

LONG TERM CARE FUNDING: "I THINK I WILL SELF-INSURE"

by John B. Linvill, Jr., CSA ~ Updated April, 2008

If the bull market had continued, I suspect most people would be very confident of their ability to self insure the potential cost for long term care. After all, one would expect one's financial resources to grow by 12-20% annually. We would all be retiring 5 years earlier than planned. Life would be good!

We would not be focused on the 5-5+% annual cost increases for all types of long term care. Today's local cost of high-level assisted living care is \$200 a day. In 30 years with 5% compounded care inflation, the annual cost for one person could be as much as \$315,000. If four years of care are needed, the cost could be \$1,200,000. With nursing home daily cost running at \$250, in thirty years the annual cost could be \$394,000 - (assuming 5% compound growth).

Many people who decide to self insure (no matter what level of wealth) are uninformed about potential life expectancies, future cost of care, etc. Also, many of these individuals are totally focused on a tight budget because it makes them feel more secure. Thus they do not wish to pay a relatively modest LTC insurance premium. Some people (usually men) just do not want to formally acknowledge that they may need care in the future. Signing a LTC insurance application is seen as an acknowledgement of this fact. Others are willing to take the risk of self insurance because they do not mind eventually having their children care for them. After all, the parents have sacrificed for their children and long term care is "pay back time". They have not focused on their own independence and the impact that care will have on their children's lives. Finally, there are those people who really believe that they will pass away quickly from a heart attack, etc. They have not asked themselves the following: "Am I right about everything? Can I afford to be wrong about a quick death departure?"

Suppose I want to establish a LTC self insurance plan. This means that I am willing to take all the financial risk for funding my care. Here are the variables:

One needs to invest a certain amount of dollars each year to create an adequate pool of capital for the projected LTC costs. What is the assumed cost of care inflation rate? 5% or maybe 6+%? A one percent increase in care inflation over just 10 years will move final costs up dramatically. What impact will the 37.7 million baby boomers (age 45-54) have on the long term care demand side as they live longer? What is my annual return on my LTC self insurance fund?

How many years of care may I need... 0,1,2,3,4,5,6,7,8,9,10+? If I only knew how many years of care I will need, I would be able to calculate an annual contribution to my LTC expense fund. Will I have Alzheimer's and required care for 8-12 years?

Thus, it is impossible to properly plan a reliable long term care self insurance funding program. There are

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just too many unknown variables.

People who claim to want to self insure are not doing any specific dollar allocations each year toward a LTC fund. They are satisfied to risk their assets (& family assets). Many American families will just continue on without ever knowing the issues around funding long term care needs.

My clients purchase LTC insurance policies for *peace of mind*. They value their *independence, security and dignity*. They have worked hard over their lives and do not wish to put their resources at risk. They are not large risk takers. They just do not want to worry about funding the care.

If care is needed, everyone wants quality care but no one wants to pay for it.

My clients tell me that they hope they never have to use the insurance policy but they do not want to be without it.

This is why 98.5% of long term care policyholders continue to pay their premiums each year to death or disability. No other insurance product has this high level of persistency. Again, the goal is independence, security and dignity.

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Inflation calculations are based upon current economic statistics and estimates for the Philadelphia area.
