TERM CARE FINANCING REFORM: LESSONS FROM THE U.S. AND ABROAD* 1 (The Commonwealth Fund eds., 2010).

2. *Genworth 2015 Cost of Care Survey*, GENWORTH 1, 16-17 (2015), https://www.genworth.com/dam/Americas/US/PDFs/Consumer/corporate/130568_040115_gnw.pdf.

3. *Id.* at 15 (This range is based on the median annual cost of “One Bedroom - Single Occupancy” assisted living facilities).

4. See *Market Survey of Long-Term Care Costs*, METLIFE MATURE MKT. INST. 4 (2011), <https://www.metlife.com/assets/cao/mmi/publications/studies/2011/mmi-market-survey-nursing-home-assisted-living-adult-day-services-costs.pdf> [hereinafter *Market Survey*].

5. GLECKMAN, *supra* note 1, at 1; see Peter Kemper et al., *Long-Term Care Over an Uncertain Future: What Can Current Retirees Expect?*, 42 *INQUIRY* 335, 342 (2005/2006), <http://www.allhealth.org/briefingmaterials/Long-TermCareOveranUncertainFuture-WhatCanCurrentRetireesExpect-461.pdf>.

6. Jeffrey R. Brown & Amy Finkelstein, *Supply or Demand: Why is the Market for Long-Term Care Insurance So Small?* 26-27 (Nat'l Bureau Econ. Research, Working Paper No. 10782, 2004), <http://www.nber.org/papers/w10782.pdf>.

7. Dana Shilling, *Long-Term Care Insurance in 2012: Part 1*, 255 *ELDER L. ADVISORY* 1 (2012).

illness, and physical frailty being the leading causes.⁸ Because extended care needs of younger persons usually arise from a disability that is not associated with aging, the provision of services to a younger person with a disability are usually not referred to as LTC.⁹

LTC refers to care provided for older persons that is provided in the home, personal care homes, assisted living facilities, and in nursing homes.¹⁰ LTC does not attempt to cure; rather, it provides assistance and comfort to those with physical or mental conditions by providing medical care (skilled nursing care) and custodial care.¹¹ The latter typically refers to the provision of services that assist the individual with the activities of daily living, which include eating, dressing, bathing, toileting, and ambulation, such as moving to or from a bed or wheelchair.¹²

The cost of LTC can be great. The average estimated annual cost of nursing home care in 2012 was over \$85,000.¹³ In that year, total nursing home expenses amounted to \$158 billion, which represented more than half of the total spent on long-term care.¹⁴ It is estimated that up to half of all LTC is provided at no cost by spouses, family members, friends, and volunteers.¹⁵ The other half is paid for by savings, income, Medicaid, Medicare, and by long-term care insurance (LTCI).¹⁶ Of these, Medicaid predominates: in 2012, the joint federal-state program paid for about one-third of nursing home expenditures.¹⁷

8. See Lauren Harris-Kojetin et al., *Long-Term Care Services in the United States: 2013 Overview*, 3 VITAL & HEALTH STAT. 1, 35 (2013), http://www.cdc.gov/nchs/data/nsltcp/long_term_care_services_2013.pdf.

9. For example, see the difference between old-age benefits and disability benefits, Federal Old-Age and Disability Insurance, 20 C.F.R. § 404.2(c)(2) (2015).

10. Brown & Finkelstein, *supra* note 6, at 1; Harris-Kojetin et al., *supra* note 8, at 2.

11. THE ADVISOR'S GUIDE TO LONG-TERM CARE 3 (R. David Watros & Erik T. Reynolds eds., 2013) [hereinafter THE ADVISOR'S GUIDE].

12. LAWRENCE A. FROLIK, RESIDENCE OPTIONS FOR OLDER AND DISABLED CLIENTS 198 (ABA ed., 2008).

13. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-14-473, MEDICAID: FINANCIAL CHARACTERISTICS OF APPROVED APPLICANTS AND METHODS USED TO REDUCE ASSETS TO QUALIFY FOR NURSING HOME COVERAGE 1 (May 2014), <http://www.gao.gov/assets/670/663417.pdf> [hereinafter FINANCIAL CHARACTERISTICS]. In the GAO Report to Congressional Requesters, a nursing home's average cost for 2012 was estimated to be \$85,000. See *Market Survey*, *supra* note 4.

14. FINANCIAL CHARACTERISTICS, *supra* note 13.

15. THE ADVISOR'S GUIDE, *supra* note 11, at fig. 2-2, 37 fig. 3-1.

16. *Id.*

17. FINANCIAL CHARACTERISTICS, *supra* note 13, at GAO Highlights.

Not all paid-for care is provided in nursing homes.¹⁸ Some elders receive long-term care in assisted living facilities, which do not provide medical care and are not typically licensed to care for non-ambulatory residents.¹⁹ Although such facilities cannot house the very sick, assisted living facilities provide care in the form of room and board, supervision, and personal assistance.²⁰ Assisted living costs about half as much as nursing home care, usually in the range of \$40,000 to \$45,000 per year.²¹ Other elderly individuals purchase care that is provided at home.²² The cost of care in the home varies based upon the hourly rate paid to caregivers, the number of hours of care needed per day, and the amount of volunteer assistance, such as care provided by a spouse, at a cost of \$20 per hour.²³ For sixteen hours of care per day, the annual cost of home care would be over \$115,000 per year.²⁴

The high cost of long-term care—and the very real possibility of needing it²⁵—would seem to lead to the purchase of LTCI. Yet, presently, only a small minority of the elderly purchase LTCI.²⁶ The question is why. What is it about LTCI that makes it such an unattractive product to so many?²⁷

18. In 2012, over 58,000 paid, regulated long-term care providers served about 8 million individuals. These services were provided by 4800 adult day care centers, 12,200 home health agencies, 3700 hospices, 15,700 nursing homes serving 1,383,700 residents, and 22,200 assisted living and other residential care facilities serving 713,000 residents. Harris-Kojetin et al., *supra* note 8, at viii.

19. FROLIK, *supra* note 12, at 193.

20. *Market Survey*, *supra* note 4, at 7-8.

21. *Id.*

22. *Id.*

23. In 2011, the national average private-pay hourly rate for a home health aid was \$21 per hour and for a homemaker/companion service was \$19 per hour. *Id.*

24. *See id.*

25. It is estimated that by 2020, 12 million Americans will need LTC. Christine Benz, *40 Must-Know Statistics About Long-Term Care*, MORNINGSTAR (Aug. 9, 2012, 6:00 AM), <http://news.morningstar.com/articlenet/article.aspx?id=564139>.

26. In 2008, only about fourteen percent of individuals aged sixty and older owned LTCI. Jeffrey Brown & Amy Finkelstein, *Insuring Long-Term Care in the U.S.* 7 (Nat'l Bureau of Econ. Research, Working Paper No. 17451, 2011); see Karyn L. Neuhauser, *Long-Term Care: Helping Clients Make the Right Choices*, J. FIN. PLAN. 44 (2012) ("Only 10 percent to 12 percent of older Americans covered by LTC insurance . . .").

27. One commentator suggests that it is not the insurance that is found wanting, but instead potential buyers simply do not want to imagine themselves so disabled as to need daily assistance. To do so is "simply too painful." RICHARD L. KAPLAN, *Financing Long-Term Care in the United States*, in AGING: CARING FOR OUR ELDERLY 65, 78 (David N. Weisstub, David C. Thomasma, Serge Gauthier & George F. Tomossy eds., 2001). See M.V. Pauly, *The Rational Nonpurchaser of Long-Term-Care-Insurance*, 98 J. POL. ECON. 153 (1990).

Despite the risk of incurring costly LTC, to date, LTCI has been only marginally attractive, and growing less so.²⁸ Although it has been on the market for over thirty years,²⁹ the last few years have seen a general exodus from the market.³⁰ In 2012, only twelve companies sold over 2500 policies; the total number of policies sold dipped below the level of sales in the 1990s.³¹ Why has that happened? Why has LTCI fallen into disfavor with both insurance companies and potential purchasers? The answers lie in the fundamentals of insurance and in the reality that the product has very limited appeal to potential purchasers who correctly perceive its limited value.

III. Selected Insurance Fundamentals

Insurance is designed to protect against losses that result from defined risks, such as death, the theft of an automobile, or the cost of health care.³² Insurance transfers the risk of loss from the insured to the insurer.³³ Insurance depends upon many purchasing it, but only a few—in any given period of time—qualify for benefits.³⁴

Insurance can roughly be divided into two kinds: casualty and life. Casualty insurance covers risks to property or business activity that are uncertain to occur and for which the amount of loss is also uncertain, though limited either by the value of what is being insured or benefit limits stated in the policy.³⁵ Typical examples of casualty insurance are fire or car insurance.³⁶ Fire insurance protects against

28. The Congressional Budget Office in 2004 estimated that LTCI paid for only four percent of long-term care expenditures. Brown & Finkelstein, *supra* note 26, at 5.

29. Marc A. Cohen et al., *Exiting the Market: Understanding the Factors Behind Carriers' Decision to Leave the Long-Term Care Insurance Market*, OFFICE OF THE ASSISTANT SECRETARY FOR PLAN. & EVALUATION, U.S. DEP'T. OF HEALTH & HUMAN SERVS. (July 2013), <http://aspe.hhs.gov/basic-report/exiting-market-understanding-factors-behind-carriers-decision-leave-long-term-care-insurance-market>.

30. Nimmi Cleve, *Long-Term Care Insurance: An Endangered Species*, 22 ANNALS HEALTH L. 181, 188 (2013).

31. Cohen et al., *supra* note 29. This does not include companies that may sell only so-called hybrid policies, i.e., policies that combine LTCI with life insurance or an annuity.

32. HERBERT S. DENENBERG ET AL., RISK AND INSURANCE 11 (2d ed., 1974).

33. *Id.* at 10.

34. *Id.* at 6.

35. See generally *Casualty Insurance*, INVESTOPEDIA, <http://www.investopedia.com/terms/c/casualtyinsurance.asp> (last visited Oct. 28, 2015).

36. See generally ROBERT H. JERRY & DOUGLAS R. RICHMOND, UNDERSTANDING INSURANCE LAW (2012).

what can be a very costly loss, but has a low likelihood of occurrence.³⁷ Car insurance covers a more likely risk, but one that usually has a smaller loss, although a very large loss does occur from time-to-time.³⁸

Life insurance insures death, a risk certain to occur, but uncertain as to when it will occur. The amount of the loss is a death benefit, which is an artificial amount determined, not by an actual loss, but by the amount of death benefit selected by the insured.³⁹ Life insurance covers a low-probability risk for any particular individual over a period of time, but the total number of losses (deaths) is highly predictable for a group of individuals over the period of time that the insurance is in force. With a predictable total number of deaths for those insured and known payouts, i.e. the death benefit stated in the policy, life insurance is an attractive insurance product for both the insurance company and the individual buyer.⁴⁰

LTCI resembles casualty insurance more than life insurance because, unlike death, the risk of paying for LTC is not certain. Like casualty insurance, LTCI insures a risk of loss that may never occur. The insured may never need LTC or may never pay for it⁴¹ and so may never trigger the payment of benefits. The amount of the loss is uncertain, but LTCI limits the amount of loss that it will recompense.⁴² For example, a LTCI policy might pay \$200 per day for up to five years of qualifying care for a maximum benefit amount of \$365,000.⁴³

37. Fire insurance is usually sold as Home Owners Insurance and covers not only fire, but covers other risks such as theft or storm damage, which results in the occurrence of the risk being greater. But, the cost of the loss being lower than if the policy insured only losses from fire.

38. See generally Donald T. Sant, *Estimating Expected Losses in Auto Insurance* 47 J. RISK & INS. 133 (1980).

39. The insured may select the death benefit as a surrogate for the loss of income available to a third party because of the death of the insured, e.g., a spouse insures her life to replace her lost earnings that her husband relies upon for his support. The loss is usually the value of lost future earnings.

40. Kyle D. Logue, *The Current Life Insurance Crisis: How the Law Should Respond*, 32 CUMB. L. REV. 1, 15-16 (2001).

41. LTCI only pays benefits if the insured is paying for LTC. If LTC is provided for free, such as by a spouse, the policy will not pay benefits.

42. Neuhauser, *supra* note 26, at 45-46.

43. A few LTCI policies have no limit on how long benefits can be paid. Realistically, however, only a small percentage of those insured will qualify for benefits for more than five years. As a result, from the perspective of the insurance company, a "lifetime benefits" policy realistically has a limit of five or six years. According to the American Association for Long-Term Care, only 4.5% of long-term care eligible for insurance reimbursement lasts longer than five years. THE ADVISOR'S GUIDE, *supra* note 11, at 178 n.26 (citing Jesse Slome, *How Much Does Long Term Care Insurance Cost?*, AM. ASS'N FOR LONG-TERM CARE INS., <http://www.>

Yet, most elderly individuals will never incur LTC costs that come close to that amount.⁴⁴ The majority of the elderly who require LTC only need it for one year or less.⁴⁵ Although some need LTC for up to three years and a few more for up to five years, only a small percentage need LTC for more than five years.⁴⁶

If most individuals need LTC for a year or less, it is questionable whether this type of care should be called “long-term care.” Even if care is provided in a nursing home, which is one of the more costly providers of LTC, the cost per year will only range from \$70,000 to \$120,000, with a median cost in 2013 of \$80,000.⁴⁷ Although sizeable, it is not clear that the potential risk of incurring a cost of \$100,000 represents the kind of unacceptable risk that should be insured, i.e., an unacceptable risk. For most who receive LTC, death is the reason for the termination of the LTC.⁴⁸ A \$100,000 cost incurred in the last year of life, while unwelcome, does not pose for most elderly individuals as an “unacceptable risk” in the same way that a \$100,000 loss, such as a house fire, poses to an individual with many years to live. Absent a need to protect a surviving spouse or to fund a bequest, the loss of \$100,000, even if it represents most or all of the individual’s savings, is better seen not as a loss, but rather a consumption of savings that has no further value to the now deceased individual.⁴⁹ Further discouraging the sale of LTCI is the reality that the elderly already own—LTCI in the form of Medicaid.⁵⁰

aaltci.org/long-term-care-insurance/learning-center/how-much-does-long-term-care-insurance-cost.php).

