Building a comprehensive financial plan will be the best way to understand the impact that potential LTC costs could have on the longevity of your retirement assets. (UBS)

Long-term care costs and solutions

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Long-term care, typically in the form of home health aides, assisted living, and nursing homes, is a reality that many people plan for without knowing if they'll eventually need it. What considerations are involved? How can you plan for an unknowable future? We take a look at common concerns and share next steps to help you prepare for the possibilities.

How much will long-term care cost you?

Long-term care can be difficult to plan for because the actual level of expenses incurred is very uncertain. Anecdotally, we find that many investors either downplay the costs of LTC or exaggerate the likelihood of needing it. Those that downplay LTC tell us that they intend to stay healthy and avoid the expense.

Alternatively, we find that investors who have witnessed family members who experienced worst-case LTC outcomes assume that they will also need years of care that will deplete the majority of their estate.

In reality, although you are likely to need LTC services, you are unlikely to experience devastating LTC expenses. About 15% of female-male households will have no LTC expenses at all, and our analysis indicates that the median 65-year-old couple will incur a total of USD 273,504 in LTC expenses during their lifetimes. However, and this is a big however, roughly 33% of families will incur expenses of more than USD 500,000, and 14% of families will incur expenses greater than USD 1mn. Therein lies the challenge.

Self-funding the worst 25% of outcomes, which results in USD 0.75–4mn of expenses, is impractical for the vast majority of American households. The functional equivalent would be trying to self-fund rebuilding your house after a fire instead of holding insurance to cover the cost.

Does insurance help?

LTC insurance can help to reduce financial plan failures stemming from LTC expenses, but it isn't designed to protect investors against worst-case scenarios. Think about a typical insurance product like homeowner's insurance. The policy is generally set up so the purchaser of the policy is responsible for a small portion of the loss (known as the deductible), while the insurance company covers the remainder of the loss. If your house burns down, you might have a USD 10,000 deductible, but the insurance company would cover losses above that level.

Ideally, an LTC policy would also have a reasonable deductible and cover expenses above that amount. For instance, a household might choose a policy where they pay the first USD 10,000 of LTC expenses per year and the insurance company would cover any amount above that number. Such a policy would add a lot of certainty to planning. However, there are no LTC policies that use that structure. Instead, policies are generally structured with low or no deductibles and also with caps on annual and lifetime coverage.

In general, there are three types of LTC insurance policies that households can use to help hedge the risk of incurring LTC costs:

- **Traditional long-term care insurance policies** generally allow the purchaser to customize benefits (amount, period, inflation, deductible) based on their needs. Premiums are typically paid monthly, quarterly, semiannually, or annually. One significant and notable drawback is that premiums can be subject to rate increases.
- **Hybrid long-term care insurance policies** provide long-term care coverage and include a death benefit. The premium is commonly paid upfront in full, or in a series of fixed installments. If long-term care is never used, the beneficiary's estate usually receives a death benefit equal to the purchase price of the policy when the insured dies.
- **Permanent insurance policies** with a long-term care insurance rider focus on providing the insured individual with a larger death benefit as does a traditional life insurance policy. However, they also provide a small rider that covers long-term care expenses.

Conclusion

The uncertainty around future long-term care expenses can create financial fragility for some families in retirement and there's no single funding strategy that is going to be appropriate for every household.

While LTC insurance can help to address the uncertainty of costs, it isn't designed to protect families against worst-case scenarios. Self-insuring by using liquid assets to pay for LTC expenses provides you with more control of the assets and allows for growth potential if you choose to invest the funds, but it is impractical for most households to self-insure against the worst-case outcomes.

Building a comprehensive financial plan will be the best way to understand the impact that potential LTC costs could have on the longevity of your retirement assets, and it will help you to identify the most suitable funding strategy for your family's unique situation.

The Liquidity. Longevity. Legacy. framework is a helpful way to frame your funding strategy decision, as well as incorporate its impact on your investment strategy and financial plan.

In general, buying LTC insurance will allow you to have more confidence about the size and timing of outflows to meet your lifetime spending needs (the Liquidity strategy and the Longevity strategy). In turn, this can give you the ability and the confidence to set aside more funds in your Legacy strategy—assets that can be earmarked for needs that go beyond your own lifetime—where they can be invested in strategies that aim to maximize the growth of assets for inheritance or philanthropy.

Next steps

As a starting point for estimating the potential cost of your LTC needs, consider the following questions and discuss them with your family and your financial advisor:

- If you need care, would you prefer to remain in your home?
- If at home, who would provide the care?
- If care is needed, what resources would you use to cover the costs (e.g., self-funding, Health Savings Account, long-term care insurance, etc.)?

Read the report for more on how to prepare for long-term care **Modern Retirement Monthly: Long-term care costs and solutions** 25 October 2023.

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