The Impact of Long-Term Care Costs on Retirement Wealth Needs

(Selections from Society of Actuaries Monograph: Managing the Impact of Long-Term Care Needs and Expense on Retirement Security: A Holistic and Multi-Generational View)

Presented by Anna Rappaport, FSA, MAAA
To NASI Round Table

January 28, 2015
Agenda

- Big picture
- Modeling results
- Four methods of private financing
- Conclusions
SOA Paper Call and Monograph*: Questions addressed

- How can individuals and families protect themselves from the expense of LTC needs?
- How can they protect against potential financial ruin?
- How can advisors help their clients improve decision making?
- Are there better ways to frame and communicate challenges and possible solutions?
- Are there better product designs (private and public)?
- Are there alternative financial approaches?
- How can individuals and families finance LTC needs while addressing basic retirement income needs and asset protection?

*Monograph available online from Society of Actuaries: https://www.soa.org/Research/Research-Projects/Ltc/research-2014-ltp-ltc.aspx
Long-Term Care and Retirement Security: What Are the Issues?

Wealth needs of the individual, spouse and other generations of family are affected

- Cost of a major long-term care event: depletes retirement assets for families who purchase services
- Impact on the surviving spouse
- Added responsibility and financial burden placed on caregiving family members
- Health and long-term care costs over what is planned for, and they outpace general inflation
- Increased longevity: greater likelihood of needing care
- Limited participation by middle income earners in the private insurance market

Also societal impact: On Social Security, Medicare, and Medicaid
How Long-Term Care Affects Seniors

<table>
<thead>
<tr>
<th>Duration of Expected LTSS Need for Persons Turning 65</th>
<th>Distribution of Future LTSS Cost for Persons Turning 65</th>
</tr>
</thead>
<tbody>
<tr>
<td>▪ None – 31%</td>
<td>▪ None – 50%</td>
</tr>
<tr>
<td>▪ Under 1 year – 17%</td>
<td>▪ Under $10,000 – 25%</td>
</tr>
<tr>
<td>▪ 1-2 years – 12 %</td>
<td>▪ $10,000 - $25,000 – 7%</td>
</tr>
<tr>
<td>▪ 2-5 years – 20%</td>
<td>▪ $25,000 -- $100,000 – 12%</td>
</tr>
<tr>
<td>▪ 5+ years – 20%</td>
<td>▪ $100,000 or more – 6%</td>
</tr>
</tbody>
</table>

Long-term care also affects caregivers and family members

Source: Federal Long-Term Commission report, page 24 and 25
Private Long-Term Care Insurance

- About 10% of population have coverage in the United States
- Usually pays benefits based on inability to perform 2 of 6 (or 2 of 5) activities of daily living
- Different types of policies
  - Stand-alone long-term care
  - LTC combined with life or annuity products
- Number of companies in market has declined and rates have risen
- Eligible for tax benefits if certain requirements are met (HIPAA) (New policies sold are generally tax qualified)
- Many seniors need some support but do not have current level of disability that makes one claim eligible
## Women Expected to Need Long-Term Care Longer than Men

### Life Expectancies in Years

<table>
<thead>
<tr>
<th>Age and Gender</th>
<th>Non-disabled</th>
<th>Mild or moderate disability</th>
<th>More severely disabled</th>
<th>Total Life Expectancy</th>
</tr>
</thead>
<tbody>
<tr>
<td>Male 65</td>
<td>12.3</td>
<td>1.5</td>
<td>1.5</td>
<td>15.5</td>
</tr>
<tr>
<td>Female 65</td>
<td>13.6</td>
<td>3.0</td>
<td>2.8</td>
<td>19.4</td>
</tr>
<tr>
<td>Male 85</td>
<td>2.9</td>
<td>1.0</td>
<td>1.8</td>
<td>5.7</td>
</tr>
<tr>
<td>Female 85</td>
<td>2.5</td>
<td>1.7</td>
<td>3.0</td>
<td>7.2</td>
</tr>
</tbody>
</table>

**Note:** Women less likely to have spouse who can offer care

Source: Stallard, Eric, Estimates of the Incidence, Prevalence, Duration, Intensity, and Cost of Chronic Disability Among the U.S. Elderly, Society of Actuaries Living to 100 Monograph, 2008
The Impact of LTC Costs on Retirement Wealth Needs: Paper overview

- Authors: Vickie Bajtelsmit & Anna Rappaport
- Background on retirement and long-term care
- Discusses impact on women
- Sets up four methods for private financing of long-term care
- Presents simulation research from SOA Retirement Adequacy Study
- Provides areas for further research
Background

- Major LTC event can devastate retirement security for most households. For households below median who need an extended stay in nursing home, Medicaid is probably only viable option.
- Major private methods of financings LTC include insurance, savings, CCRCs, and use of home equity. Can be combined.
- None of these match needs perfectly. Some have better chance than others depending on situation.
- Longest lived people most likely to have major needs.
- By age 80, 1/3 have some disability and by 86, majority have disability.
- Women have greatest challenges.
Building Long-Term Care into Stochastic Retirement Modeling