44. *Id.*

45. Neuhauser, *supra* note 26, at 45-46.

46. *Id.*

47. *Genworth 2014 Cost of Care Survey*, GENWORTH 1, 16 (2014), https://www.genworth.com/dam/Americas/US/PDFs/Consumer/corporate/130568_032514_CostofCare_FINAL_nonsecure.pdf (showing that the cost of nursing homes varies greatly from state to state). In California, the median average cost was \$86,815, in Texas \$50,735, in Florida \$83,950, and in New York \$124,100. *Id.*

48. See generally Marianne Purushotham & Nancy Muise, *Long-Term Care Insurance Persistency Experience*, LIMRA INT’L & THE SOC. OF ACTUARIES LTC COMM. 3, 10 (2006), <https://www.soa.org/Research/Experience-Study/Group-Health/hlth-long-term-care-insurance-persistency-experience.aspx>.

49. See *Present Value-PV*, INVESTOPEDIA, <http://www.investopedia.com/terms/p/presentvalue.asp> (last visited Aug. 31, 2015).

50. Medicaid has a significant impact upon the sale of LTCI. “[D]ue to Medicaid crowd-out, few individuals would choose to buy insurance even if they were rational, far-sighted, and well-informed.” Leora Friedberg et al., *Long-Term Care: How Big a Risk?* 7 (Ctr. for Retirement Research at Boston College, Working Paper No. 14-18, 2014), http://crr.bc.edu/wp-content/uploads/2014/11/IB_14-18_508_rev.pdf.

IV. Medicaid and LTCI

Thanks to Medicaid, the cost of LTC in a nursing home is often paid for by the government.⁵¹ Medicaid, a federal program jointly funded by both the federal government and the states, pays for health care for impoverished elderly, among others.⁵² On average, about fifty percent of Medicaid costs are funded by the federal government, although the percentage paid varies from state to state.⁵³ Although states operate Medicaid under federal requirements, states are permitted some variance and may be more generous in awarding benefits.⁵⁴

Medicaid will pay for the cost of LTC provided in a nursing home and, to a limited extent, for some care provided at home.⁵⁵ Eligibility for Medicaid differs from state to state, but Medicaid eligibility essentially requires that older persons impoverish themselves by spending substantially all of their assets and income on their cost of care.⁵⁶ Married couples are permitted to retain some assets and income for the non-institutionalized (community) spouse.⁵⁷

Medicaid, a welfare program that pays for LTC provided by a nursing home,⁵⁸ can also be conceived of as a form of insurance that has a deductible—the need to spend all assets on the cost of care—

51. CTRS. FOR DISEASE CONTROL & PREVENTION, LONG-TERM CARE SERVICES IN THE UNITED STATES: 2013 OVERVIEW 2 (2013), http://www.cdc.gov/nchs/data/nsltcp/long_term_care_services_2013.pdf.

52. Some states refer to their Medicaid program as Medical Assistance. In California, Medicaid is called Medi-Cal.

53. ANDY SCHNEIDER ET AL., THE MEDICAID RESOURCE BOOK 94 (The Kaiser Comm'n on Medicaid & the Uninsured ed., 2002), <http://www.kff.org/medicaid/2236-index.cfm> (“States with per capita incomes above the national level receive a lower federal matching percentage.”).

54. 42 U.S.C. § 1396 (2012). For a discussion of the eligibility requirements for Medicaid payment of nursing home care, see LAWRENCE A. FROLIK & MELISSA C. BROWN, ADVISING THE ELDERLY OR DISABLED CLIENT (2d ed. with Supplement 2015) (discussing eligibility requirements for Medicaid in Chapter 14).

55. Sidney A. Watson, *From Alms Houses to Nursing Homes and Community Care: Lessons from Medicaid's History*, 26 GA. ST. U. L. REV. 937 (2010). A few states are now experimenting with paying for LTC provided in an assisted living facility. See generally Robert L. Mollica, *State Medicaid Reimbursement Policies and Practices in Assisted Living*, NAT'L CTR. FOR ASSISTED LIVING & AM. HEALTH CARE ASS'N (Sept. 2009), <http://www.ahcancal.org/ncal/resources/documents/medicaidassistedlivingreport.pdf>.

56. Peter Kyle, *Confronting the Elder Care Crisis: The Private Long-Term Insurance Market and the Utility of Hybrid Products*, 15 MARQ. ELDER'S ADVISOR 110, 114 (2013).

57. Enid Kassner & Lee Shirey, *Medicaid Financial Eligibility for Older People: State Variation in Access to Home and Community-Based Waiver and Nursing Home Services*, THE PUB. POL'Y INST. 1, 9 (2000), http://assets.aarp.org/rgcenter/health/2000_06_medicaid.pdf.

58. Watson, *supra* note 55, at 938.

and a continuing co-pay in the form of the requirement that the individual spend all of his or her income for LTC.⁵⁹ For example, imagine an eighty-year-old single woman enters a nursing home that costs \$8000 per month. Her monthly income is \$4030 and she has savings worth \$10,000. In two months, she will have reduced her savings to \$2000 and face a monthly nursing home bill of \$8000 while having an income of only \$4030.⁶⁰ She is eligible for Medicaid because she is permitted to have \$2000 in savings (known as resources, the amount can be higher depending on the state).⁶¹ She applies for Medicaid and is declared eligible. She is permitted to retain thirty dollars per month as a personal needs allowance, but must apply the remaining \$4000 of her income to the monthly cost of the nursing home. Medicaid will then reimburse the nursing for the remaining cost of her care.⁶²

Medicaid is, in essence, publically subsidized LTCI, which may explain in part why LTCI has found such a low rate of acceptance.⁶³ Many who incur LTC expenses have enough savings and income to pay for their care for a limited period of time.⁶⁴ After they exhaust their resources, they qualify for Medicaid.⁶⁵ Unless the individual has a strong incentive to protect his or her savings, either to protect the quality of life of a spouse or to pass it on to heirs as a bequest, there is little incentive to purchase LTCI because the cost of LTC beyond the individual's income and savings will be paid for by the government.⁶⁶ For many, that degree of risk is acceptable and not worth insuring. Put another way, because of the existence of Medicaid, the payment of

59. Kyle, *supra* note 56.

60. She will pay the \$8000 monthly cost by spending \$4000 per month from her income and \$4000 per month from her savings.

61. 42 U.S.C. § 1396a(a)(10)(ii)(I) (2015); Kassner & Shirey, *supra* note 57, at 6-7.

62. Medicaid pays at a rate the state determines to be appropriate, which is usually less than the rate charged by the nursing home to a private pay individual. For a discussion of the factors that affect the state approval rate, see Vernon K. Smith et al., *Medicaid in an Era of Health & Delivery System Reform: Results from a 50-State Medicaid Budget Survey for State Fiscal Years 2014 and 2015*, KAISER FAM. FOUND. (Oct. 14, 2014), <http://kff.org/report-section/medicaid-in-an-era-of-health-delivery-system-reform-provider-rates-and-taxes-or-fees-8639/>.

63. Kyle, *supra* note 56, at 111; see Brown & Finkelstein, *supra* note 26, at 12 (claiming that economic theory suggests that Medicaid significantly limits the market for LTCI by making it largely redundant). The authors rely solely on economic models and do not cite any actual evidence of Medicaid suppressing the sale of LTCI. *Id.*

64. See Kyle, *supra* note 56, at 114.

65. *Id.*

66. See Brown & Finkelstein, *supra* note 26, at 14.

premiums for LTCI reduces consumption of other goods and services without providing any significant benefit.⁶⁷

Only a small minority of the elderly will experience out-of-pocket LTC costs that exceed \$100,000.⁶⁸ Of those, most will qualify for Medicaid.⁶⁹ If so, their financial exposure is limited to the value of their assets prior to qualifying for Medicaid benefits and to the value of the income received after being qualified for Medicaid.⁷⁰ Many will have a net worth below \$100,000, which makes their financial exposure very limited.⁷¹ The result is that the actual pool of potential LTCI purchasers is not all of the elderly—not the 42 million age sixty-five and older⁷²—but a small subset of people who have enough net worth to make it sensible for them to consider buying LTCI.

V. LTC as an Insurable Risk

Although Medicaid reimbursement of LTC costs may make LTCI difficult to sell, the cost of LTC appears to meet the criteria of insurability, at least for those elderly with sufficient assets to be concerned about the possible cost of LTC.⁷³ As stated, “[t]he possibility of needing long-term care is exactly the sort of large, uncertain expenditure risk for which insurance would seem to be most valuable.”⁷⁴ The potential loss is essentially random because whether someone who owns LTCI will become eligible for benefits is not controlled by the

67. MARK J. BROWNE, COMPETITIVE FAILURES IN INSURANCE MARKETS, THEORY AND POLICY IMPLICATIONS 101 (Pierre-Andre Chiappori & Christian Gollier eds., 2006).

68. Kemper et al., *supra* note 5, at 346.

69. *Id.*

70. The actual dollar amount at risk is less for a couple because the community spouse is permitted to retain the greater of at least half of the countable resources or \$23,844 (in 2015, adjusted annually for inflation) up to a maximum of \$119,220. 42 U.S.C. § 1396r-5(f) (2012); 2015 SSI and Spousal Impoverishment Standards, CTRS. FOR MEDICARE & MEDICAID SERVS. (2015), <http://www.medicaid.gov/medicaid-chip-program-information/by-topics/eligibility/downloads/2015-ssi-and-spousal-impoverishment-standards.pdf>. The community spouse is also permitted to retain the home, although the state can impose a lien on the house up to the value of the Medicaid benefits provided to the institutionalized spouse. 42 U.S.C. § 1382b(a)(1) (2012); 42 U.S.C. § 1396p(a) (2012). The income of the community spouse is not liable for cost of the institutionalized spouse’s nursing home care. 42 U.S.C. § 1396r-5(b) (2012).

71. FINANCIAL CHARACTERISTICS, *supra* note 13, at 14-16.

72. THE ADVISOR’S GUIDE, *supra* note 11, at 62.

73. For an extended discussion of the concept of insurability, see BARUCH BERLINER, LIMITS OF INSURABILITY 13-15 (1982).

74. Brown & Finkelstein, *supra* note 26, at 5.

insured or by a third party and so is a random occurrence, albeit one that rises with the age of the insured.⁷⁵

A. Amount of Potential Payable Benefits

Insurance covers risk, which is a measurable certainty of loss.⁷⁶ The insurance company must be able to accurately project the maximum possible loss per each insured and collectively for all of the insureds.⁷⁷ The estimate of future losses among a group of insured individuals is thus premised upon two things. First, it is premised upon having counted a sufficiently large number of loss events in the past to have a statistically relevant pool.⁷⁸ Second, it is premised upon the causes of those losses, and therefore, the number and extent of the losses remain constant in the future.⁷⁹ The maximum loss for a LTCI policy is based on the daily benefit amount and on how many days of LTC are insured.⁸⁰ Typically, three to five years of LTC are commonly insured, although there are policies that pay as long as the insured qualifies for benefits.⁸¹ Even lifetime LTCI benefits have a limit because the possible loss cannot exceed the individual's life.⁸²

Therefore, the viability of LTCI for the insurance company depends on accurate projections of how many policy owners will claim

75. To the extent that the need for LTC is a function of lifestyle, *i.e.*, does the insured exercise, smoke or otherwise live a manner that will decrease or increase the risk of needing LTC, it can be said that the risk, if not controlled by the insured, is at least subject to some manipulation. It is highly unlikely, however, that older individuals modify their manner of living based on whether they do or do not own LTCI. After the need for LTC arises, however, policy owners have some control as to when they will purchase LTC and thereby trigger the payment of benefits. See also DENENBERG ET AL., *supra* note 32, at 4-9.

76. *Id.* at 4.

77. *Id.* at 33.

78. *Id.*

79. *Id.* at 33-34.

80. THE ADVISOR'S GUIDE, *supra* note 11, at 62.

81. Howard Gleckman, *10 Questions to Ask Before Buying Long-Term Care Insurance*, FORBES (Jan. 18, 2012, 11:40 AM), <http://www.forbes.com/sites/howardgleckman/2012/06/28/10-questions-to-ask-before-buying-long-term-care-insurance>.

82. Presumably, if the company sells policies with benefits that exceed five years, it does so on the assumption or actuarial evidence that few policy owners will ever qualify for benefits longer than five years. If the assumed number is low enough, the premiums charged for those policies will not rise enough to discourage sales of such policies. If, however, the assumptions about the number of those insured who qualify for benefits for longer than five years (and do so for a significant number of days) are wrong, the insurance company faces exposure to higher than projected benefit payments and so may suffer a loss if the premiums prove to be insufficient.

benefits and for how many days.⁸³ Statistics as to what percentage of LTCI policy owners collect benefits and for how long are not available because that is proprietary information.⁸⁴ However, the need for LTC among the elderly is known to some extent. The American Association for Long-Term Care Insurance (Association) published LTC statistics in its 2008 LTCI Sourcebook.⁸⁵ As pointed out by the Association, most LTC is actually received at home, but, unfortunately, there are few statistics about the extent of LTC provided in the home.⁸⁶ However, the Association did release statistics about LTC provided in a nursing home.⁸⁷

Average Length of Stays (Nursing Homes)

5 years or more	12.0%
3 to 5 years	12.0%
1 to 3 years	30.3%
6 to 12 months	14.2%
3 to 6 months	10.0%
less than 3 months	20.0%

Average Length Of Stay in Years

Female	2.6 years
Male	2.3 years
Married	1.6 years
Single / Never Married	3.8 years
Widowed	2.3 years
Divorced / Separated	2.7 years

83. See DENENBERG ET AL., *supra* note 32, at 30-33.

84. *Proprietary Information*, BLACK'S LAW DICTIONARY (10th ed. 2014) ("information in which the owner has a protectable interest.").

85. Press Release, Am. Ass'n for Long-Term Care Ins., 2008 Long-Term Care Insurance Industry Sourcebook Published (Mar. 3, 2008) (on file with company).

86. See *The Ability To Remain In Your Own Home Is One Of The Greatest Benefits Of Owning Long-Term Care Insurance*, AM. ASS'N FOR LONG-TERM CARE INS., <http://www.aaltci.org/long-term-care-insurance/learning-center/home-health-care.php> (last visited Aug. 31, 2015).

