Long Term Care University

Long Term Care University – Question of the Month

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Q: We are considering removing the inflation protection feature before buying our long term care insurance policy. What are the advantages and disadvantages of purchasing polices with inflation protection?

The Problem – Determining Whether or Not to Purchase Inflation Protection
Most long term care insurance policies offer you the option to remove the inflation protection option from your policy when applying. Many consumers purchase an adequate amount of care per day (daily benefit) and an adequate amount of care over the life of their policy (total pool of money). Unfortunately, many consumers shortchange themselves when they either forgo the purchase of inflation protection or they purchase an inadequate level of inflation protection. **A policy with adequate coverage today, which has inadequate or no inflation protection, simply cannot keep pace with the 5% compound price increases long term care service providers have been implementing.**

The Solution – Purchasing Inflation Protection
Purchasing a policy with inflation protection reduces the risk that an adequate level of coverage today will become inadequate in the future.

Disadvantages of Inflation Protection
Higher cost is really the only disadvantage to purchasing a policy with inflation protection. This should come as no surprise to most consumers. If the insurance company has a growing responsibility they must charge more than a policy without a growing responsibility.

Advantages of Inflation Protection
If long term care expenses continue to grow at the same 5% compound rate and you purchase a policy with no inflation protection and you need long term care, your benefits are very likely to be inadequate. If you purchase a policy with Consumer Price Index (CPI) compound inflation protection and you need long care, your benefits are likely to be inadequate. If you purchase a policy with 3% compound inflation protection and you need long term care, your benefits are likely to be inadequate. **If you purchase a policy with 5% compound inflation protection and you need long term care, your benefits are very likely to be adequate.**

Let's look at an example of four policies with the same initial daily benefit and the same initial pool of money: one policy has no inflation protection, another has CPI compound inflation protection (with a 2% estimated growth rate), another has 3% compound inflation protection and another has 5% compound inflation protection. **Although they all begin with the same adequate level of coverage, only the 5% compound inflation protection policy grows at the same pace as the actual cost of care, as seen below.**

	5% Compound		None		CPI Compound at 2%		3% Compound		5% Compound	
Policy Year	Acutal Cost of Care Per Day	Total Cost of Care	Daily Maximum	Total Pool of Money	Daily Maximum	Total Pool of Money	Daily Maximum	Total Pool of Money	Daily Maximum	Total Pool of Money
1	$ 200	$ 219,000	$ 200	$ 219,000	$ 200	$ 219,000	$ 200	$ 219,000	$ 200	$ 219,000
5	$ 243	$ 266,196	$ 200	$ 219,000	$ 216	$ 237,053	$ 225	$ 246,486	$ 243	$ 266,196
10	$ 310	$ 339,741	$ 200	$ 219,000	$ 239	$ 261,725	$ 261	$ 285,745	$ 310	$ 339,741
15	$ 396	$ 433,605	$ 200	$ 219,000	$ 263	$ 288,966	$ 303	$ 331,257	$ 396	$ 433,605
20	$ 505	$ 553,402	$ 200	$ 219,000	$ 291	$ 319,042	$ 351	$ 384,018	$ 505	$ 553,402
25	**$ 645**	**$ 706,297**	$ 200	$ 219,000	$ 322	$ 352,248	$ 407	$ 445,182	**$ 645**	**$ 706,297**

Often Overlooked – Partnership Program and CPI Inflation
Most consumers must purchase a long term care insurance policy with inflation protection or the policy cannot be certified under the Partnership Program – the program that allows you to protect your assets away from Medicaid. Although the table above assumes a 2% compound growth rate as an estimate of CPI, actual CPI could be negative (as it has been in the recent past), zero, 1%, 2% or more than 2%. Some insurance companies that offer CPI inflation protection will not reduce your benefits even if CPI is actually negative. **With CPI inflation protection, your benefits may not keep up with the rising costs of long term care.**

Action Step – Protect Yourself with Inflation Protection
When you purchase a long term care insurance policy with inflation protection you protect yourself from the rising cost of long term care. Be sure your policy benefits increase as the cost of long term care increases or be prepared to spend significantly more out of your own pocket.

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