**EBRI model**
- Aggregate approach
- Focuses on entire population
- Identifies % of population who will not have enough money

**SOA Retirement Adequacy Study**
- Individual approach
- Focuses on sample individuals near the middle
- Estimates how much money a household needs for retirement success

**Both studies:**
- Shocks including long-term care are important
- Long-term care is a major factor in inadequate assets
## SOA Study: Effect of LTC Insurance on Retirement Adequacy

### Wealth Needed at Retirement in 000s

<table>
<thead>
<tr>
<th></th>
<th>Base Case: No LTCI</th>
<th>Buy LTCI for Both Spouses</th>
<th>Buy LTCI for Wife</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Median family</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Wealth at retirement:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>50(^{th}) percentile</td>
<td>$170</td>
<td>$227</td>
<td>$195</td>
</tr>
<tr>
<td>95(^{th}) percentile</td>
<td>$686</td>
<td>$333</td>
<td>$338</td>
</tr>
<tr>
<td><strong>75(^{th}) family</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Wealth at retirement:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>50(^{th}) percentile</td>
<td>$544</td>
<td>$599</td>
<td>$581</td>
</tr>
<tr>
<td>95(^{th}) percentile</td>
<td>$1,011</td>
<td>$851</td>
<td>$871</td>
</tr>
</tbody>
</table>

Median family: $60,000 income and $100,000 non-housing wealth
75\(^{th}\) family: $105,000 income and $250,000 non-housing wealth
Observations

- EBRI and SOA-RA models include long-term care and health risk in broader retirement simulation models. Many models exclude these risks.
- Results are very different when these risks are included. Huge difference between 50th and 95th percentile because of shocks.
- Strategies like changing retirement age or reducing spending help at the median but can’t handle the full impact of shocks.
- Advance planning for LTC very important for low and middle income households.
- LTC insurance can be useful for those in middle-income brackets.
## Four Options for Financing Care

<table>
<thead>
<tr>
<th></th>
<th>Insurance</th>
<th>Savings</th>
<th>CCRC</th>
<th>Housing Equity</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Prevalence</strong></td>
<td>&lt; 10%</td>
<td>15% of care pd out of pocket</td>
<td>Low overall, higher net worth only</td>
<td>Little use of reverse mortgages</td>
</tr>
<tr>
<td><strong>When to do</strong></td>
<td>While still healthy</td>
<td>Ongoing – all ages</td>
<td>Time of entry and monthly</td>
<td>When needed</td>
</tr>
<tr>
<td><strong>Match to needs</strong></td>
<td>Depends on contract, situation</td>
<td>No direct match</td>
<td>Depends on contract, situation</td>
<td>No direct match</td>
</tr>
<tr>
<td><strong>Applies to</strong></td>
<td>Middle and upper income</td>
<td>Higher income and net worth</td>
<td>Higher net worth</td>
<td>All levels who own home</td>
</tr>
</tbody>
</table>
### Four Options for Financing Care (cont’d)

<table>
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<tr>
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</tr>
</thead>
<tbody>
<tr>
<td><strong>Risks</strong></td>
<td>Premium increases, costs exceed limits, situation not covered</td>
<td>Investment risk, may not have enough money, difficulty of managing assets</td>
<td>Monthly costs can increase, bankruptcy risk, don’t know if needs covered</td>
<td>Equity unmatched to need, illiquidity, interest rates affect reverse mortgages</td>
</tr>
<tr>
<td><strong>Costs no LTC need</strong></td>
<td>Premiums paid</td>
<td>None</td>
<td>Buy-in price, higher monthly premiums</td>
<td>None</td>
</tr>
<tr>
<td><strong>Issues for surviving spouse</strong></td>
<td>Reduces risk of asset depletion</td>
<td>Survivor may not have enough assets left</td>
<td>Security of CCRC; higher monthly costs; possible relocation</td>
<td>Survivor may not have enough assets left</td>
</tr>
<tr>
<td><strong>Taxation</strong></td>
<td>Some policies tax advantaged</td>
<td>Most retirement savings tax deferred</td>
<td>Part of price = insurance premium</td>
<td>Gain on sale of house often tax free</td>
</tr>
</tbody>
</table>
Ideas for Further Research

- Look at more refined model with regard to:
  - LTC events
  - Variations of insurance solutions
  - Comparisons of financing methods
  - Medicaid
  - Family support strategies
  - Individuals tested

- When is insurance superior to use of savings and housing equity?

- How do CCRC’s fit into the picture?
Conclusions

- Risks, including LTC, are critical part of retirement financing; most people do not have enough money to cover the risks
- The retirement planning aspect on family members and of serving as a caregiver is often overlooked
- No method of private financing is a perfect match and risk free
- Insurance can be very helpful to the middle market
- CCRCs can be very helpful, but are limited to more affluent and entail risks
- Major events requiring marketplace care will often deplete assets and need to be financed by Medicaid
Thank You!