87. 2008 LTCI Insurance Fact File: Industry Data—Group LTCi, SOURCEBOOK 6 (2008), http://selectltc.com/Downloads/articles_studies/2008%20AALTCi%20Study.pdf.

As these statistics indicate, forty-four percent of those who enter a nursing home “leave” (either recover or die) within one year; only about twenty-five percent of those who enter a nursing home stay for three years or more. Given that most individuals never enter a nursing home, the above statistics make it clear that an individual’s need for care in a nursing home for three years or more is fairly low.

While statistics can tell what has occurred, they do not guarantee what will occur in the future. Apparently, insurance companies have had difficulty in projecting the risks associated with LTCI as demonstrated by the companies’ need to raise the premiums on existing LTCI policies.⁸⁸ The need to raise premiums for policies in force suggests that the projections used to set the original premium were incorrect.⁸⁹ That, in turn, shows that the companies may have underestimated benefit payouts, possibly because of unexpected adverse selection or moral hazard.⁹⁰

B. Adverse Selection

Adverse selection refers to the tendency of those, who are at an above average risk of suffering a loss, purchasing insurance at higher rates than the average potential purchaser.⁹¹ Those who consider buying an insurance product differ in their expectation or calculation of the likelihood of the feared loss. Many are simply more risk adverse, but some potential purchasers are better informed as to the probability of experiencing the loss than others. Because they have a higher-

88. See *Long-Term Care Rate History-Archive*, CAL. DEP’T OF INS., <http://www.insurance.ca.gov/01-consumers/105-type/as-guides/05-health/01-ltc-rate-history-active.cfm> (last visited Aug. 31, 2015). For a discussion of premium increases, see Shilling, *supra* note 7.

89. Thomas J. McInerney, CEO of Genworth Financial, the largest seller of LTCI policies with about thirty-five percent of the market, was quoted as stating that the need for asking for premium increases beginning in 2012 was that the insurance company made incorrect assumptions when it set premiums, particularly for policies issued before 2002. He did not explain which assumptions were incorrect. Ann Carrns, *Premiums Rise for Long-Term Care Insurance. Keep It or Drop It?*, N.Y. TIMES B7 (Mar. 21, 2014), <http://www.nytimes.com/2014/03/21/your-money/premiums-rise-for-long-term-care-insurance-keep-it-or-drop-it.html>.

90. One news report stated as much. Jesse Slome, executive director of the long-term care insurance industry trade group noted that insurance companies were becoming more selective in terms of accepting applicants, which translates into rejecting more applicants who represent adverse selection. See H. Cutner, *Long Term Care Insurance Discounts and Costs Vary Widely*, LIVE INS. NEWS (Aug. 28, 2013), <http://www.liveinsurancenews.com/long-term-care-insurance-discounts-costs-vary-widely>.

91. KENNETH A. ABRAHAM, INSURANCE LAW AND REGULATION 6 (Robert C. Clark et al. eds., 5th ed. 2010).

than-average expectation of incurring the loss, they are more likely to purchase insurance. They may be even better informed as to their risk of loss than the insurance company and therefore have an advantage over the insurance company in valuing the insurance.

Because the insurer cannot identify the likelihood of the need to pay for LTC for any particular purchaser of the insurance, the insurer must set the premiums at a price that represents the expected average loss for all purchasers.⁹² This projection, however, assumes little to no adverse selection, such as purchasing more of the insurance by those with a higher rate of risk.⁹³ To avoid adverse selection, the insurer attempts to reject applications by those with above-average risk.⁹⁴ For companies that sell LTCI, the primary way to reject is to insist on a physical and a family history of medical care to identify those more likely to eventually need LTC and so qualify for benefits.⁹⁵ However, because of asymmetrical information, the individual who is applying for LTCI may have better knowledge about his or her relative risk of loss, so, despite the best efforts of the insurance company, it is likely that some degree of adverse selection is present. It is certainly true that those who perceive a higher level of risk—whether or not the perception is correct—will be more likely to purchase the insurance.⁹⁶ To the extent the fear of needing LTC corresponds with the reality of needing it, some adverse selection occurs.⁹⁷ Adverse selection requires the seller of the insurance to set rates higher than if the risk was representative of the entire pool of purchasers.⁹⁸ Adverse selection, if correctly anticipated by the insurance company, therefore results in higher premiums.⁹⁹

As a result of adverse selection, LTCI is overpriced for most of those who purchase it. It is particularly overpriced for those who correctly perceive that they have a lower risk of loss, which includes those who expect that a great deal of free, voluntary LTC will be pro-

92. *Id.*

93. *Id.*

94. Peter Siegelman, *Adverse Selection in Insurance Markets: An Exaggerated Threat*, 113 *YALE L.J.* 1223, 1253 (2004).

95. Ronen Avraham, *The Economics of Insurance Law – A Primer*, 19 *CONN. INS. L.J.* 29, 44 (2012) (discussing the lack of clarity in whether the insurer will be successful in pushing back against adverse selection).

96. *Id.*

97. *Id.*

98. *Id.*

99. *Id.*

vided by a spouse or adult children.¹⁰⁰ The “overpricing” due to adverse selection likely discourages the purchase of LTCI by those who are at a lower risk of ever paying for LTC. The combination of lower-risk elderly not purchasing LTCI with higher-risk elderly purchasing it creates a reinforcing loop of even higher benefit claims that drive up premiums, which in turn discourages other low-risk elderly from purchasing LTCI. If the insurance company set the premium rate for the average level of risk, which due to unanticipated adverse selection is less than the actual level of risk insured, the company may need to increase premiums on preexisting policies, which, in turn, may cause some purchasers to allow these policies to lapse.¹⁰¹ If the cycle of higher premiums exist off low-risk purchasers and yet higher premiums still continue, it can result in a death cycle. Thus, the insurance product is essentially unsellable.¹⁰²

In reality, the market for LTCI does not feature a significant degree of asymmetrical information because most potential purchasers of LTCI cannot reasonably predict the likelihood that they will have to pay for LTC.¹⁰³ Still, even though potential purchasers may not accurately foresee whether they will need LTC, it is likely that those who purchase LTCI reflect some degree of adverse selection as well as the avoidance of the product by those who correctly believe that they will not incur significant LTC costs.

C. Moral Hazard

An even more likely cause of the difficulty for an insurance company in setting the premiums for LTCI is moral hazard, which is the ability of the insured to create eligibility for benefits by behaving in a way that increases the risk of the loss.¹⁰⁴ Although it is unlikely that individuals who own LTCI choose to live in a manner that increases their need for LTC,¹⁰⁵ moral hazard is possible because not all

100. Many may need LTC, but most of that care will be provided for free by spouses and other relatives. It is estimated that over half of all LTC is provided at no cost. H. Stephen Kaye et al., *Long-Term Care: Who Gets It, Who Provides It, Who Pays, And How Much?*, 29 HEALTH AFFAIRS 11, 20 (2010).

101. BROWNE, *supra* note 67, at 103.

102. *Id.*

103. Jeffrey A. Brown & Amy Finkelstein, *The Private Market for Long-Term Care Insurance in the United States: A Review of the Evidence*, 76 J. RISK & INS. 5, 14 (2009).

104. Avraham, *supra* note 95, at 66.

105. For example, some need LTC because of a broken hip. It seems improbable that just because an individual owns LTCI that he or she would be more likely to engage in activity that might result in a broken hip.

LTC qualifies for LTCI benefits.¹⁰⁶ As a result, the insured can create eligibility for benefits by choosing a form of LTC that triggers payment of the LTCI benefits.¹⁰⁷ For example, initially, an insured may be cared for at home at no cost by a spouse or child. The need to seek paid LTC, such as moving into a nursing home, may be dictated by a decline in the insured's health, but not always. Whether one should replace free care with paid assistance is often an elective decision based on the care needs of the insured, the extent of the burden of providing care on the caregiver, and the cost of the nursing home.¹⁰⁸ Within those variables lies a degree of moral hazard because the insured has the choice of whether to move into the nursing home and trigger the LTCI benefits.¹⁰⁹ Of course, often the insured's condition will deteriorate to the point that the volunteers can no longer provide adequate care, thus, there is then no choice but to purchase professional assistance. In other cases, however, the insured and the volunteers may agree that it is time to trigger the LTCI policy benefits by purchasing care even though the volunteers could continue to provide sufficient care.¹¹⁰ The volunteers may simply not see the point in not collecting insurance benefits that are "going to waste." Or, the insured may decide that he or she is too much of a burden for the volunteers and choose to hire professional assistance in order to permit the volunteers to reduce their commitment of time, energy, and emotional concern.

The moral hazard aspect of LTCI also arises because the need for LTC, that is, assistance with the activities of daily living, depends in part on what level of discomfort or inconvenience the individual is willing to endure.¹¹¹ Even if the insured has no volunteer assistance, some individuals will postpone and delay paying for LTC for as long

106. Nanda Kumar et al., *Understanding the Factors Behind the Decision to Purchase Varying Coverage Amounts of Long-Term Care Insurance*, 29 HEALTH SERVS. RES. 653, 654 (1995).

107. *Id.* at 656.

108. Brown & Finkelstein, *supra* note 103, at 17.

109. Under most policies, the insured could also obtain the LTCI policy benefits by hiring in-home assistance or moving into an assisted living facility. The insured must also meet the medical criteria for eligibility for benefits, but this discussion assumes that the insured's physical or mental condition meets those criteria.

110. A good example is an insured suffering from progressive Alzheimer's dementia. At some point, the insured will be so demented that the family volunteers can no longer meet his or her needs, but different families will determine that at different levels of the impairment of the insured.

111. Pauly, *supra* note 27, at 163.

as possible in order to avoid the cost of care.¹¹² Yet, if they have LTCI, there is much less incentive to delay the purchase of LTC. For example, if the individual owns a LTCI policy that pays a daily benefit of \$150, there is less reason to put off purchasing \$200 daily care, which would only cost the insured \$50 per day.¹¹³

Another form of moral hazard arises when the elderly person is not the driving force behind the purchase of LTCI. Some adult children urge their parents to purchase it so that the children will not have to provide free care. The children may even help pay for the premiums, which they perceive as insuring them from either having to personally care for—or having to pay for—care for their parents. Some may see LTCI as a means of protecting an anticipated inheritance from being depleted by the cost of LTC for their parents. If the desires and concerns of the children were the motivation for the purchase of the insurance, it is likely that the insured parent will resort to paid care much earlier than those whose children are willing to provide free care or financial assistance.

Moral hazard factors and adverse selection also arise from patterns of living and marriage.¹¹⁴ Current family patterns mean less family care.¹¹⁵ Families have fewer children, more women are in the work force and do not have the time to volunteer care, divorce may make the children less willing to provide care to the noncustodial parent, or adult children may be divorced or too involved with their own family issues to provide care. Many adult children face caregiving responsibilities for their own children.¹¹⁶ Fewer adult children live close enough to their parents to be able to provide care. Often, the smaller the size of current houses means it is unlikely that the aging parent

112. *Id.*

113. Co-pays and deductibles are used by insurance companies to reduce the risk of moral hazard. Avraham, *supra* note 95, at 72.

114. It is not clear whether the elderly who are single or who are married are more likely to purchase LTCI. Because spouses are the most prevalent form of voluntary LTC, it may be that single individuals lacking that form of free care might be disproportionate purchasers of LTCI or might be encouraged to do so by their children. That likelihood is off-set by the tendency of married couples to purchase LTCI for fear that the cost of care for one spouse will reduce or exhaust the couple's savings and so leave the non-disabled spouse with inadequate resources.

115. Richard Johnson et al., *Meeting the Long-Term Care Needs of the Baby Boomers: How Changing Families Will Affect Paid Helpers and Institutions*, in DISCUSSION PAPER SERIES, at 27 (The Retirement Series, 2007); Janice I. Wassel, *Family Aging and the Practice of Elder Law: A Financial Gerontology Perspective*, 3 NAELA J. 67, 69 (2007).

116. Wassel, *supra* note 115, at 69-70.

will move in with a child. All of these factors likely contribute both to adverse selection in those who purchase LTCI, as well as to the moral hazard of a longer period of benefit payments, because the purchaser will choose to trigger benefits sooner than a purchaser whose children or other family members are more able and willing to provide free LTC.¹¹⁷

VI. The Growth of Assisted Living as an Alternative to Nursing Home Care

Another possible explanation for higher than anticipated benefit payouts for existing policies is the rise of the use of care not provided in nursing homes, such as assisted living or care in the home.¹¹⁸ As with any risk, insurability depends to a great degree on the ability of the insurance company to project the probability of the risk, which, for LTCI, means the frequency of entry into a nursing home and the length of stay.¹¹⁹ When setting premium rates in the past, insurance companies focused on the number of policy owners that it expected to enter a nursing home, and for how long.¹²⁰ In making that determination, insurance companies could rely on the reality that all of those that it insured did not want to move into a nursing home. Simply put, older individuals are extremely reluctant to move into a nursing home and subject themselves to the inflexible, impersonal demands of institutional living.¹²¹ They often resist moving into a nursing home long after their condition would warrant such a move by relying on volunteer assistance from spouses or family members.¹²² This strong desire to avoid moving into a nursing home both delays the payment of LTCI benefits and reduces the time period for which benefits are paid

117. See BROWNE, *supra* note 67, at 102, 104, 110.

118. See Harris-Kojetin et al., *supra* note 8, at 3.

119. See generally BROWNE, *supra* note 67, at 100-01 (“insurers may not be able to classify risks with percission”); Kyle, *supra* note 56 (“An actuary attempting to price an insurance policy for a forty-year old individual must predict that individual’s likelihood of needing long-term care services several decades in advance.”).

120. Cohen et al., *supra* note 29.

121. See, e.g., FROLIK, *supra* note 12, at 281.

122. Some may delay entry so long that they die without ever entering a nursing home and so may never qualify for benefits. Others do finally move into a nursing home, but do not live beyond the elimination period and so may never collect benefits. And, of course, even those who eventually qualify for benefits will not reside in the nursing home for as long and so may receive fewer benefits under the policy. See Cohen et al., *supra* note 29 (describing how policyholders not wanting to go into nursing homes served as the primary risk management tool for managing claims on traditional long-term care insurance products).

by shortening the time between entry into the nursing home and death.¹²³ Presumably, insurance companies factor in this “delay” of movement into a nursing home when setting premium rates.

The reluctance of individuals to move into a nursing home has likely not changed much. What has changed, however, is the alternative of obtaining LTC in an assisted living facility, which has changed the map of long-term care.¹²⁴

Some older LTCI policies paid only for care provided in a nursing home, but that limitation has largely disappeared from more recent policies.¹²⁵ A LTCI policy now almost certainly pays benefits for policy owners who live in an assisted living facility or who live at home and otherwise meet the requirements for benefits.¹²⁶ Many older persons who would be very reluctant to move into a nursing home are willing to move into assisted living because it typically permits the resident to live in a single room (nursing homes almost always have shared rooms for two) and not be subject to the regimentation and sterile nature of nursing homes.¹²⁷ Simply put, a nursing home often resembles a hospital while assisted living has the appearance of a hotel.¹²⁸ The growth of assisted living is possible because many elderly who need LTC, but do not need daily medical care, are able to obtain

123. See generally Harris-Kojetin et al., *supra* note 8, at 3 (discussing consumer’s desires to stay in their own homes). See also *Planning for Nursing Homes and Long Term Care*, MACDONALD LAW OFFICE, LLC, http://maclaw-llc.com/index.aspx?TypeContent=ARTICLES&Art_Title=-Medicaid--Long-Term-Care--Nursing-Homes&art_id=509 (last visited Oct. 28, 2015) (“The insurance company wants to save on the costs of servicing the policies that they have issued, and keeping customers out of nursing homes as long as possible will advance that goal.”).

124. Neuhauser, *supra* note 26, at 48.

125. Kyle, *supra* note 56, at 106-07.

126. Typically, this is either an inability of performing two activities of daily living or a significant cognitive impairment that necessitates daily personal assistance. Activities of daily living are usually defined as bathing, toileting, eating, dressing and ambulating - the ability to get out of a bed or chair on one’s own. FROLIK, *supra* note 12, at 199.

127. Lawrence A. Frolik et al., *Housing Options for the Older Client*, 22 PROB. & PROP. 40, 41 (2008).

128. Most LTCI policies also pay benefits for care at home if the insured meets the policy requirements and pays for care. Typically, the policy daily limit will not be enough to pay for all of the care needed. The insured may not be able to afford the cost of care not covered by the policy. Even if cost is not a determining factor, many find it difficult to hire adequate care in the home or families may not feel comfortable with home care because of the heightened risk of substandard care and the need to supervise the care worker and the tax and payroll obligations associated with in-home care. For an extended discussion of assisted living, see FROLIK, *supra* note 12, at 193-206.

sufficient assistance in an assisted living facility.¹²⁹ Even individuals with significant cognitive decline, such as is caused by Alzheimer's disease, are often cared for in an assisted living facility that features special dementia wings or floors.¹³⁰

Because the purchaser of LTCI selects a daily benefit limit with the cost of a nursing home in mind, the much lower cost of assisted living may be less than the policy limit.¹³¹ For example, suppose the policy will pay up to \$200 per day. The insured's need for LTC causes her to move into assisted living. Initially, the daily cost is \$125 per day, so she collects \$125 per day from her LTCI policy.¹³² As a result, her cost of care in assisted living is essentially zero. If she remained at home and depended on volunteer care, she might not have any out-of-pocket cost for her care, but the heavy burden of care would fall on those who volunteered care, usually her spouse or adult children.

The attraction of the acceleration of claiming benefits by moving into an assisted living facility creates a moral hazard element that may help explain the pullout of many insurance companies from the LTCI market.¹³³ How soon a policy owner is willing to shift from voluntary care to paid care is very difficult to quantify. It may simply be so uncertain that it is a significant contributing factor to why insurance companies cannot set premiums at rates low enough to make LTCI an attractive insurance product for potential purchasers.

VII. The Nature of the Risk to the Insured Makes the Purchase of LTCI Problematic

For insurance to be viable, the risk of loss, the frequency, and the amount of benefit payments must be accurately forecast to permit the

129. Frolik et al., *supra* note 127, at 42.

130. *Id.*

131. An individual who owns a LTCI policy may therefore move into assisted living where the policy will pay for all of the daily cost and attempt to stay there as long as possible to avoid moving into a nursing home whose daily cost would exceed the policy benefit. See Brown & Finkelstein, *supra* note 26, at 7, 16.

132. Some policies permit the insured to "bank" any daily benefit that exceeds the cost of care. Richard L. Kaplan, *Business Law Forum: The Aging of the Baby Boomers and America's Changing Retirement System*, 11 LEWIS & CLARK L. REV. 407, 416-17 ("[T]he insured has a 'pool of funds' available equal to the maximum insured benefit..."). In the above example, where the daily benefit was \$175, but the cost of the assisted living care only \$135, the insured could bank the \$40 per day excess and apply it to the cost of care if she exhausted her benefits limits, such as three years of care.

133. Cohen et al., *supra* note 29, at 15.

setting of premiums.¹³⁴ The issuing insurance company must determine a premium¹³⁵ that will create enough revenue to make the product profitable for the insurance company, but still attractive to the potential purchaser.¹³⁶ To set the premium, the insurance company must make assumptions based on statistical probabilities about a number of factors, including: the number of policies expected to be sold, how long they will remain in force, the frequency and size of benefit claims by those insured, the projected rate of investment return on retained premiums, and projected marketing and administrative expenses.¹³⁷

The most insurable risks are those that have a high frequency of a small average loss.¹³⁸ LTCI insures risk with a moderate frequency of occurrence and a large average loss.¹³⁹ The likelihood of an owner of LTCI needing LTC is fairly high.¹⁴⁰ However, many will not need to pay for their LTC or will only need to pay for it for a limited time.¹⁴¹ The average length of stay in a nursing home or assisted living facility varies greatly and there is no good information as to the dollar cost to insurers attributable to those forms of care.¹⁴² Apparently, about two-

134. *See id.*

135. LTCI premiums vary according to the age of the purchaser; the older the purchaser, the higher the premium will be for the same product. Once set, the premium does not rise even as the insured ages. The insurance company, however, can request that the state regulatory agency permit it to raise the premium by a fixed percentage for existing policies if the premium rate is inadequate to support the benefit payouts generated by the insurance. Kaplan, *supra* note 132, at 434, 440.

136. *See generally* Neuhauser, *supra* note 26, at 44, 51 (discussing how cost is the most often cited reason for failing to purchase long-term care insurance).

137. THE ADVISOR'S GUIDE, *supra* note 11, at 90. At least one analyst believes that long-term care insurance has not been in effect long enough to obtain accurate information on the number of purchasers who will become eligible for benefits and the total cost of those benefits. Gary A. Simon, *Can Long-Term Care Insurance Be Fixed?* 37 J. HEALTH CARE FIN. 51 (2010). Although insurance companies thought they could accurately estimate both the number and cost of claims, apparently they were mistaken, as evidenced by requests in recent years for increases in premiums and the departure of insurers from the LTCI market. *See generally* Cohen et al., *supra* note 29.

138. BERLINER, *supra* note 73, at 41.

139. *See generally* BROWNE, *supra* note 67, at 99, 111 ("[L]ong term care is expensive.") ("Many during their lifetimes will have a need for long-term care.")

140. Mark Meiners, *Should You Purchase Long-Term-Care Insurance?: Yes: Don't Just Hope for the Best*, WALL ST. J. (May 14, 2012), <http://www.wsj.com/articles/SB10001424052702303425504577352031401783756>.

141. Prescott Cole, *Should You Purchase Long-Term-Care Insurance?: No: The Cost Is Too High*, WALL ST. J. (May 14, 2012), <http://www.wsj.com/articles/SB10001424052702303425504577352031401783756>.

142. The average length of time spent in a nursing home is difficult to document. Kemper et al., *supra* note 5, at 342. A surrogate is the length of life for those with dementia, the most prevalent cause of the need for LTC. One study found the fifty percent survival time in men was 4.3 years for those with mild dementia,

thirds of those who receive LTCI benefits initially apply for it as home care and, under some policies, the daily benefit paid is lower.¹⁴³ Due to the use of in-home care and the use of assisted living facilities, the average number of months for which benefits are paid is higher than the average time spent by a policy owner in a nursing home.¹⁴⁴ The policy owner may begin with the purchase of in-home care, later move to an assisted living facility, and finally move into a nursing home. Even so, most who are insured likely do not collect benefits for more than two years.¹⁴⁵ In short, benefit payments—losses—paid by LTCI companies have aspects of both frequent, but small losses, and less frequent, but large losses.¹⁴⁶

The reality is that individuals are more likely to purchase insurance to protect themselves against risks with a high frequency and a low average loss amount than to protect against risks with a low frequency of occurrence, but a very high average amount of loss.¹⁴⁷ This tendency to not insure very costly but low risk events likely accounts for the lack of consumer interest in LTCI. This is because if consumers correctly perceive the need for extended LTC as being a

2.8 years for those with moderate dementia, and 1.4 years for those within severe dementia. In women, the survival time was 5.0 years for those with those with mild dementia, 2.8 years for those with moderate dementia, and 2.4 for those with severe dementia. Ólafur Aevarsson et al., *Seven-Year Survival Rate After Age 85 Years Relation to Alzheimer Disease and Vascular Dementia*, 55 ARCH. NEUROLOGY 1226, 1229 (1998). These numbers indicate that once dementia has entered the moderate stage, on average, the individual has a life expectancy and, therefore, a need for LTC of fewer than three years.

143. *Association Address Long Term Care Insurance Fallacious Facts*, AM. ASS'N FOR LONG-TERM CARE INS. (Aug. 29, 2013), <http://www.aaltci.org/news/long-term-care-insurance-news/association-addresses-long-term-care-insurance-fallacious-facts>. Policies that have a lower daily benefit for in-home care create a higher co-pay for the policy owner.

144. Thomas Day, *About Nursing Homes*, NAT'L CARE PLAN. COUNS., http://www.longtermcarelink.net/eldercare/nursing_home.htm (last visited Aug. 31, 2015).

145. *Id.*

146. *Long-Term Care Insurance: Frequently Asked Questions*, LANDA UMPIERRE PSC, <http://www.landaumpierre.com/faq-longtermcare.php> (last visited Aug. 30, 2015).

147. "Many consumers do not voluntarily buy coverage against potentially risky and serious losses. For instance, fewer than half the residents in flood- and hurricane-prone areas were insured against water damage from Hurricane Katrina and Hurricane Sandy. . . . A principal reason for this insufficient coverage is that many people tend to view insurance as an investment rather than a protective measure. If after several years one does not make a claim, then there is very likely a feeling that ones' premium has been wasted." Howard Kunreuther & Mark Pauly, *Improving Insurance Decision Making*, REG BLOG (Mar. 4, 2013), http://opim.wharton.upenn.edu/risk/library/J2103RegBlog_HK-MP-Improving-Insurance-Decision-Making.pdf.

low or moderate risk, albeit a high cost event, they are less likely to purchase LTCI.

Those who do purchase LTCI are more fearful of paying for LTC for an extended time and are less concerned with the more likely shorter period of paying for LTC.¹⁴⁸ It is the fear of five years of care at a total cost of \$450,000 that motivates many to purchase LTCI.¹⁴⁹ Yet, even if they own LTCI that provides five years of benefits, they will still face paying a considerable amount for their care.¹⁵⁰

The daily benefit amount paid by LTCI is very unlikely to cover the full cost of care in a nursing home.¹⁵¹ It makes no sense for the purchaser to select a daily limit that will exceed the cost of nursing home care; to do so would mean paying a higher premium for an unnecessary benefit. The result, however, is that LTCI essentially creates a co-pay for the insured in the amount of the difference in the daily benefit and the actual daily charge by the nursing home. For example, if the policy benefit is \$200 per day, but the daily charge is \$225 per day, the insured has a de facto daily co-pay of \$25.

Further contributing to the lack of appeal of LTCI is the elimination period, which functions as a deductible.¹⁵² LTCI policies do not pay from day one of the incurred cost of care or from entry into a nursing home.¹⁵³ LTCI policies almost always contain an elimination period, typically thirty, sixty, or ninety days, during which time the insured is not eligible for benefits.¹⁵⁴ If, for example, the elimination period was ninety days, i.e. the insured is not eligible for benefits for the first ninety days of care, then LTCI benefits would begin on the ninety-first day.¹⁵⁵ The elimination period dramatically reduces the nature of the insured risk because it means that much LTC that is paid for is not insured even though short-term periods of residence in an

148. Jean Lown & Lance Palmer, *Long Term Care Insurance Purchase: An Alternative Approach*, 15 FIN. COUNS. & PLAN. EDUC. 1 (2004).

149. *Id.* at 2.

150. *Id.* at 9.

151. *Id.* at 6.

152. Cole, *supra* note 141.

153. *Id.*

154. *LTCI Policy Options*, WALL ST. INSTRUCTORS (2009), http://www.wallstreetinstructors.com/ce/continuing_education/ltc6/LTC4NAIC3_files/Page299.htm.

155. The elimination period usually applies to each separate residence in a nursing home or assisted living facility rather than being cumulative. For example, the insured enters a nursing home on June 1 and is discharged back home on June 30. She re-enters the nursing home on August 1 of the same year. She will not be eligible for benefits for ninety days after the August 1 re-entry.

assisted living facility or in a nursing home represent the most likely occurrence. The elimination period helps explain why, of those who buy LTCI at age sixty-five, only thirty-five percent will receive benefits.¹⁵⁶ If there was no elimination period, the percentage would rise to fifty percent.¹⁵⁷ The elimination period, together with the limits on the number of days of coverage and on the daily benefit amount, results in insurance coverage that, for most, would cover significantly less than their total incurred cost of LTC.¹⁵⁸

VIII. Additional Factors that Discourage the Purchase of LTCI

Because of adverse selection, insurance companies screen applicants and refuse those who are deemed to present an unacceptable risk, particularly those who might qualify for benefits in the near future.¹⁵⁹ According to the Association of Long-Term Insurance¹⁶⁰ the percentage of applicants by age who are rejected for coverage because of their health are:

Below age 50: 11%
Ages 50-to-59: 17%
Ages 60-to-69: 24%
Ages 70-to-79: 45%¹⁶¹

Insurance companies screen LTCI applicants by requiring physicals, inquiring about medical and family history, and may even

156. *What Is the Probability You'll Need Long-Term Care? Is Long-Term Care Insurance a Smart Financial Move?*, AM. ASS'N FOR LONG-TERM CARE INS. (2015), <http://www.aaltci.org/long-term-care-insurance/learning-center/probability-long-term-care.php> (last visited Aug. 27, 2015). Some policies that require a ninety day elimination period only apply it to institutionalized care, such as a nursing home or assisted living, but do not have an elimination period for home care. It is unclear whether the thirty-five percent rate of use estimate takes account of the possibility of a zero day elimination period. If it does not, the percentage of policy owners who will receive benefits would be somewhat greater than thirty-five percent.

157. *Id.*

158. Brown & Finkelstein, *supra* note 26, at 8. It is estimated that a policy with a sixty day deductible, four years of benefits and a \$150 per day (adjusted upward 5% per annum) will only pay for about two-thirds of expected LTC costs. *Id.*

159. James Capretta & Tom Miller, *How to Cover Pre-existing Conditions*, NAT'L AFFAIRS (Summer 2010), <http://www.nationalaffairs.com/publications/detail/how-to-cover-pre-existing-conditions>.

160. Slome, *supra* note 43.

161. *Id.* The higher rates of rejection with advanced aged likely indicates the operation of adverse selection.

attempt to use the applicant's genetic information, because both dementia and congestive heart failure appear to have a genetic causal component.¹⁶² Those who know that they have a genetic predisposition to needing LTC are more likely to purchase LTCI and do so when they are still young enough to qualify before the condition has manifested itself.¹⁶³ In response, an insurance company may legally acquire and use genetic information about the applicant that may result in the company refusing to sell LTCI to the applicant.¹⁶⁴ The result is a potential pool of purchasers who are healthier than the average older person.¹⁶⁵ Perversely, selling LTCI to healthier elders may result in more benefit claims.¹⁶⁶

On average, the healthy elderly have higher incomes and are likely to live longer,¹⁶⁷ but that longer life comes at a price. As they pass into their eighties, this population of potential LTCI purchasers is likely to suffer from a chronic condition that gives rise to the need for LTC.¹⁶⁸ For example, it is believed that forty-five percent of those age eighty-five or older have Alzheimer's or another kind of dementia.¹⁶⁹

Those with higher incomes who purchase LTCI likely apply for LTCI benefits earlier in time than lower income insureds because they will be more likely to seek out paid LTC earlier than those with lower

162. Michael Chamberlain, *Long-Term Care Insurance Becoming Tougher for Women to Purchase*, FORBES (Feb. 26, 2013, 12:52 PM), <http://www.forbes.com/sites/feonlyplanner/2013/02/26/long-term-care-insurance-becomes-tougher-to-purchase-for-women>.

163. Norma Coe et al., *Long-Term Care Insurance: Does Experience Matter?*, 40 J. HEALTH ECON. 122, 128 (2015).

164. Although the Genetic Information Nondiscrimination Act of 2008 protects Americans against discrimination based on their genetic information when it comes to health insurance and employment, the Act does not apply to the use of genetic information for underwriting purposes by insurance companies that sell long-term care insurance. Mark A. Rothstein, *HIPAA Privacy Rule 2.0*, 41 J. L. MED. & ETHICS 525, 527 (2013). The legal and practical realities that might permit an insurance company to use genetic testing to screen applicants for long-term care insurance are discussed in Mark A. Rothstein, *Predictive Genetic Testing for Alzheimer's Disease in Long-Term Care Insurance*, 35 GA. L. REV. 707, 707 (2001).

165. Sheila A. White, *Understanding LTC Underwriting Makes All the Difference*, LIFEHEALTH PRO (July 6, 2007), <http://www.lifehealthpro.com/2007/07/06/understanding-ltc-underwriting-makes-all-the-diffe>.

166. Rothstein, *supra* note 164, at 732.

167. Derek Thompson, *Get Rich, Live Longer: The Ultimate Consequence of Income Inequality*, ATLANTIC (Apr. 18, 2014), <http://www.theatlantic.com/business/archive/2014/04/more-money-more-life-the-depressing-reality-of-inequality-in-america/360895/>.

168. Alzheimer's Ass'n, *2012 Alzheimer's Disease Facts and Figures*, 8 ALZHEIMER'S & DEMENTIA 1, 42 (2012), http://www.alz.org/downloads/facts_figures_2012.pdf.

169. *Id.* at 14.

incomes.¹⁷⁰ A potential purchaser of LTCI ought to consider that the benefit paid by LTCI is a co-pay that lowers their cost rather than being a barrier to its use.¹⁷¹ For example, if the daily cost of a nursing home is \$250 and the daily LTCI benefit is \$200, the cost of nursing home care, once past the elimination period, is reduced by eighty percent to \$50 per day. For a higher income individual, paying \$50 per day for care that has a market rate cost of \$250 may seem sensible and so may hasten the time that they enter a nursing home.¹⁷² The lower income individual with LTCI is more likely to perceive the obligation to pay even \$50 per day (about \$1500 per month) as a significant cost barrier to entering a nursing home, and so will defer doing so for as long as possible despite owning LTCI.

Those who purchase LTCI are also likely to have more assets because protecting assets is a strong incentive to purchase LTCI.¹⁷³ Yet, paradoxically, having more assets makes paying for the elimination period as well as the “co-pay” of institutionalized care easier, thus making the co-pay less of a barrier to moving sooner into an institution, which thereby triggers the payment of benefits.¹⁷⁴ In contrast, those with lower incomes and fewer assets may rely on volunteer care for as long as possible in order to not incur fees for care.¹⁷⁵

Underestimation of the lapse rate by issuers of LTCI may also account for higher than anticipated benefit claims.¹⁷⁶ From the standpoint of the insurance companies, lapsed policies assure them of hav-

170. David Bear & Ellen O'Brien, *Federal Estate Income Tax Incentives for Private Long-Term Care Insurance*, AARP PUB. POLICY INST. 6 (Nov. 2010), <http://assets.aarp.org/rgcenter/ppi/econ-sec/2009-19-tax-incentives.pdf>.

171. See generally *A Shopper's Guide to Long-Term Care Insurance*, TEX. DEP'T OF INS. (July 2015), <http://www.tdi.texas.gov/pubs/consumer/cb032.html>.

172. It is also possible that the opportunity cost for those who provide free, voluntary care for a higher income person in need of LTC may be higher than the opportunity cost for someone providing free, voluntary care for a lower income person. For example, the adult child of a higher income parent is likely to have higher wage earning potential than an adult child of a lower income parent. For the higher wage earning adult child, the cost of not working or reducing hours spent working may be so costly that the child will encourage the parent to seek institutionalized care, either in an assisted living facility or a nursing home, and thereby trigger the payment of LTCI benefits. The lower wage earning adult child has less incentive to persuade a parent to move into an institution, something both the child and the parent are loath to see happen.

173. Cohen et al., *supra* note 29; Lown & Palmer, *supra* note 148.

174. See generally *Long-Term Care Insurance: What You Should Know*, NAT'L ASS'N OF INS. COMM'RS, http://www.naic.org/documents/consumer_alert_ltc.htm (last visited Aug. 31, 2015).

175. Cohen et al., *supra* note 29, at 2.

176. *Id.* at 10.

ing received premiums without the risk of paying benefits.¹⁷⁷ Along with those who die without ever paying for LTC, those who permit the policy to lapse subsidize those who continue to maintain the insurance until they qualify for benefits.¹⁷⁸ If the insurance company underestimates the lapse rate in the first few years after the policy is sold, it may also have underestimated the rate of benefit claims because claims rise with the age of the insured.¹⁷⁹ The lapse rate likely sharply declines the longer the policy is in effect because the insured is aware that the likelihood of needing LTC is increasing while the policy premiums remain constant. Having paid premiums for many years, a policy owner will be reluctant to let it lapse, knowing that he or she is entering the time of life that might make the purchase of that insurance a very financially successful choice. Lapse rates may also reflect adverse selection because those with declining health are more likely to keep the insurance in force.¹⁸⁰

To counter underestimation of the lapse rate and other variables, including higher than expected benefit payouts, the insurance company may raise premiums on existing policies.¹⁸¹ To do so, however, it

177. Voluntary (not due to death) lapse rates declined between from 5.2% from 2002-2004 to 3.8% from 2005-2007. Policies with lower annual premiums have higher voluntary lapse rates. THE ADVISOR'S GUIDE, *supra* note 11, at 93. This may reflect those who take out policies at a younger age when the premium is lower, let it lapse because the likelihood of needing LTC and qualifying for benefits seems a long way off. Those who bought the policy when older may have a more realistic understanding of the probability of needing LTC and thus the desirability of having LTCI.

178. *Id.* at 94.

179. Cohen et al., *supra* note 29.

180. Amy Finkelstein et al., *Dynamic Inefficiencies in Insurance Markets: Evidence From Long-Term Care Insurance*, 95 AM. ECON. REV. 224, 224 (2005). Conversely, higher than anticipated lapse rates can also be financially harmful to the insurer because every lapsed policy means fewer premiums collected. From the standpoint of an insurance company, the ideal lapse would occur the year before the policy owner needed LTC that met the policy's benefit eligibility requirements. Interestingly, the insurer's desire for long-term policy owners to permit a policy to lapse is the opposite of an insurer who sells auto insurance. The latter profits from long-term policy owners because benefit claim costs decline over time for two reasons. First, older auto insurance policy owners have fewer accidents than younger policy owners. Second, the higher risk policy owners who have had accidents are either required to pay higher premiums or have their policies cancelled. William H. Panning, *Asset-Liability Management for a Going Concern*, in THE FINANCIAL DYNAMICS OF THE INSURANCE INDUSTRY (Edward I. Altman & Irwin T. Vanderhoof eds., 1995).

181. As with all insurance, LTCI is subject to state regulation and approval of premium rates. Not surprisingly, sellers of LTCI are not permitted to raise premiums merely because the policy owner grows older and are more likely to need LTC. Moreover, policies typically suspend the payment of premiums during the time benefits are paid. In contrast, auto insurance policies are issued for only one

must first obtain the approval of the state insurance agency that regulates insurance companies.¹⁸² There is no guarantee, however, that a request for an increase will be granted or, even if approved, that the percentage increase will be as large as requested.¹⁸³ Moreover, a request for an increase in premiums means incurring costs in seeking approval and a possible delay as the state agency reviews the request.¹⁸⁴

Yet, another risk faced by insurance companies that sell LTCI are lower-than-projected investment returns on accumulated premiums.¹⁸⁵ Insurance companies have two sources of revenue.¹⁸⁶ One is premiums and the other is the investment return on the invested assets—the retained premiums—of the insurer.¹⁸⁷ When selecting investments, the insurer must balance the need for the safety of the principal—because it will be needed to pay benefit claims—against the relative rate of return on the investment.¹⁸⁸ The higher the rate of return means the lower the premiums need to be and the greater profit for the insurer.¹⁸⁹ The fundamental choice for the insurer is whether to invest in stocks or fixed income investments, primarily bonds.¹⁹⁰ Although the investment allocation varies among companies based upon the kind of insurance sold and the relative willingness to take risks, most insurers invest more of their assets in fixed income securities including government bonds, corporate bonds, and mortgages rather than in equities such as common stocks.¹⁹¹

year and the premiums can be adjusted every year and also reflect the number of claims filed by the insured.

182. An industry survey found that concern about the ability to obtain approval for rate increases by state insurance departments was the second most cited reason for insurance companies ceasing to offer LTCI. Cohen et al., *supra* note 29, at 28. For a discussion of state regulation of insurance, see *State Insurance Regulation*, NAT'L ASS'N OF INS. COMM'RS (2011), http://www.naic.org/documents/topics_white_paper_hist_ins_reg.pdf.

183. Cohen et al., *supra* note 29, at 28.

184. *Id.*

185. *Id.* at 10.

186. *Microstrategy Business Intelligence: Solutions for Maximizing Policyholder Profitability*, MICROSTRATEGY, <http://www.microstrategy.com/Strategy/media/downloads/white-papers/MicroStrategy-BI-Solutions-for-Maximizing-Policyholder-Profitability.pdf> (last visited Aug. 31, 2015).

187. *Id.*

188. DENENBERG ET AL., *supra* note 32, at 548.

189. *Id.*

190. Walter Blasberg et al., *Asset Allocation for Property and Casualty Insurance Companies*, in *THE FINANCIAL DYNAMICS OF THE INSURANCE INDUSTRY* 302 (Edward I. Altman & Irwin T. Vanderroof eds., 1995).

191. *Id.* at 302-03.

This large investment in fixed income investments means that the financial well-being of LTCI companies is very sensitive to interest rates. When those rates rise, the insurers reap greater returns on their investments.¹⁹² Yet, when interest rates decline, insurers experience a marked drop in revenues, possibly below the level projected as the minimum necessary to sustain the expected amount of benefit payments.¹⁹³ The low interest rates over the past years that have resulted in lower returns on retained premiums may account, at least in part, for the need of many insurers to seek a raise in premiums on outstanding policies.¹⁹⁴

IX. LTCI Offers Little Value to Most Single Persons

If judged by the low percentage of those age sixty-five and older who have purchased it, LTCI is not an attractive insurance product.¹⁹⁵ Perhaps, most Americans prefer to self-insure against the risk of incurring costly LTC. “Self-insurance” describes managing risk by setting aside a pool of money to pay for a possible, but uncertain, loss.¹⁹⁶ Self-insurance is often employed when the loss is likely, but the amount of the loss is relatively small.¹⁹⁷ If the risk of the occurrence of a small loss is very high, the cost of the premiums begins to equal the potential loss, in part, because the insurance company sets premiums at rates equal to the average loss, and also adds the cost of doing business and an expected profit.¹⁹⁸ Therefore, for the risk of small losses that have a high rate of occurrence, self-insurance is a rational response. Of course, the risk of paying for LTC does not fit that model, but nevertheless, self-insurance is a sensible choice for many.

192. Insurance companies presumably do not just “buy and hold” bonds, but actively trade them. Nevertheless, the higher the interest rate on bonds, the better the financial returns for the insurance companies.

193. Serena Ng & Leslie Scism, *Low Interest Rates Hurt Insurers’ Bottom Line*, WALL ST. J.: BUS. (Nov. 6, 2010, 12:01 AM), <http://www.wsj.com/articles/SB10001424052748704405704575596932278239578>.

194. The interest rate on ten year treasury bonds was 6.66% on Jan.1, 2000; 1.91% on Jan. 1, 2013; 2.86% on Jan. 1, 2014; and 1.88% on Jan. 1, 2015. *10 Year Treasury Rate by Year*, MULTPL.COM, <http://www.multpl.com/interest-rate/table> (last visited Aug. 31, 2015).

195. A 2004 study found that only ten percent of the elderly own LTCI. Brown & Finkelstein, *supra* note 6.

196. DENENBERG ET AL., *supra* note 32, at 124-25.

197. *Self-insure*, INVESTOPEdia, <http://www.investopedia.com/terms/s/self-insure.asp> (last visited Aug. 31, 2015).

198. DENENBERG ET AL., *supra* note 32, at 128-29.

Self-insuring the cost of LTC is also often the choice of individuals with considerable income and savings because the possible cost of LTC is a risk that they can afford.¹⁹⁹ Although a few may have adequate income to support the cost of whatever LTC they need, most do not, but they can still self-insure by having sufficient savings.²⁰⁰ For example, if LTC costs \$100,000 per year, even five years of care amounts to \$500,000 total, which may be affordable for those with assets of \$1,000,000 or more. A more likely cost of care would be two years of assisted living at \$40,000 and three years of nursing home care at \$100,000 per year for a total of \$380,000—again, a cost that the individual with a net worth of over \$1,000,000 can afford to pay for out of savings. Unless they are determined to protect the value of their estates, those with considerable net worth have the financial means to pay for LTC.

Even for single individuals with modest net worth, the purchase of LTCI is not compelling, except to preserve an estate.²⁰¹ For example, purchasing LTCI is not compelling for an individual with savings of \$250,000 (perhaps from a distribution from a 401(k) retirement account) and a house with a value of \$150,000, for a total net worth of \$400,000. Even ignoring his income, he can afford ten years of assisted living at a cost of \$40,000 per year or four years of nursing home care at a cost of \$100,000 per year. Of course, after exhausting his savings and the proceeds from the sale of the house, the individual would be eligible for Medicaid and so would continue to receive LTC.

199. THE ADVISOR'S GUIDE, *supra* note 11, at 156.

200. *Id.* at 56, 58.

201. To encourage the purchase of LTCI and so reduce the cost to Medicaid of paying for LTC in nursing homes, federal law permits states to participate in the Partnership Program and not impose eligibility for Medicaid or impose estate recovery on an amount equal to the benefits paid by LTCI. For example, the applicant received \$100,000 in LTCI, and having exhausted her rights to more benefits, qualifies for Medicaid as to the income requirements, but has \$100,000 in nonexempt assets. However, because of the receipt of the \$100,000 in insurance benefits, the applicant's \$100,000 is considered an exempt asset and so the applicant qualifies for benefits. After the death of the applicant, the state cannot impose estate recovery, *i.e.*, recover amounts spent for the nursing home care of the applicant. Joshua M. Wiener et al., *Federal and State Initiatives to Jump Start the Market for Private Long-Term Insurance*, 8 *ELDER L. J.* 57, 85-86 (2000). The Program has apparently not persuaded many to purchase LTCI. The value to the applicant is the ability to pass on assets to heirs equal to the value of the LTCI benefits. That possible benefit has not changed attitudes about the desirability of purchasing LTCI. Perhaps the cost of that potential legacy in the form of the insurance premiums that the applicant must pay for possibly many years, outweighs the possible benefit.

Moreover, LTCI provides only limited financial benefits: the daily benefit limit times the number of years of coverage, except for LTCI that pays lifetime benefits.²⁰² Expressed in present dollars, the total benefits paid by a LTCI policy can be surprisingly low.²⁰³ A policy that pays \$150 per day for up to five years will pay \$54,750 per year or \$273,750 for five years. How valuable to most potential purchasers is a policy really worth if its maximum payout is less than \$275,000? If the actual cost of care is \$225 per day or \$82,125 per year or \$410,625 for five years, the policy owner will have paid a co-pay of \$136,875. If the elimination period was ninety days, the policy owner will have to pay an additional \$20,250 for those ninety days, for a total cost of \$157,125. The LTCI will have paid only sixty-four percent of the cost of care for five years and ninety days. Even if the policy paid \$200 per day, the total value of the possible benefits would only be \$365,000. Those who can afford the cost of the LTCI premium are very likely to be able to absorb a possible, but unlikely, loss of \$365,000.

For an individual with net worth of \$1,000,000, a maximum benefit of \$273,750 represents twenty-seven percent of those assets. An individual with a net worth of \$1,000,000 has to ask whether protecting a little over a quarter of her net worth justifies buying LTCI, keeping in mind that it is not certain that she will incur any LTC costs, much less that she will qualify for five years of LTCI benefits. Insurance is supposed to be purchased for a loss you cannot sustain. A potential loss of twenty-seven percent of an estate seems like a sustainable loss for many potential purchasers of LTCI.

X. LTCI and Married Couples

The calculation of the financial risk posed by the cost of LTC is different for a married couple because of the effect on the noninstitutionalized, that is, the community spouse.²⁰⁴ If income from the couple's savings is necessary for the well-being of the community spouse,

202. The value of those benefits will grow if the policy contains a so-called inflation rider that guarantees an annual increase in benefits, such as five percent per year, but if the annual rise in the cost of a nursing home rise in the cost of nursing home care exceeds five percent, the policy benefits would be declining in absolute value.

203. Brown & Finkelstein, *supra* note 6, at 8.

204. Medicaid refers to the spouse of the Medicaid applicant as the "community spouse," no matter where he or she resides. 42 U.S.C. § 1396r-5(h)(2) (2012). In this Article, the spouse who is not living in an institution, a nursing home, or an assisted living facility will be referred to as the community spouse.

the couple may fear that paying for the LTC of one spouse may reduce the quality of life of the community spouse.²⁰⁵ However, the risk in the loss of investment income that supports the community spouse must be measured against the annual cost of LTCI premiums.²⁰⁶ If, for example, a couple has assets worth \$1,000,000 plus a house, and one spouse needs five years of care at a cost of \$100,000 per year for a total of \$500,000, all of which is spent out of their savings (the couple's income being needed to support the community spouse), the loss of income at the end of five years of paying \$500,000 of principal on care for the institutionalized spouse, at an after-tax rate of five percent, would be \$25,000. The remaining \$500,000 would produce \$25,000 annual income—down from the \$50,000 annual income produced by the original \$1,000,000.

That does not mean, however, that the community spouse's income would be cut in half. First, if the couple owns a house, the community spouse receives imputed income by occupying the house.²⁰⁷ Second, the community spouse is almost certain to receive Social Security.²⁰⁸ In 2013, the average Social Security benefit for a surviving spouse was \$14,928.²⁰⁹ The reality is that most couples with \$1,000,000 in savings were likely above-average earners who qualify for above-average Social Security benefits so that the community spouse would receive more than the average amount.²¹⁰ A community spouse, based on his or her own earnings record, in 2015, could receive as much as \$31,996 per year in benefits.²¹¹ Even if the community spouse did not qualify for significant benefits on his or her earnings record, at the

205. Kelly Green, *What You Need to Know About Long-Term-Care Insurance*, WALL ST. J.: RET. PLAN. (July 1, 2013, 11:01 PM), <http://www.wsj.com/articles/SB10001424127887323475304578501822156473886>.

206. See generally THE ADVISOR'S GUIDE, *supra* note 11, at 171-72.

207. 26 I.R.C. § 1041 (2012); Lewis Mendell, *Can you really live better longer without long-term care insurance?*, PBS NEWSHOUR (Mar. 20, 2014), <http://www.pbs.org/newshour/making-sense/can-really-live-better-longer-without-long-term-care-insurance/>.

208. *Retirement Planner: Benefits for You as a Spouse*, U.S. SOC. SEC. ADMIN., <http://www.ssa.gov/Planners/retire/applying6.html> (last visited Aug. 31, 2015).

209. *Social Security Basic Facts*, U.S. SOC. SEC. ADMIN., (Apr. 2, 2014), <http://www.ssa.gov/pressoffice/basicfact.htm>.

210. *Id.*; Nari Rhee & Ilana Boivie, *The Continuing Retirement Savings Crisis*, NAT'L INST. ON RETIREMENT SEC. 1 (2015), <http://laborcenter.berkeley.edu/pdf/2015/RetirementSavingsCrisis.pdf>.

211. This is assuming that the community spouse claimed benefits at her full retirement age, which is sixty-six for those born in 1943-1954. *Retirement Planner: Full Retirement Age*, U.S. SOC. SEC. ADMIN., <http://www.ssa.gov/retire2/retirechart.htm> (last visited Aug. 31, 2015).

death of the spouse who needed LTC, the community spouse would receive Social Security income in an amount at least equal to what the institutionalized spouse had been receiving.²¹²

After the death of the institutionalized spouse, based on receiving Social Security benefits equal to one hundred percent²¹³ of what the deceased spouse was receiving, assume the community spouse receives Social Security benefits of \$25,000 per year. Assume that while the institutionalized spouse, the husband, was alive, the community spouse, the wife, received \$15,000 in Social Security benefits based upon her own earnings record. While the husband was alive, and before the couple began drawing down their savings to pay for his care, the couple's pre-tax income was \$90,000: \$50,000 income from their savings²¹⁴ and combined \$40,000 (husband's \$25,000 and the wife's \$15,000) of Social Security benefits plus the imputed income from occupying the house. After the husband's death and after spending \$500,000 on his care, the wife would have income of \$50,000²¹⁵ plus the value of occupying the house. Ignoring the imputed value of the right to occupy the house, her pre-tax income would have declined by \$40,000 or by forty-four percent²¹⁶—a significant diminution even with the reduction of half of the number of persons in the household. As a result, the wife would suffer a decline in her standard of living and in the quality of her life.

For this couple, the purchase of LTCI that would cover either spouse who enters a nursing home might seem to be a wise choice. But a closer examination of the cost of LTCI insurance brings that analysis into question.²¹⁷ If they are both age seventy when they were to purchase LTCI that insured both of them, had a sixty day elimination period, a limit of three years of benefits at \$150 per day, and had a

212. *Id.*

213. *Survivors Planner: How Much Would Your Benefit Be?*, U.S. SOC. SEC. ADMIN., <http://www.ssa.gov/planners/survivors/ifyou5.html> (last visited Aug. 31, 2015).

214. This example assumes no change in the value of the \$1,000,000 savings. That is, withdrawal of the \$50,000 equaled the earnings on the savings.

215. \$25,000 from savings (\$500,000 × 5%) and \$25,000 from Social Security because as a surviving spouse she would receive an amount equal to 100% of his Social Security benefit. See 42 U.S.C. § 402(k)(3)(B) (2012).

216. Her consumable income would decline by a lesser percentage because her marginal federal income tax would be lower, and with lower taxable income, less of her Social Security would be subject to the federal income tax. See I.R.C. § 86 (2012).

217. At least one commentator has concluded that those with low to middle incomes cannot afford long-term care insurance premiums. Simon, *supra* note 137.

five percent annual increase in benefits, the annual premium would be in the range of \$7000.²¹⁸ Returning to the above example, the couple had a \$90,000 income, which, if they purchased LTCI, would be reduced by the \$7000 premium, leaving them \$83,000 or a 7.7% reduction in income.

If they had purchased LTCI, they would have paid \$50 per day for the husband's care (\$200 per day charge less \$150 per day insurance benefits) for three years (the benefit period of the policy) or approximately \$50,000, and having exhausted the insurance, they would then have paid \$100,000 each for two years.²¹⁹ They would have paid a total of \$250,000. Their savings would have declined to \$750,000 and the income from savings by about \$12,500 per year ($\$250,000 \times 5\%$).²²⁰ After the death of the husband, the wife's income would consist of \$25,000 from Social Security and \$37,500 from savings income for a total income of \$62,500.²²¹ The purchase of LTCI would have increased her income from \$50,000 to \$62,500, a twenty-five percent increase. Yet, paying the premiums for the LTCI would have reduced their income by 7.7% before the husband entered a nursing home.

This is the choice presented to the couple: is it worth it to them to accept a modest, but permanent reduction in income by buying LTCI to protect against a somewhat larger, but uncertain reduction in income caused by the need to pay for LTC? Another way of considering the matter is for the couple to ask how much current income are they willing to sacrifice for the right to collect up to \$164,250 of LTCI benefits (365 days for three years at \$150 per day would equal \$164,250).

If the couple wants more benefits and more protection for the community spouse, they could purchase insurance that extends five years and also increase the amount of the daily benefit. Doing so, however, would sharply raise the annual premium and so diminish

218. Premium costs vary greatly by insurance company and by the state where issued. In New York, the premium would be much higher. See, e.g., *What Policies Cost*, N.Y. ST., <http://www.nyspltc.org/benefits.htm> (last visited Aug. 30, 2015).

219. For purposes of simplicity, the sixty-day elimination period is ignored. The example also ignores the effect of inflation upon the cost of a nursing home, the purchasing power of the investment income, and the annual cost-of-living raises for Social Security benefits.

220. This assumes that the premiums for the insurance are suspended during the period of the payment of benefits.

221. The percentage difference is less if the imputed value of the house is included in her income under both scenarios.

the quality of life for them in the years before either one qualifies for the payment of the benefits.²²²

Even assuming the couple has fewer savings does not change the conclusion. For example, a couple, both age sixty-five, owns a house worth \$100,000 and has \$300,000 in savings. At age eighty, the husband enters a nursing home. He dies at the end of the third year. If we assume fifteen years of \$5000 per year premiums, the total cost of the insurance premiums would have been \$75,000. If we assume that the institutionalized spouse collects benefits for three years and the LTCI pays \$150 per day, or about \$55,000 per year for a three year total of about \$165,000, for which \$75,000 of premiums were paid, the insurance would have had produced a net value of only about \$90,000, which is not a great financial gain.²²³

By permitting couples to protect their savings from the cost of paying for LTC, owning LTCI can protect some of the surviving spouse's income in the years after the death of the institutionalized spouse.²²⁴ The longer the surviving spouse lives after the death of the spouse for whom LTC was needed, the greater the value of the LTCI to the extent that it protected the couple's savings and thus protected investment income available to the community spouse for the remaining years of her life.²²⁵ Conversely, the value of LTCI decreases if the community spouse dies before the institutionalized spouse or does not live very long after he dies.²²⁶ Thus, LTCI can be perceived as a

222. The couple can reduce the cost of the insurance if they purchase it when they are both age sixty rather than seventy. Doing so may cut the cost of the annual premium by more than half, but add ten years more of payments. If we assume the same insurance purchased at age sixty costs \$3000 versus the \$7000 cost at age seventy, and they pay premiums until age eighty-five, the total cost of the insurance acquired at age sixty would be \$75,000 (25 x \$3000) versus \$105,000 if taken out at age seventy. The savings in the cost of the premiums of \$30,000 does not markedly change the calculus when comparing the value of purchasing LTCI.

223. Many LTCI policies have a rider that automatically increases the daily benefit by a set percentage—such as five percent—per year. *See, e.g., Choosing among long-term care insurance riders*, INSURE.COM (last updated Jan. 12, 2010), <http://www.insure.com/long-termcare/riders.html>. The example in the text does not include such a rider, but the example also does not include the time value of the money spent on insurance premiums, which if assumed to be four or five percent per year largely offsets any increase in benefit amounts.

224. *See, e.g., Mark Patterson, 5 Ways to Protect a Surviving Spouse in Retirement*, U.S. NEWS: MONEY (June 17, 2010, 12:57 PM), <http://money.usnews.com/money/blogs/on-retirement/2010/06/17/5-ways-to-protect-a-surviving-spouse-in-retirement>.

225. *See generally Medicaid Protections for the Healthy Spouse*, ELDER L. ANSWERS, <http://www.elderlawanswers.com/medicaid-protections-for-the-healthy-spouse-12019> (last visited Aug. 31, 2015).

226. *Id.*

device to shift disposable income from the couple, by lowering it in the form of paying the annual premium to the surviving spouse in the form of protecting her income from the couple's savings. The success of that strategy, of course, depends upon the community spouse outliving the institutionalized spouse and doing so for enough years to offset the lowered standard of living caused by the payment of the LTCI premiums.

If the couple is concerned about preserving their estate, perhaps they should purchase second-to-die insurance, which will usually cost less than LTCI and is certain to pay benefits.²²⁷ "Buy LTCI or your spouse may become homeless," versus "Buy life insurance and your children will have an inheritance."²²⁸ A second-to-die policy that pays a death benefit of \$200,000 would be comparable in total value to a LTCI policy that paid \$200 per day for a maximum of three years that would have a total possible benefit payout of \$219,000.²²⁹ Yet, unlike LTCI, the life insurance policy is sure to pay the benefit.

For couples with very modest savings, LTCI offers little value. Imagine a couple with savings of \$60,000 and house worth \$100,000. They have annual income of \$50,000 from Social Security, \$23,000 per year for the husband and \$27,000 per year for the wife. If either must purchase LTC, the cost of that care, whether provided at home, in assisted living, or a nursing home, will soon exhaust their savings and overwhelm their income.²³⁰ To pay for LTC care, they will have to resort to Medicaid.²³¹ If the husband entered a nursing home at a daily rate of \$220, he would incur an annual cost of \$80,300. Medicaid eligibility rules require him to devote essentially all of his income towards the payment of the cost of the nursing home, or \$23,000.²³² His wife,

227. See, e.g., *Fundamentals of Estate Planning*, INS. C.E. COURSES 1, 31, http://www.insurancecourses.com/CE_courses/est_plan_pdf/Est_Plan.pdf (last visited Aug. 31, 2015).

228. Terence Lennon, *Objectives and Expected Impact of Risk-Based Capital Requirements for Life Insurance Companies*, in *THE FINANCIAL DYNAMICS OF THE INSURANCE INDUSTRY*, 13, 16 (Edward I. Altman & Irwin T. Vanderhoof eds., 1995).

229. *Fundamentals of Estate Planning*, *supra* note 227, at 64.

230. Marsha A. Goetting, *Medicaid and Long-Term Care Costs*, MONTGUIDE (revised May 15, 2015), <http://store.msuetension.org/publications/FamilyFinancialManagement/MT199511HR.pdf>.

231. For a detailed description of how Medicaid operates as a payor of long-term care, see FROLIK & BROWN, *supra* note 54 (discussing how Medicaid operates as payor of long-term care in Chapter 10.1).

232. He is allowed to retain a monthly personal support allowance that varies from state to state, but must be at least thirty dollars a month. For example, for a description of Washington's personal care allowance, see *Long Term Care--Personal*

the community spouse, is not required to use any of her \$27,000 annual income towards his care.²³³ She would also be able to retain a community spouse resource allowance, which, in most states, would be one-half of the couple's savings or \$30,000.²³⁴ Finally, she would be able to retain and live in the house for the rest of her life.²³⁵ At her death, in many states, Medicaid could put a lien on the house to recapture what it had paid on account of the husband and so effectively claim most, if not all, of the entire \$100,000 value of the house.²³⁶

The "cost" to the couple of the husband's annual nursing home cost would be \$53,000 the first year (\$30,000 of their savings plus his \$23,000 income) and his \$23,000 income for the years thereafter. If he stays in the nursing home for three years, the total cost to the couple would be \$99,000 (savings of \$30,000 plus income of \$69,000 (three years multiplied by \$23,000)). Medicaid would pay for the cost of the nursing home beyond the \$53,000 paid from his savings in the first year and his contribution of his \$23,000 income thereafter.²³⁷

Suppose the couple had purchased LTCI that paid a daily benefit of \$200 for up to three years for a total of \$219,000 with a ninety day elimination period. In the first year, the insurance would pay for 275 days of care or \$55,000. The couple would pay \$220 for the first ninety days and \$20 for the remaining 275 days or a total of \$25,300, which would reduce their savings to \$34,700. For the next two years, the couple would pay \$20 per day or \$7300 per year or \$14,600 for the two years. This would reduce their savings to \$20,100. After three years, the institutionalized spouse dies. While he was in the nursing home,

Needs Allowance (PNA) Chart, WA. ST. HEALTH CARE AUTHORITY (last revised Nov. 15, 2013), <http://www.hca.wa.gov/medicaid/manual/Pages/62-610.aspx>.

233. FROLIK & BROWN, *supra* note 54, at 14-23.

234. Thomas D. Begley, Jr. & Jo-Anne Herina Jeffreys, *Medicaid Planning for Married Couples*, 17-SPG NEALA Q. 19 (2004). To become eligible for Medicaid, the husband would have to "spend down" his \$30,000 allocated portion of the couple's savings. He does not have to spend it on the cost of his care in the nursing home but he might use it to partially pay for his first year in the nursing home. For a comprehensive discussion of Medicaid planning as a means of creating eligibility for Medicaid reimbursement of nursing home expenses, see Sean R. Bleck et al., *Preserving Wealth and Inheritance Through Medicaid Planning for Long-Term Care*, 17 MICH. ST. J. MED. & L. 153 (2013).

235. Begley & Jeffreys, *supra* note 234, at 4.

236. States may, but are not required to, impose a lien against the homes of Medicaid recipients to be foreclosed only upon the death of the recipient or the sale of the home. See 42 U.S.C. § 1396p(a)(1) (2012).

237. *Id.* With a modest amount of planning, the couple could retain or use the \$30,000 allocated to the husband for the benefit of the wife. But this example assumes no such planning took place.

the community spouse would have income of \$50,000. After the husband died, the community spouse would have Social Security income of \$27,000 and savings of \$20,100. But, there would be no Medicaid lien against the value of the \$100,000 house.

Compare the couple with LTCI to the couple who did not purchase it and relied on Medicaid to pay for the husband's nursing home care.

	LTCI	Medicaid
Wife's annual income	\$50,000 (total \$150,000)	\$27,000 (total \$81,000)
Wife's savings at the end of three years	\$20,100	\$30,000
Lien on House	No	Yes

The purchase of LTCI would have meant that the wife had \$69,000 in additional income over the three years, but \$8900 less savings or a net financial gain of \$60,100, and the house would not be burdened with a lien.

But the comparison must also account for the cost of the LTCI to the couple. Assume that the couple had purchased the insurance when the husband was age sixty-five and the wife was age sixty-three. Further, assume that thirteen years later, at age seventy-eight, the husband begins to show symptoms of dementia. For two years, the wife is able to care for him at home, but when he turns eighty, and she is seventy-eight, she can no longer care for him. She admits him to a nursing home, where he dies after three years at age eighty-three. The couple would have paid a LTCI premium for fifteen years at \$5000 per year²³⁸ for a total of \$75,000. The resulting value to the wife would have been \$60,100 with no lien on the house (the latter value is captured not by her, but by her heirs). The couple would have spent \$75,000 in LTCI premiums to generate \$60,100 in value to the wife, hardly a wise investment. Of course, if the husband had entered a nursing home at age seventy, the insurance would have proven a better value. But if he had not entered a nursing home until he was eighty-five, or not at all, the LTCI would have been an even more financially unwise purchase.

238. LTCI policies typically suspend the payment of premiums once the insured qualifies for benefits.

Is it sensible for the couple to purchase LTCI? Most observers think not.²³⁹ They contend that the cost of the insurance is a certain cost and one that is likely to rise as the insurance company imposes premium rate increases.²⁴⁰ During the years they pay premiums, the cost of those premiums lowers the couple's standard of living while the LTCI provides an uncertain and only marginal increase in the income of the community spouse.²⁴¹ True, the LTCI may protect the value of the house from a Medicaid lien, but that value accrues to the heirs, not to the couple. For many couples, buying LTCI merely to potentially protect their house from a lien while lowering their income for life appears to be a poor choice.

The better reason to purchase LTCI is to pay for care in an assisted living facility.²⁴² If one spouse needs LTC, he might be able to obtain it by moving into an assisted living facility, which, as discussed, costs about half as much as a nursing home and is a much more preferred source of care.²⁴³ But even at a monthly cost of \$40,000, a couple with limited assets will soon exhaust their savings paying for assisted living.²⁴⁴ LTCI, unlike Medicaid, will pay benefits for assisted living and so may permit the spouse to reside in assisted living for much longer before having to resort to a nursing home in order to qualify for Medicaid.²⁴⁵ Note, however, that using assisted living as the reason for buying LTCI depends on the assumption that the individual's need for LTC can be met in an assisted living facility, which is not true for those with medical care needs.²⁴⁶ The LTCI, therefore, will prove to be a "successful" purchase only if: (1) a spouse needs LTC for more than a few months; (2) the spouse's care needs necessitate the purchase of LTC (as opposed to being provided free care by the well spouse or family members); (3) the care can be provided for several months, if not years, in an assisted living facility; and (4) the spouse in

239. See, e.g., *Long-term-care insurance*, CONSUMERREPORTS.ORG (Aug. 2012), <http://www.consumerreports.org/cro/2012/08/long-term-care-insurance/index.htm> (advises that those with net worth below \$300,000 should not purchase long-term care insurance because the value of the assets that they are potentially protecting are not sufficient to warrant the cost of the insurance).

240. *Id.*

241. Anne Theisen Cramer & Gail A. Jensen, *Why Don't People Buy Long-Term-Care-Insurance?*, 61B J. GERONTOLOGY: SOC. SCI. S185, S189 (2006), <http://psychsocgerontology.oxfordjournals.org/content/61/4/S185.full.pdf+html>.

242. *Long-term-care insurance*, *supra* note 239.

243. *Market Survey*, *supra* note 4, at 4.

244. Kemper et al., *supra* note 5, at 335.

245. *Id.* at 343.

246. *Id.*

need of the care lives for a considerable period of time after the beginning date of purchasing the care. Given the number of prerequisites, the desire to insure the ability to purchase care in an assisted living facility does not seem to be a compelling reason to purchase LTCI.

XI. Alternatives to Basic LTCI

Because of the lack of appeal of LTCI, some insurance companies have responded by creating hybrid policies that combine LTCI with life insurance.²⁴⁷ In the most basic form, the policy offers a death benefit that can be accessed by the insured to pay for LTC with a corresponding reduction in the death benefit.²⁴⁸ For example, the policy might offer a death benefit of \$100,000. At age eighty, the insured enters a nursing home. She elects to draw down \$75,000 from her policy to pay for her LTC. She then dies. The policy will pay a \$25,000 death benefit. This product can be thought of as a traditional life insurance policy that contains the possible acceleration of the payment of benefits before death in the event that the insured incurs qualified LTC costs.²⁴⁹

The premium for a hybrid policy that pays a death benefit, which can be accelerated into payments for LTC, will be modestly higher than a standard, pay-at-death insurance policy because of the possible benefit payments prior to the actuarial projected date of death.²⁵⁰ The policy will also cost more than a pure LTCI policy be-

247. *Long-term-care insurance, supra* note 239.

248. THE ADVISOR'S GUIDE, *supra* note 11, at 85.

249. An alternative is a standard life insurance policy with an extended benefits option (at a higher premium) that provides LTCI at amounts that are much greater than the death benefit. For example, if the death benefit is \$100,000, the LTCI benefits might be \$200,000, which are in addition to the death benefits. Essentially, the purchase of life insurance is a requirement to be allowed to purchase LTCI. The life insurance policy is often sold as permanent insurance financed by a single pay premium with the LTCI rider being paid for by annual premiums. It is possible that the premium for the life insurance subsidizes the cost of the LTCI and so lowers its annual premium. Still other policies require the payment of a much larger single premium and no future payments for the LTC benefits. This prepayment of the LTCI premiums may be attractive to purchasers who like making a single "investment" to guarantee both life insurance benefits and LTCI benefits, with the LTCI benefits being the primary motivator and the death benefit the secondary consideration. THE ADVISOR'S GUIDE, *supra* note 11, at 85. Prepaying may also be attractive to those who are purchasing the life insurance and LTCI as a means of preserving the value of an estate. Presumably, the amount of the combined premium payments will be returned to the estate at the death of the insured or as benefits paid for the cost of LTC.

250. *Id.*

cause of the certain payment of the death benefits if the policy holder keeps the policy in force until death.²⁵¹ Put another way, pure LTCI policies provide more LTC coverage dollars per premium dollar paid than do hybrid policies.²⁵²

Often, these hybrid policies are paid for by a single up-front premium, which is necessary to protect the insurer against LTC cost claims being submitted relatively soon after the issuance of the policy.²⁵³ Some policies permit the cost to be paid over a term of years, such as ten.²⁵⁴ Of course, deferring the payment of the premium either increases the total cost of the policy or reduces the total benefits.²⁵⁵ The greater the upfront premium, the greater the amount of money available for LTC costs, with the average purchaser paying \$130,000.²⁵⁶ These single-premium policies are actually an investment, rather than insurance, with the LTCI benefits being an insurance add-on that helps sell the investment product.²⁵⁷ The death benefit of such policies often grows at a rate dependent upon the rate of return earned by the insurance company on the single premium. Such policies represent an investment because the purchaser expects to get back the entire initial "premium" and more. In contrast, with pure LTCI, the purchaser has no guarantee of ever recovering what was paid in premiums.²⁵⁸

The high upfront cost of these policies suggests that they appeal to individuals with higher net worth. They may also be attractive to those who own traditional insurance policies that have cash surrender value because they can "pay" the premium using the value of the traditional insurance policy by virtue of an I.R.C. § 1035 exchange of the life insurance policy for the hybrid life insurance and LTCI policy.²⁵⁹

251. *Id.*

252. *Long-term-care insurance, supra* note 239.

253. The premiums would be suspended during the period the policy owner qualified for benefits. And since death would be the likely event to terminate payment of benefits, the insurer would have paid out the face amount of the policy after collecting only a few months of premiums.

254. Presumably, if benefits are claimed before the end of the payout period, the amount of benefits are reduced by the amount of the unpaid premium.

255. Neuhauser, *supra* note 26, at 47 (discussing the benefits and costs of long-term care).

256. Anne Tergesen, 'Hybrid' Long-Term-Care Policies, WALL ST. J. (May 4, 2014), <http://online.wsj.com/news/articles/SB10001424052702304393704579530130606718764>.

257. THE ADVISOR'S GUIDE, *supra* note 11, at 85.

258. Tergesen, *supra* note 256.

259. 26 U.S.C. § 1035 (2012).

How popular such policies will prove to be is uncertain. The hope of insurance companies is that with a certainty of receiving benefits at death, if not sooner, potential purchasers will find these products attractive.²⁶⁰ That hope may be coming to fruition. While sales of pure LTCI policies fell by twenty-three percent to 233,000 in the five years that ended in 2012, sales of hybrid insurance policies rose almost fivefold to 86,000.²⁶¹ Still, selling fewer than 100,000 policies per year²⁶² is not evidence of a “successful” insurance product.

Another new insurance product is the term (time) limited annuity combined with a LTCI rider.²⁶³ The policy owner pays an upfront premium that purchases an annuity for a fixed number of years, as well as a LTCI policy that also pays a death benefit.²⁶⁴ The amount of LTCI benefits is a multiple of the value of the annuity.²⁶⁵ For example, if the annuity has a projected payment value of \$150,000, the LTC benefit might be an additional \$300,000 payable as a daily benefit that pays for a specified term of years. While the annuity is in payment mode, the LTCI rider will not pay benefits.²⁶⁶ The concept is that the annuity payment period delays the onset of the LTCI benefits until the policy owner is older and more likely to be paying for LTC.²⁶⁷ While in payment mode, the annuity is expected to help the owner of the annuity pay for LTC, should that be required. After the annuity payout period ends, the coverage by the LTCI commences and remains in place for the duration of the life of the insured. If the LTCI benefit never pays out or pays out for less than the benefit limit amount, at the death of the insured, a predetermined lump sum is paid to a designated beneficiary.²⁶⁸ As such, the LTCI is a hybrid in that it either pays LTCI benefits or it operates as life insurance and pays a death benefit.²⁶⁹

260. See David Port, 2013: *The Year of the Hybrid*, LIFEHEALTHPRO (June 24, 2014), <http://www.lifehealthpro.com/2013/06/24/2013-the-year-of-the-hybrid>.

261. Tergesen, *supra* note 256.

262. Marc A. Cohen et al., *Who Buys Long-Term Care Insurance?* 11 HEALTH AFFAIRS 208 (1992), <http://content.healthaffairs.org/content/11/1/208.full.pdf>.

263. Andrew Wone, *Another Option? The Future Combination Long-Term Care Policies Following the Pension Protection Act of 2006*, 3 NAELA 207, 224 (2007).

264. *Id.*

265. *Id.* at 229.

266. *Id.* at 233.

267. *Id.*

268. *Id.*

269. THE ADVISOR'S GUIDE, *supra* note 11, at 86. Another proposal is a single-premium life annuity with payments that increase if the individual meets a prescribed standard of need for LTC. The amount of the increase for LTC, however, is

These hybrid insurance policies, however, are essentially a product aimed at high asset individuals who can afford to pay high upfront premiums and who are motivated to do so to protect against the diminution of their estates due to the cost of LTC. Although called a hybrid, the policies more closely resemble single premium life insurance or an annuity that features the add-on of LTCI. As such, these products are not going to be attractive or affordable for most middle class Americans.

XII. Mandated LTCI?

In the absence of a viable insurance product, Medicaid will continue to bear most of the cost of LTC, which means state governments will face ever-increasing Medicaid LTC costs.²⁷⁰ Unlike the federal government, states do not have the option of running budget deficits to finance entitlement programs such as Medicaid.²⁷¹ As the cost of Medicaid rises, states must either raise taxes or spend less for other governmental activities. To lessen the pressure on state finances, the federal government could increase the percentage that it contributes to the program, but nothing in the current political climate suggests that increased federal assistance is forthcoming.

An alternative is to rethink how the nation finances LTC.²⁷² Neither traditional LTCI nor the new hybrid LTCI policies are the solution because private LTCI defines paying for LTC as an individual problem that can be met by the individual.²⁷³ That, however, is a fundamental miscasting of the problem. The cost of LTC, while falling on the individual, is better perceived as a societal problem. Growing old and needing to pay for care is a potential risk that all Americans face. Paying for LTC is a collective risk that deserves a collective response in the form of social insurance.²⁷⁴ Just as Medicare was finally seen as

only \$2000 per month. This is not nearly enough to pay for care in a nursing home and even when combined with the basic annuity of \$1000 per month and not even enough to pay the monthly cost of care in an assisted living facility. Mark J. Warshawsky, *The Life Care Annuity*, (Geo. U. Long-Term Care Fin. Project, Working Paper No. 2, 2007).

270. Bleck et al., *supra* note 234, at 155-56.

271. Watson, *supra* note 55, at 951.

272. Judith Feder et al., *Long-Term Care Financing: Policy Options for the Future*, GEO. U. LONG-TERM CARE FIN. PROJECT 71 (June 2007), <http://www.globalaging.org/health/us/2007/lctfinancing.pdf>.

273. *Id.* at 45.

274. For a discussion of why the government needs to step-in and protect the very old from poverty (which, *inter alia*, can arise from paying for LTC), see *general-*

the solution to paying for health care for the elderly, so too should the cost of LTC be seen as a societal problem that demands a political solution.

The cost of LTC fits the model of an insurance risk. Yet, the failure of private sector LTCI as a significant payer of the cost of LTC suggests that a public solution is necessary. After all, LTC costs are merely a subset of health care costs.²⁷⁵ A possible alternative that deserves public debate is mandatory LTCI. Just as the solution to paying for medical care for the elderly was subsidized health care insurance—Medicare—perhaps LTC should also be paid for by wage tax and general governmental revenues.²⁷⁶

Following the example of Medicare, LTCI could be mandated for older individuals, perhaps for everyone age fifty or older and be paid for in part by a dedicated wage tax and subsidized by general governmental revenues.²⁷⁷ Imposing a tax at age fifty would be consistent with the creation of an insurance product that is modestly subsidized by general government revenues, the latter being needed to capture non-wage wealth that accrues to higher income taxpayers.²⁷⁸ In turn, the wage tax would ensure that the insurance covered almost all—much like Social Security—wage tax creates eligibility for its benefits for almost all Americans.²⁷⁹

ly Jonathan Barry Forman, *Supporting the Oldest Old: The Role of Social Insurance, Pensions, and Financial Products*, 21 *ELDER L. J.* 375 (2014).

275. See generally *id.*

276. Expanding Medicare to pay for LTC has been proposed. The focus of the paper is on the funding mechanism rather than the implementation. The authors of the proposal do not address how the program would be administered, that is, who would determine when an individual is eligible for the benefits and what standards would be used to make that determination. Leonard E. Burman & Richard W. Johnson, *A Proposal to Finance Long-Term Care Services Through Medicare with an Income Tax Surcharge* (Geo. U. Long-Term Care Fin. Project, Working Paper No. 8, 2007).

277. See generally, Lawrence A. Frolik, *The Need for Mandatory Long-Term Care Insurance*, N.Y. U. REV. EMP. BENEFITS & EXEC. COMPENSATION (2010) (Chapter 1C).

278. Imposing the tax at age fifty would help relate the tax to the possible risk of paying for LTC, a risk that those under age fifty are unlikely to accept as a risk that they should insure against. Like Medicare, a wage tax could be on all wages, unlike Social Security that only taxes wages up to \$118,500 (adjusted annually for inflation). 2015 *Social Security Changes*, U.S. SOC. SEC. ADMIN., <http://www.ssa.gov/news/press/factsheets/colafacts2015.html> (last visited Aug. 31, 2015). Assuming that the wage tax was set at a single flat rate, the wage tax portion of financing it, would nevertheless result in higher wage earners subsidizing the insurance of lower wage earners by paying more for the same benefits.

279. According to the Government Accountability Office, in 2007, the Social Security system covered approximately ninety-six percent of the American workforce. Francine Lipman & Alan Smith, *The Social Security Benefits Formula and the*

Medicaid would be largely replaced as a payor of LTC; the mandated LTCI would pay for the LTC costs of older individuals. And while the public LTCI would indeed be insurance and not a means-tested welfare program like Medicaid, the policies could contain extended elimination periods to discourage premature triggering of benefits. To avoid excessive use of assisted living facilities and to promote voluntary, free care, the benefit amount paid for assisted living could be set below the average daily cost charged by assisted living facilities. Similarly the benefit amount for nursing home care could be set below the expected daily cost, perhaps, with the benefit being a percentage of the daily cost, rather than a fixed dollar amount, to reflect the variance in nursing home costs across the nation. Benefits could also be paid to in-home care that is defined along the lines of the current Home and Community based case; that is, limited dollar amounts for limited forms of care. Whatever the level of care, the insurance would only pay for a set number of years, perhaps four. The combination of extended elimination periods, limited daily benefits capped at rates that reflect the form and cost of the provided care, and a restriction on the number of years of benefits would help keep the total benefit payments in check and help make the insurance supportable through wage tax and general revenues.²⁸⁰ Medicaid would have to continue to exist as a source of payment for the elimination period and as daily co-pay for those unable to afford even these more modest costs. The insurance benefits, however, would greatly reduce the cost to Medicaid of paying for the LTC of the elderly. Most of the cost of that care would be shifted to individuals in their working years by the imposition of wage taxes and to the federal government's general revenues.

State Medicaid agencies would continue to play an important role by virtue of determining who qualifies for insurance benefits. Just as private insurance companies must exercise care in approving the payment of benefits, so should the public LTCI.²⁸¹ Each state, in

Windfall Elimination Provisions: An Equitable Approach to Addressing Windfall Benefits, 39 J. LEGIS. 181, 183 (2013).

280. The savings in Medicaid expenditures for LTC could be the source of the general revenue support of the payment of benefits. The savings in Medicaid expenditures by the states could also be diverted to paying benefits as the determination of eligibility for benefits could be determined at the state level.

281. Insurance company denials of claims for benefits has led to allegations that often these denials are not made in good faith. Michael C. Abourezk & Alicia Garcia, *Long-Term Care Insurance: How to Recognize Improper Claim Denials*, 23 NO. 1 EXPERIENCE 30 (2013).

effect, would act much like the claims department of an insurance company and adjudicate whether the insured's psychological and medical needs qualified them for the insurance benefits. Private LTCI would continue to have a market by insuring elimination period co-pays and extending benefits beyond the time limit of the governmental LTCI and so resemble private Medigap insurance policies that offer reimbursement for medical costs that are not covered by Medicare.²⁸²

Japan and Germany both mandate LTCI.²⁸³ While the details of those plans differ, the larger point is that these countries realize that LTC is a universal risk that is best met by universal insurance. Private, voluntary LTCI has failed to meet the need. The current modest subsidy provided by federal income tax incentives have not been able to generate much demand for LTCI.²⁸⁴ The time has come to admit that LTC needs a much larger source of stable funding. Public, mandatory LTCI is the answer. As we age, we are all potential users of LTC; thus, we should all be required to buy insurance to pay for that care and hope we never need to collect benefits.

282. *MedigapPlans 2015*, MEDIGAPPLANS2015.COM, <http://www.medigapplans2015.com> (last visited Aug. 31, 2015).

283. GLECKMAN, *supra* note 1, at 6-7; James C. Campbell & Naoki Ikegami, *Long-Term Care Insurance Comes to Japan*, 19 HEALTH AFFAIRS, 26, 39 (2000); Alison Evans Cueller & Joshua M. Wiener, *Can Social Insurance for Long-Term Care Work?: The Experience of Germany*, 19 HEALTH AFFAIRS 8 (2000); Joseph White, *(How) Is Aging a Health Policy Problem?* 4 YALE J. HEALTH POL'Y L. & ETHICS 47, 65 (2004).

284. In 2015, LTCI premiums are deductible up to an amount of \$4660 for a taxpayer age seventy-one or older. I.R.C. § 213(d)(1)(C). Tax incentives in the form of a deduction for premiums disproportionately benefits higher income taxpayers who are subject to higher marginal tax rates. But, as shown, this population is unlikely to find LTCI to be an attractive product. Wiener et al., *supra* note 201, at 98.